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Since the introduction of its own Code of Corporate Governance in March 2000, Malaysia has made strides in improving its standards of corporate governance. Other key reforms followed suit, including the formulation of a ten-year master plan for capital markets in 2001 and the demutualization of the stock exchange Bursa Malaysia. Disclosure rules were also strengthened in 2004.

The establishment in 2008 of a corporate governance department, or corporate surveillance and investigation division, by Bursa Malaysia to implement and monitor corporate governance policies of listed companies has aligned Malaysia’s corporate governance practices closer to international best practices.

But significant challenges remain and more are needed to be done – to which the Securities Commission (SC) has commenced work on a new blueprint on corporate governance to chart a new course of action for the next five years to 2015. This is borne by the results of a recent survey by SC which show that a large number of companies have chosen merely to comply with form rather than substance of the regulations and best practices. The new blueprint will be comprehensive and forward-looking and includes strategic priorities from board governance to active shareholder participation.

Indeed, the recent global financial crisis has again brought to the fore the governance practices in various countries, including Malaysia. This came as fraud cases emerged out of the difficult financial crunch that the regulatory authorities have to take swift action to protect the integrity of the market and investment environment. The significant changes in the corporate landscape have made the adoption of the new corporate governance blueprint even more critical.

Malaysia, through the SC and Bursa Malaysia, has enhanced its surveillance mechanisms, resulting in the convictions of a number of rogue market participants and revocation of business licenses. With the state-of-the-art surveillance information system technology, Bursa Malaysia can act swiftly to curb any potential market misconduct, and fulfill its paramount priority of investor protection.

Aldrin Monsod
Publisher
Regulatory responses to the financial crisis: The view from Hong Kong

“Hong Kong has traditionally been the “gateway” for many Mainland Chinese enterprises seeking to access the international capital markets”

Introduction Good morning. It’s a pleasure to be here with you today. I’ve been asked to provide some thoughts on regulatory responses to the financial crisis and the various measures we have taken or are taking in Hong Kong. Having an externally-oriented economy and open securities and futures markets, Hong Kong has not escaped unscathed, although it has not been as hard hit as some markets. Despite the economic downturn, our financial sector has largely withstood the strains placed upon it. None of our banks has had to be bailed out. Neither has any of our brokers failed. During the height of the financial meltdown, when other major markets imposed bans or restrictions on short selling in their securities markets, we were able to stay our course. Still, Hong Kong has faced several of the same issues as other markets as a result of the crisis. Short-term emergency measures were taken to address frozen credit markets, provide liquidity and increase the protection provided for bank deposits. The crisis has highlighted several areas in which our regulatory regime needed to be strengthened. In addition to this, we, along with regulators around the world, continue to work to identify steps which should be taken to prevent or minimise the likelihood of future crises.

What I’d like to do today is look at some of the current regulatory matters relating to the securities and futures markets that have been identified at a global level and give you a Hong Kong perspective on these. These are, of course, my personal views and not necessarily those of the Securities and Futures Commission (SFC).

First, though, for those of you who aren’t very familiar with Hong Kong, perhaps I can provide a bit of general background.

Hong Kong – context
Hong Kong is a large banking and asset management centre. It also has a mature, open and active equity market. We are both part of China and its offshore financial centre, in short, an international, developed market within an emerging market. Hong Kong has traditionally been the “gateway” for many Mainland

Hong Kong will ensure that its regulation and standards meet international requirements.
Chinese enterprises seeking to access the international capital markets. In recent times, it has also played an increasing role in the evolution of the renminbi (RMB) into an international currency. Our banks have accepted RMB deposits since 2004. Since 2009, international trade settlements in RMB have been able to be transacted between Hong Kong and designated Chinese cities on the Mainland. In recent years there have been a good number of RMB bond issuances in Hong Kong, including a sovereign bond issuance last year. As Hong Kong continues to increase its capacity for RMB financial transactions and applies its considerable expertise to expanding the range of RMB-denominated investment products (such as RMB-denominated, traded and settled equity products), and in light of China’s overall strong growth prospects and the opportunities that the internationalisation of the RMB would bring about, Hong Kong has enjoyed strong incoming fund flows. The potential for RMB financial and investment products is enormous and will have major ramifications not only for Hong Kong but for all of us, as will the increasing number of Chinese investors, financial professionals and enterprises seeking investment and trade opportunities and financial services outside the Mainland of China. I note here that South Africa, of course, has increasing economic and diplomatic relations with China.

Global financial market reforms
While economists would point to 2007 as the time when the cracks perforated the fabric of calm in the world financial markets, it was the collapse of Lehman Brothers in September 2008 that brought immediate meltdown. While pumping massive amounts of public money into their banking and financial systems, governments around the world had to examine how and why existing regulation had failed and, with that, to put in train reforms to address the inability of national regulatory regimes to supervise financial markets and players that operate globally, but which impose a burden on national governments and taxpayers when they fail, and to resolve cross-border crises. These international efforts have been spearheaded by G20 leaders and co-ordinated by the Financial Stability Board (FSB), drawing on support from international standards-setters (such as the International Organization of Securities Commissions, the IOSCO) and the international financial institutions (such as the International Monetary Fund, the IMF). The focus is on systemic risks, macro-prudential regulation and international co-operation. The aim is to seek global solutions to minimise the recurrence of the problems. Having experienced first hand how inter-connected and correlated the world markets have become, world leaders understand that they have to create global tools which should be applied across markets and countries where necessary.

Concurrently with the global initiatives, individual countries are working on national laws to deal with their problems. In the US, market discipline and self-regulation, the brainchild of the 80’s and 90’s, has been so badly discredited that the pendulum has swung from deregulation to re-regulation. The Dodd-Frank Wall Street Reform and Consumer Protection Act, anticipated to be signed into law in the near future, will usher in a new paradigm of more intrusive regulation. Since the US is home to the largest number of systemically important global financial institutions and since these institutions are also present and operating in markets around the world, not just in Europe but also in Asia and Africa, the US legislation will influence the final shape of global reforms.

The EU is another major driver of financial reforms. The debt crisis has raised questions about EU solidarity in dealing with the problems, the sustainability of the Euro and even the longer term viability of the union. That individual member states are taking their own ad hoc measures to deal with the current debt crisis, such as bans on naked short selling, is not helping, as this raises the question of whether future actions will be co-ordinated. Meanwhile, some of the reforms proposed at the EU level have raised concerns about market entry barriers. The Alternative Investment Fund Managers Directive (AIFMD), for instance, has been criticised in some circles as creating “Fortress Europe”, or even “Prison Europe”.

Not every country has the same imperative for financial reform, or the exact same set of issues. However, because of the importance attached to global adherence to international standards, the pressure is on for all markets to comply or risk being marginalised. It is therefore vital that the standards that are set are reasonable, and don’t represent knee-jerk reactions to particular issues.

Being an international financial centre with open securities and futures markets, Hong Kong will ensure that its regulation and standards meet international requirements.

Within the global theatre of action, a number of areas are of particular relevance to the Hong Kong securities market. They include the regulation of credit rating agencies (CRAs) and of hedge fund managers, and investor protection. I will focus on these areas today.

Short selling restrictions, transparency
First, let me talk a little bit about the regulation of short selling as this issue took centre stage during the meltdown. Hong Kong was one of the few developed markets that did not impose emergency short selling regulations during September and the last quarter of 2008.

“World leaders understand that they have to create global tools which should be applied across markets and countries where necessary”
We have had an “uptick” rule since 1998; essentially, a short sale cannot be made below the best current ask price. Naked short selling is generally prohibited and covered short selling in Hong Kong may be executed only on the stock exchange’s trading system in designated securities.

Our uptick rule was introduced in the wake of the Asian financial crisis. As some of you may recall, in 1998 the Hong Kong Government intervened heavily in the stock market in response to speculative pressure on Hong Kong’s currency and abusive short selling of Hong Kong stocks. The short selling rules that were introduced in the wake of these events were quite controversial at the time, not least because a breach of the rules attracted criminal sanctions in addition to any penalties for failed settlements. The regime that we put in place was intended to endure for some time. In subsequent years there was a push in the market for us to relax the rules, but we did not do so, and events in September 2008 reaffirmed for us that the uptick rule should remain in place. In fact, events since September 2008 have vindicated the efforts we put in in 1998.

The financial crisis exposed the weaknesses and insufficiencies in the regulation of short selling in many jurisdictions. The IOSCO Technical Committee saw merits in having a common approach to the regulation of short selling across different markets – to reduce multiple compliance costs and to minimise any potential for regulatory arbitrage. One of the drivers was to require more reporting and disclosure. In Hong Kong, we conducted a public consultation on proposals to introduce a position reporting requirement. The obligation will be triggered once a short position reaches 0.02% of the issued share capital of the relevant issuer, or the value of the short position amounts to or exceeds HK$30 million (about ZAR29.6 million, or about US$3.85 million), whichever is lower. In setting the threshold we were mindful that substantial positions needed to be captured, but that the limit should not be set so low as to impose undue compliance burdens. We looked at thresholds in other markets, and also had regard to the characteristics of the local market (for example, we noted that ratio of short selling to turnover in Hong Kong appeared to be much lower than in London and New York, and that the ratio of short exposure to market capitalisation in Hong Kong is much lower than in New York). We took a risk-based approach in proposing an initial list of shares to be covered by the reporting regime, since our underlying objective in imposing these requirements was to facilitate identification of positions with the potential to affect market stability. We will retain the discretion to require more frequent reporting, to lower the applicable thresholds or require reporting of positions in additional shares should contingencies arise. We propose to publish the data collected, aggregated per stock and without identifying the short sellers, on a delayed basis.

I’d note here that we continue of course to monitor the short selling measures being considered and adopted in other parts of the world.

Credit rating agencies
Let me now turn to the regulation of credit rating agencies.

Credit rating agencies are not currently required to be registered or licensed in Hong Kong, and we do not specifically regulate the conditions for the issue of credit ratings. However, in light of the recommendations by the G20 and the Financial Stability Board, the IOSCO Principles and regulatory developments in other parts of the world, the Hong Kong Government has stated its intention to regulate this area.

The issuance of credit ratings is, of course, a global business. Issuers, rating firms and analysts, and the end-users of ratings could all be based in different places. Thus, the regulatory approach in this area needs to reflect this, and it’s important that the measures adopted in different markets are harmonised as much as possible.

Taking the EU as an example, under new regulations, credit ratings issued in third countries can be used in the EU for regulatory purposes only if they comply with regulatory requirements which are as stringent as those imposed in the EU. Credit rating agencies established in the EU may endorse credit ratings issued in third countries where conditions can be satisfied and where the activities resulting in the issuance of the credit ratings are undertaken in whole or in part by the endorsing agency or members of the same group. Alternatively, credit ratings issued by third parties without a presence or affiliation in the EU may be certified in certain circumstances. In these scenarios, there is a requirement that the relevant legal and supervisory framework in the third country is equivalent to or as stringent as that in the EU and that there be suitable co-operation arrangements in place between the relevant supervisory authorities.

These measures will affect credit rating agencies issuing ratings in Hong Kong to the extent that they are used in the EU for regulatory purposes. The transitional timeline for these third-country
requirements is very tight; provisions in this regard will apply from mid-2011.

For our part, we are working together with the Hong Kong Government on proposals for licensing and supervision of credit rating agencies issuing credit ratings in Hong Kong. The objective is to put in place a regime that meets international standards. Our proposals are largely based upon the Code of Conduct Fundamentals for Credit Rating Agencies issued by the IOSCO. Once finalised, they will be released for public consultation.

“Developments in Europe and in the US relating to regulation of hedge funds and their managers have huge implications for the international asset management industry and related sectors”

Hedge funds and hedge fund managers

Another, very important, area of focus globally is the asset management industry.

The regulation of collective investment schemes and fund managers in other parts of the world is something that has significant effects in Hong Kong. I mentioned before that Hong Kong is a large asset management centre. A large proportion of the funds managed by Hong Kong-based asset management professionals are not domiciled in Hong Kong. But asset managers carrying on business in Hong Kong are required to be licensed by us. In addition, if a fund is to be distributed to the public in Hong Kong, it must be authorized by us.

One of the current considerations in this area at the international level is regulation of certain alternative investment funds and/or the managers of these funds, both in terms of requirements for registration and operations and in terms of reporting and other transparency measures. Some of the measures being proposed target hedge funds in particular.

Hedge fund managers carrying on business in Hong Kong are subject to our regulatory regime and are required to be licensed. Once licensed, they are subject to our supervision. To improve the transparency of Hong Kong’s hedge fund industry, we have conducted surveys of Hong Kong-licensed hedge fund managers in recent years, and have published reports on the results. Together with other IOSCO members, we are also participating in the collection of information from hedge funds pursuant to the framework developed by the IOSCO to facilitate assessment of systemic risk. We have been carrying out joint inspections with the Securities and Exchange Commission (SEC) in the US and in Hong Kong of hedge fund managers who are both licensed in Hong Kong and registered with the SEC. Thus, while other jurisdictions are putting in place a licensing and supervision regime covering hedge fund managers, we already have regulatory supervision over those hedge fund managers who operate in Hong Kong. One of the areas of focus of the G20 and Financial Stability Board is on systemically important non-banks. We will follow the global regulatory developments in this area closely to ensure that our regime continues to meet international standards.

Developments in Europe and in the US relating to regulation of hedge funds and other alternative investment funds and their managers have huge implications for the international asset management industry and related sectors. Of particular concern are the proposed provisions in the AIFMD relating to the marketing in the EU, or sale to EU investors, of funds managed by non-EU managers or located in non-EU countries. Much has already been said about this aspect of the draft Directive, and its terms are still being debated, but it has the potential to restrict substantially the universe of these types of funds available to EU investors. In my view at least, this could be detrimental not just to the managers and funds concerned but also to the EU investor base.

International co-operation

All of this leads me to a point which has been raised many times recently— the importance of international co-ordination in considering and implementing regulatory measures. In calling for convergence or for consistency, however, we also need to set standards that are reasonable and that achieve the underlying objectives without imposing unduly high burdens or having unnecessary adverse effects.

Large, regulated firms are internationally active, operating through affiliates in many countries, and financial markets themselves are increasingly linked. We need to ensure that we minimise scope for arbitrage between different regulatory requirements and that data is able to be analysed at the appropriate level when assessing matters such as systemic risk.

The challenges here, of course, are numerous. Once regulatory “gaps” or imbalances are identified and measures are being considered to address them, we need to weigh up the “cost” or regulatory burden against the benefit sought, and determine the best way to achieve the main objective. We need to take into account not just universal but local and/or regional needs or market characteristics, and also the time-sensitivity of a given matter at issue. And obviously there will be issues and measures that have implications at a global level and others that by their nature have a more localised effect.

To deal with these challenges, I believe that it’s important for us to continue our efforts to identify the matters that have the potential to have widespread repercussions and develop sensible, effective and timely regulatory, supervisory and other financial sector policies within international forums.

Investor protection issues

I would like to spend some time talking about some investor protection issues that have arisen in Hong Kong. Investor protection is, of course, one of the general objectives underpinning the Principles
of Regulation developed by the IOSCO, and we’re not the only jurisdiction considering these sorts of matters.

For many investors in Hong Kong, the collapse of Lehman Brothers directly affected investments they had made in structured products linked to Lehman group entities, or where Lehman group entities were counterparties to transactions underpinning the products. We received tens of thousands of complaints from investors in respect of the sale of these products, and devoted huge amounts of time and resources to investigating them. The SFC has the power to revoke or suspend the licence or registration of an intermediary, or to impose a fine of up to HK$10 million per instance of misconduct, but we do not have power to compel an intermediary to pay compensation to a third party. In determining whether and what disciplinary action to take against a regulated person, however, we may take into account any actions that person has taken voluntarily to remedy or mitigate misconduct. Using these tools, we were able to reach agreement with various of the intermediaries who sold these products. The intermediaries made voluntary repurchase offers to qualifying investors and agreed to take steps to address complaints and enhance their systems and processes. So far, more than HK$5.6 billion has been paid to about 30,000 investors in Lehman-related products.

We conducted an extensive public consultation in 2009 on measures to strengthen investor protection. The proposals that were the subject of this consultation were broad-ranging, and many were aimed at addressing issues we had identified as a result of the complaints we had received. At the same time, we were mindful that any regulatory response needed to be measured. We sought to balance appropriate safeguards for investors with the need to avoid unduly stifling the market.

The “investor protection” proposals covered requirements both for the authorization of investment products for public sale in Hong Kong and in respect of the conduct of intermediaries.

On the product side, we set out additional requirements, particularly in the area of structured products. These covered things like eligibility of key product parties, minimum requirements for collateral and guarantees, specific measures addressing conflicts of interest and the need for functional independence between certain key parties (for example, a fund manager and a swap counterparty), and mandatory market-making for some products. In addition to a generally-applicable disclosure standard and detailed product-specific disclosure items, we introduced the requirement for a summary document setting out key features and risks for investors, as has been done in many other jurisdictions. The objective is to make it easier for investors to understand and compare different products. We added on-going disclosure obligations throughout the life of certain products.

“The objective is to make it easier for investors to understand and compare different products. We added on-going disclosure obligations throughout the life of certain products”

Concluding remarks
I’ll wrap up here, as we have covered quite a bit of ground. I hope that this has provided some insight into some of Hong Kong’s considerations in this area. And, since the actions of any of us can affect the others, I hope that it serves to highlight the importance of co-operation and consistency between countries and regions and the importance of measured responses as we work to address imbalances and improve the regulatory framework.

Regulatory responses to the financial crisis: The view from Hong Kong
Keynote Address Alexa Lam Executive Director and Deputy Chief Executive Officer Securities and Futures Commission 5 July 2010.
The Philippines: Creating opportunities through effective governance

"The country’s external debt profile continues to improve. Six years ago, our external debt-to-GDP ratio was around 70 percent. As of March 2010, this ratio was down to 33 percent."

Let me start with a review of the major reforms that the BSP has adopted in pursuit of its mandated responsibilities.

First, on monetary policy - the BSP has adopted the inflation targeting framework that has provided us with a disciplined approach to safeguarding price stability. The forward-looking perspective under the framework as well as the associated transparency and accountability practices have helped better anchor the inflation expectations of the markets and the public. This, in turn, has contributed to improved inflation management and to well-contained inflation dynamics.

Let us look at the numbers...

Stable food prices have helped temper inflation pressures, despite the occurrence of the El Niño phenomenon early this year. From January to July 2010, headline inflation fluctuated between 3.9 percent and 4.4 percent, staying within the Government's target range of 3.5-5.5 percent for 2010.

The benign inflation environment has given the BSP the flexibility to keep policy rates steady. With stable domestic financial conditions, the BSP also started a measured and paced unwinding of its accommodative monetary policy stance in the first half of the year.

Second, on external sector policy – the BSP adheres to a flexible exchange rate system and to an appropriately designed foreign exchange regulatory framework. The BSP also has in place an external debt management strategy that helps promote debt sustainability. As a result, we have seen the emergence of strong external payments dynamics, providing comfortable buffers against external shocks.

Reflecting these prudent external sector policies, the country’s balance of payments (BOP) position posted a surplus of US$3.2 billion in the first half of the year. The resilience of OF remittances and the sharp recovery of exports contributed largely to the country's favorable external payments dynamics.

The country’s external debt profile continues to improve. Six years ago, our external debt-to-GDP ratio was around 70 percent. As of March 2010, this ratio was down to 33 percent.

The long-dated maturity structure of our foreign currency debt, helps limit rollover and foreign exchange risks. The country's debt service burden as percent of GDP, which had previously hovered around 10 percent [2001-2003], eased to 6 percent as of March 2010.

International reserves have climbed to new highs, providing strong coverage for both imports and short-term external debt. At end-July 2010, the GIR stood at US$48.6 billion. At this level, the GIR can cover 9 months of imports and is equivalent to 9.3 times the country's short-term external debt based on original maturity and 5.1 times based on residual maturity, thus providing a strong cushion against external shocks.

As a result of the strong external liquidity position, the Philippine peso has remained broadly stable. The trends in the real effective exchange rate (REER) show that the peso has generally maintained its international competitiveness.

**Tetangco:** As a result of the strong external liquidity position, the Philippine peso has remained broadly stable.
over the last ten years. With generally lower inflation rates, the Philippine peso has accommodated some appreciation, but without undermining external price competitiveness.

Third, on financial sector policy – the BSP has put in place critical reforms geared toward maintaining a healthy banking system. The package of reforms includes the disposal of banks’ bad assets, the promotion of good corporate governance and transparency practices, and the upgrading of risk management standards. As a result, we have today an efficient, sound, and competitive financial system.

These critical reforms have been successful in steadily expanding and strengthening the banking system. Indicators of the health of the banking system continue to post favorable readings, with asset levels and bank earnings continuing to improve. The capital adequacy ratio remained high at 16 percent and non-performing loans also remained generally low at less than 4 percent of total loans.

The favorable performance of the domestic financial markets reflects the upturn in the country’s economic prospects. Thus, despite global market volatility following sovereign debt concerns in Europe and uncertainties regarding the depth and breadth of the global economic recovery, the spillovers on our domestic financial markets have been limited.

With continued improvements in domestic economic conditions and a broadly favorable global outlook, we foresee a firmer growth path for the Philippine economy in 2010.

Inflation is expected to stay within the target range of 3.5 to 5.5 percent for 2010. The outlook for the BOP position and the GIR level continues to be favorable, with the current account projected to remain in surplus.

While we expect the economy to continue to perform strongly, we remain conscious of the risks and challenges that lie ahead.

First is the multispeed recovery across the globe. Growth in emerging countries is outpacing growth in advanced economies. Given global interdependencies and linkages, this could result in sub-par global growth over the medium term.

Second, the potential heavy inflow of capital into the country, as risk appetites perk up, can lead to liquidity management problems which could pose inflationary risks.

Third, the rebound of the global economy could create upward pressures on commodity prices and fan inflation.

The BSP’s responses to these challenges are, as always, founded on its primary mandate of promoting monetary and financial stability.

In particular, our focus in the area of monetary policy will be on addressing the risks to price stability and re-examining policy settings when warranted.

On the external front, our priority is to promote policies that will help shield the economy against adverse shocks.

On the financial sector, the BSP will endeavor to maintain a well-functioning banking system that will efficiently mobilize funds and channel them to productive uses.

The BSP’s policy commitments, going forward, are supportive of the Government’s agenda of creating an enabling environment for durable, sustainable and inclusive growth and broad-based development, including through the pursuit of far-reaching and meaningful structural reforms and disciplined macroeconomic policies.

Ladies and gentlemen, the fundamental strengths of the Philippine economy, which saw us through a tough period, provide a huge opportunity for us to consolidate the gains we have achieved thus far and allow us to create an environment that will propel the economy forward.

The BSP, together with the other government agencies, are firmly committed to continue pursuing sound macroeconomic management and structural reforms to address the challenges ahead.

To this end, let us be guided by our shared commitment to serve the general good and by our common desire to make better things happen for the Philippines.

Governor Amando M. Tetangco, Jr. Philippine Mid-Year Economic Briefing August 18, 2010 speech in Manila
Strong recovery from the recession

The Singapore economy has recovered strongly from the recession. Five quarters since GDP reached a trough, Singapore’s output has exceeded its pre-crisis peak by 13.3%. The rapid climb from the trough can be traced to several inter-related factors. In particular, the domestic economy had been lifted by the cyclical upturn in global trade and financial market conditions since early 2009, supported by inventory restocking and unprecedented policy stimuli in the major economies. Given its openness and competitiveness, Singapore was in an especially strong position to benefit from these global forces through our externally-oriented sectors. In addition, investments made in the earlier years were completed in time to tap onto the global upturn. These investments introduced new activities in Singapore’s economic landscape, including high-end manufacturing and tourism services, and strengthened the competitiveness of our existing industries.
Global markets also recovered strongly after March as the financial system stabilised and investor confidence recovered. Taking into account translation effects stemming from the stronger Singapore dollar, interest and dividend income, as well as gains in the valuation of assets, MAS recorded a net profit of $10.12 billion during the financial year.

Looking forward, considerable risks remain in the global economy and the global financial system. Singapore’s financial system has, by and large, weathered the crisis well. However, we must not be complacent and we need to prepare ourselves to respond to any future challenges. There are three areas which MAS has been working on and which we will continue to focus on in the coming year: first, sustaining macroeconomic stability in the post-crisis period; second, strengthening the financial system; and third, maintaining the growth of Singapore’s financial services sector.

Sustaining macroeconomic stability in the post-crisis period

The strong pace of growth seen in the first half of this year is not expected to be sustained. Growth is likely to have peaked at the middle of this year, and will moderate to a more sustainable rate, as external demand slows after the post-crisis bounce from stimulus measures and inventory effects wane worldwide. For 2010 as a whole, the Singapore economy is expected to expand by 13 to 15%.

After two quarters in negative territory, headline inflation turned positive in Q1 this year and reached 3.1% in Q2. For the rest of the year, headline CPI inflation is expected to rise, reflecting higher car and commodity prices on a year-ago basis. However, the outlook for underlying price pressures remains largely unchanged from MAS’ monetary policy review in April. Despite stronger-than-expected GDP growth, the pass-through of domestic business costs to retail prices due to tightening factor markets is expected to be moderate, alongside the slowing in the economy. In part, domestic wage growth and other business costs could be temporarily tempered by the initial cyclical productivity uptick in some capital intensive sectors of the economy. For the year as a whole, headline CPI inflation is projected to average between 2.5% and 3.5%. MAS underlying inflation, which excludes the cost of accommodation and private road transport, will come in at around 2%.

When Singapore entered the recession in 2008, monetary policy, followed by fiscal policy, was eased to provide support to the domestic economy. As economic activity recovered swiftly in 2009, macroeconomic policy settings were recalibrated to levels which were conducive to sustainable growth and medium-term price stability. In a preemptive move, MAS tightened monetary policy in April 2010 by re-centring the S$NEER policy band upwards and restoring its modest and gradual appreciation path.

Looking ahead, the outlook of the industrialised economies remains uncertain. However, there is sufficient momentum from the Asian economies and domestic industries that will continue to support Singapore’s economic activity at a high level for the rest of the year. While CPI inflation is expected to pick up towards the latter part of the year, it has evolved broadly as anticipated during the April review. At this stage, we assess that the current monetary policy stance of a modest and gradual appreciation of the S$NEER policy band remains appropriate.

Strengthening the financial system

Singapore’s financial system remained resilient during the global crisis. In maintaining the soundness of the financial system in Singapore, MAS’ approach is centred on establishing sensible rules appropriate to our circumstances, strengthening prudential and market conduct supervision, and working in partnership with the industry to develop a shared ownership of supervisory outcomes.

This approach has served us well. As global reforms reshape the financial landscape, we will continue to strengthen our supervisory and regulatory regimes and market infrastructure, consistent with new international standards and best practices. As we have done in the past, we will calibrate these changes to take into account our environment and regulatory objectives.

MAS is supportive of global reform efforts to strengthen capital and liquidity frameworks. We have always considered capital adequacy and effectiveness of a bank’s risk management and capital planning processes as important parts of overall prudential management of banks. As a member of the Basel Committee on Banking Supervision, we participated actively in international discussions that helped shape the broad agreement reached earlier this week on the main design elements of the new capital and liquidity reform package. Other design details such as calibration, and phase-in arrangements as well as the framework for regulatory buffers will be determined later in the year. We would like to see a set of final proposals that can be implemented globally in a meaningful manner to promote the long term stability of the banking system. There should be a judicious balance between limiting banks’ activities that are incongruent to their role as an intermediary of financial flows, and allowing them to perform their role in fa-
cilitating economic activity and sustaining the recovery. MAS will continue to be actively involved at these discussions to shape the proposals.

Our Singapore banks start from relatively strong capital and liquidity positions. They are generally well-capitalised and have in practice maintained capital ratios much higher than our minimum requirements. As such, on a relative basis, we do not expect the proposals to affect them in a significant manner. Nevertheless, the global reforms will set new norms for the banking sector and the Singapore banks would have to take these into consideration in their capital and liquidity plans moving forward.

I mentioned last year that MAS will be reviewing the Corporate Governance Regulations and Guidelines for locally-incorporated banks and significant life insurers. We have since issued a public consultation paper setting out proposed enhancements to the Corporate Governance Framework for these financial institutions. The main thrusts of the proposals emphasise the need for directors to have the relevant skills and commitment to oversee the operations of the financial institutions, and the important role of independent directors on the Board. MAS will issue our response to the public consultation shortly.

On market conduct, MAS has issued two consultation papers on the sale of listed and unlisted investment products, to strengthen safeguards for retail customers and enhance MAS’ regulatory powers. We will be issuing our response to the feedback received in 2H2010. Proposals which do not require legislative amendments will be implemented first. Financial institutions will be expected to adopt the remaining proposals even before legislative implementation as good practice in conducting business with their customers.

MAS also issued the Guidelines on Fair Dealing last year. The Guidelines stress the responsibilities of the Board and Senior Management of financial institutions to set the corporate culture and direction to deliver fair dealing outcomes to customers. Over the last year, MAS has written to CEOs and Boards of major financial institutions to emphasise our expectations. We have noted increasing awareness among financial institutions of the importance of dealing fairly with customers. Going forward, MAS will continue to engage the Board and Senior Management of financial institutions, and assess their implementation of the Guidelines through off-site and on-site supervision. Financial institutions are also expected to conduct their own mystery shopping, while MAS’ mystery shopping exercise will serve as an independent check and benchmark practices across financial institutions.

In strengthening our regulatory and supervisory regimes, MAS will continue to maintain our balanced and consultative approach. We remain focused on achieving good regulatory outcomes that are appropriate to Singapore and seek to promote sustainable development of the financial sector.

Besides financial regulations, MAS is taking steps to strengthen the robustness of interbank funding markets. The financial crisis revealed the need to enhance banks’ management of liquidity. As the banking system grows, demand for high quality, liquid assets will grow. To address this, MAS will do two things.

First, we will increase the availability of liquid securities to banks by issuing short-term MAS bills as part of money market operations. Currently, we use three instruments in our money market operations - foreign exchange swaps, borrowings and repos. MAS Bills will be our fourth instrument. These bills are negotiable, so banks needing liquidity can sell them or pledge them as collateral in interbank repo markets as well as the MAS Standing Facility. This will facilitate banks in managing their liquidity.

We expect to commence issuing MAS Bills in 2Q 2011. To prevent overlapping with SGS T-bills, MAS bills will have tenors of up to 3 months. We will phase MAS Bills in gradually, with up to $20 billion initially, and then build up from there.

Second, we will continue to enhance the Standing Facility, which is the key liquidity facility for banks.

Last year, I announced that we would accept AAA-rated Singapore dollar debt securities issued by supranationals, sovereigns and sovereign-guaranteed companies. We also admitted these securities as Tier 2 liquid assets under Notice 613 with the same haircut as Singapore Government Securities. With immediate effect, we will extend the list of issuers to AAA-rated and zero risk-weighted public sector entities.
I also announced last year that we have established a cross-border collateral arrangement with De Nederlandsche Bank. This year, we have established such arrangements with the Banque de France, Bundesbank and Bank of England. These arrangements will allow banks in Singapore to pledge Euro and Sterling cash and eligible government securities, customised with these central banks, as collateral when they access the MAS Standing Facility.

These measures will help to broaden the availability and diversity of regulatory and liquid assets for banks and allow international banks greater flexibility to tap on their global sources of liquidity, while maintaining the high quality of eligible collateral of the Standing Facility.

**Maintaining the growth of Singapore’s financial services sector**

Let me now turn to the performance of our financial sector. The sector has staged a strong rebound as global financial conditions improved. In the first quarter of this year, the financial sector grew by 3.5%, its fourth straight quarter of expansion. More recent data such as bank lending suggests that the financial sector continued to expand in Q2. Meanwhile, hiring in the financial sector has picked up from 4,000 in Q4 2009 to 5,500 in Q1 this year. The 5,500 financial sector jobs created accounted for 15% of total job creation in Q1 2010.

The recovery in the financial sector is broad-based - banking intermediation, trading and asset management activities have all rebounded. In particular, financial assets managed by the Singapore asset management industry reached a new high in 2009. Total assets managed grew by 40% to reach $1.2 trillion (US$861 billion), exceeding the pre-crisis peak in 2007. Average daily trading volume of foreign exchange (FX) and FX derivatives have recovered to US$290 billion in April 2010, an increase of 11% from six months ago in October 2009 and near pre-crisis levels. We are also today one of Asia’s leading commodity derivatives trading centres.

The financial sector’s strong recovery is, in part, due to our strong fundamentals, as well as action taken by the industry. We will continue to take steps to ensure that the financial industry remains vibrant. One key lesson from this financial crisis is that we need to strengthen the nexus between the financial system and the real economy, to ensure efficient intermediation of capital to support growth and development.

The Singapore Exchange (SGX) implemented a series of measures to facilitate fund raising by listed companies in the midst of difficult external market conditions. Earlier this year, MAS and SGX introduced a concurrent review process for initial public offerings (IPOs) and a reduction in public exposure period for prospectus review from 14 days to 7 days. These steps to shorten the time-to-market would make Singapore a more attractive listing destination.

To give investors a broader range of investment products, MAS will continue to enhance individual investors’ access to debt capital markets, building on initiatives undertaken earlier for Singapore Government Securities. We worked with the industry to develop infrastructure for individual investors to participate in auctions of Singapore Government Securities and Treasury Bills via the ATMs of local banks, and to customise these investments together with their equity investments in the Central Depository. To promote secondary market trading for individual investors, MAS and SGX will work towards having an SGS trading platform by the first quarter of next year.

To promote bilateral trade and investment between Singapore and China, MAS and the People’s Bank of China announced the establishment of a $30 billion currency swap arrangement last week. We are working with our Chinese counterparts and banks to operationalise the swap line, and will announce details in due course.

The completion of the Marina Bay Financial Centre is timely as it provides the physical infrastructure for financial institutions as they gear up to take part in the next phase of Asia’s economic development. The industry has also continued to invest in talent even during the crisis, hiring over 800 graduates under the Finance Graduate Immersion Programme (FGIP) and the Finance Graduate Leadership Programme (FGLP). We will continue to work with the industry to invest in the development of talent and in deepening research.

**Conclusion**

Let me now conclude. While Singapore has made a strong recovery from the recession, considerable risks and policy challenges remain in the global economy and financial markets. MAS will continue to be vigilant and take appropriate steps to maintain medium-term price stability and enhance the resilience of our financial system. In strengthening our regulatory and supervisory regimes, we will do this in a manner which is consistent with international standards and best practices, but at the same time, sensitive to our environment and needs. Riding off Asia’s growth, we will also continue to build on our strong fundamentals to provide for sustainable growth in the financial sector.

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*Opening Remarks by Managing Director Heng Swee Keat at MAS Annual Report 2009/10 Press Conference, 29 July 2010*
Corporation governance – developments in the UK

Introduction
Recent turbulent events in the world's global financial markets triggered a series of major reviews of UK corporate governance which have resulted in a revised best practice code as well as a new stewardship code for institutional investors. This article takes a look at the key outcomes of these reviews and provides some perspective on how the new codes are expected to contribute to improvements in governance practice. It also considers how the governance debate is likely to evolve.

Impact of the crisis
Wind the clock back two years and the UK was in the thick of what has become known as the global financial crisis, despite the fact that some countries emerged virtually unscathed. Some of Britain's best known banks, such as the Royal Bank of Scotland (RBS) were on the verge of collapse and had to be rescued by the UK government. It is going to be some time before these banks return to private ownership.

It is no surprise that the then UK Prime Minister, Gordon Brown, ordered a review into corporate governance in the banking sector. Sir David Walker, an experienced banker with a stint at the Bank of England under his belt, conducted his review over the course of 2009, drawing in a wide range of opinions. His final report was published in November 2009 with 39 recommendations. These covered five broad areas as follow:

- Board size, composition and qualifications - for example, the time commitment of a non-executive director should be greater than has been normal in the past and should be at least 30-36 days per year.
- Functioning of the board and evaluation of performance. Walker laid particular emphasis on the behavioural aspects of governance, which we will see, have risen to particular prominence in the UK in the light of recent events. So non-executive directors are now expected to challenge executive proposals on strategy.
- The role of institutional shareholders

“A key question to address was whether corporate governance ‘failures’ during the crisis had in fact been confined to the banking sector – or whether there was a more widespread problem that needed to be addressed”
– Walker observed that institutional shareholders needed to take a far more active role in engaging with the companies in which they hold shares and to this end, recommended that there should be a best practice code relating to good stewardship.

Risk governance – Walker argued that banks needed to strengthen this by establishing a dedicated risk committee.

Remuneration – it goes without saying that bankers’ pay is an emotive topic and Walker made a number of recommendations covering issues such as disclosure, the need to link remuneration to the bank’s risk profile and the role of the remuneration committee.

So far so good. But what did all this mean for companies beyond the banking sector? Responsibility for the overall UK corporate governance regime is held by the Financial Reporting Council (FRC). It regularly reviews the UK code which has now evolved over the course of nearly twenty years. What drove the first best practice code (the so-called Cadbury Code) in 1992 was a series of corporate scandals such as the collapses of BCCI and Polly Peck. And since then, it is safe to say that further collapses or problems invariably provoke a further round of soul-searching.

So it is no surprise that the FRC was watching the Walker Review with great interest – and indeed, launched its own review shortly after Sir David Walker started work. A key question to address was whether corporate governance ‘failures’ during the crisis had in fact been confined to the banking sector – or whether there was a more widespread problem that needed to be addressed. There was real concern that there would be a ‘knee-jerk’ reaction to the crisis rather than a considered and measured response based on actual evidence. The general feeling was that, while UK companies were feeling the effects of economic recession, there was very little, if any, evidence of major corporate failures on account of poor governance. There was no doubt that the FRC would need to consider carefully the extent to which any Walker recommendations would need to be extended to the broader corporate sector.

The answer quickly became clear. The UK Combined Code and its predecessors were felt to have made a real difference to governance standards. And most commentators considered that at least some of the perceived shortcomings in governance in the banking sector were specific to that sector. There was also widespread recognition that the quality of corporate governance depends ultimately on behaviour not process and that there is a limit to the extent to which any regulatory framework can deliver good governance. The UK approach to governance, which is one of best practice principles rather than one reliant on legislation and regulation was also regarded as more flexible to changing circumstances and the different needs of companies. It became clear that the Walker recommendations would not be applied wholesale to the corporate sector, but only those that were appropriate - in particular, those relating to the role and behaviours of the board and the board’s responsibility for risk. The FRC also took on board the recommendation for a stewardship code for institutional investors.

Rather than overhauling the code completely, the FRC therefore looked to make improvements to the current code – and in particular, to ensure that it is the spirit rather than the letter of the code that prevails. The UK regime is based on the so-called ‘comply or explain’ principle which means that UK listed companies can deviate from the provisions of the code – but if they do, they must provide a considered explanation. This gives companies flexibility to, say, allow a chief executive to become chairman of the company if it makes sense to do so.

The new UK Corporate Governance Code

After a year of review and consultation, the FRC issued a revised UK Corporate Governance Code for listed companies in May 2010. It applies to accounting periods starting on or after 29 June 2010, so it will be some time before we actually see companies reporting on the new requirements.

Until this latest revision, the UK code was known as the Combined Code. This was one of those accidents of history that made sense at the time, but is no longer relevant. So the name of the code has been changed to the UK Corporate Governance Code.

The main changes are more about emphasising key messages and behaviours rather than adding a long list of new requirements. In some cases, this has meant significant structural changes to the code in terms of rearranging some of the sections. A key element of the new code is to emphasise the pivotal role of the chairman in ensuring good governance.

Nevertheless, there were two specific changes that have attracted particular comment:

• The annual re-election of all directors on the board – we look at this further below;

• Companies must now include explicitly the gender mix of the board as a factor in considering new board appointments. This reflects the view that greater diversity in the boardroom can improve the quality of decision-making and that explicit reference to gender would encourage cultural change in this regard.
Let’s now take a look at some of the other key highlights.

The new introductory sections really set the scene for the new code and are really important in understanding the philosophy behind how it works. Don’t be tempted to skip over them in the quest to read the actual principles and detailed provisions of the code! A new preface emphasises the need to follow the spirit of the code and the importance of improving the relationship between companies and their shareholders. This lays the ground for the introduction of the complementary UK Stewardship Code which is regarded as part of one piece with the UK Corporate Governance Code.

Company chairmen are also urged to report personally in their annual statements as to how the principles relating to the role and effectiveness of the board have been applied with the hope that this might address what has been dubbed the ‘fungus of boiler-plate governance reporting’.

An additional section clarifies the ‘comply or explain’ principle, in particular, the message that companies should feel free to depart from code provisions if they can achieve the principles of good governance in other ways.

The new code sets considerable store by the need for strong leadership. It clarifies that the board is responsible for the long-term success of the company. There is particular emphasis on the role of the chairman with the addition of a new principle that ‘the chairman is responsible for leadership of the board and ensuring its effectiveness on all aspects of its role’. Another new principle highlights that ‘non-executive directors should constructively challenge and help develop proposals on strategy’. This is designed to address a perceived weakness in board behaviour which led to disastrous strategies such as the RBS acquisition of the Dutch bank, ABN Amro.

Risk is now mentioned more explicitly in the code. Although the Walker Review recommended financial sector companies to have separate risk committees, the FRC did not consider it appropriate to extend this recommendation to all companies. Nevertheless, it was recognised that the board’s role in overseeing risk did need to be strengthened. What used to be known as the ‘internal control’ principle has now been renamed ‘risk management and internal control’. The principle has been revised to clarify that ‘the board is responsible for determining the nature and extent of the significant risks it is willing to take in achieving its strategic objectives’ and that the board should maintain a sound system of risk management and internal control.

This now addresses what the FRC considers to have been a significant omission from previous versions of the Code. As a follow-up action, the Turnbull Guidance which provides additional guidance on this section of the code, will be reviewed later in 2010.

And in terms of remuneration, performance-related pay should be designed to promote the long-term success of the company. There are a number of new provisions in the code. In essence, these provide further detail on how a company should apply the high-level principles of the code. However, it is important to recall that while we often talk about a new provision imposing new requirements, all the provisions are subject to ‘comply or explain’. This means that a company may choose not to comply with a specific provision, but it will need to give a reasoned explanation in its corporate governance report.

Here are the key new provisions:

- The chairman should agree and regularly review a personalised approach to training and development with each director.
- For larger companies, evaluation of the board should be externally facilitated at least every three years.
- Annual re-election of all directors - this has been the most controversial change in the code. Supporters of the change, which included a majority of institutional investors who responded, felt that it would promote better engagement between the board and shareholders. The argu
ment is that if boards are receptive to shareholder concerns, then the situation should not arise where the shareholders feel compelled to oust the board en masse at the annual general meeting. Those who argued against the change, such as listed companies, felt that it would lead to short-termism and create the potential to destabilise the board.

The FRC will monitor the impact of this revised provision as there are concerns about boards coming under pressure from shareholders to pursue the ‘latest fad’ when it may be in the company’s long-term interest to follow a more cautious strategy.

- The directors should include in the annual report an explanation of the basis on which the company generates or preserves value over the longer term (the business model) and the strategy for delivering the objectives of the company. This will help to ensure that boards think carefully about the long-term sustainability of the company.
- The board should satisfy itself that appropriate systems are in place to identify, evaluate and manage the significant risks faced by the company. This reinforces the more explicit inclusion of risk in the new code.
- The provisions relating to remuneration have been amended to clarify that payouts under incentive schemes should be subject to non-financial performance criteria where appropriate and compatible with the company’s risk policies and systems.

**The role of investors – the new UK Stewardship Code**

As touched on earlier, there have been concerns expressed about the quantity and effectiveness of engagement between institutional investors and company boards – particularly in the light of the financial crisis. The fact that UK share ownership is very widely dispersed and shares are held in some cases, for a matter of nanoseconds, has even led to the fear that some UK companies are, in effect, ‘ownerless corporations’.

The Walker Review made a number of recommendations relating to institutional investors. These included the proposal that the FRC’s remit should be extended to cover best practice in stewardship and that the FRC should ratify the existing Code on the Responsibilities of Institutional Investors (prepared by the Institutional Shareholders’ Committee). It should operate this code as a Stewardship Code on a ‘comply or explain’ basis and review it on a regular basis.

As a consequence of this recommendation and subsequent consultation, the FRC issued a UK Stewardship Code in July 2010. The FRC sees this code as complementary to the UK Corporate Governance Code because it can help to strengthen the link between governance and the investment process and so help to lend greater substance to the ‘comply or explain’ concept.

The code comprises seven broad principles, supported by guidance. These cover issues such as disclosure of governance, collective engagement and reporting on stewardship and voting activities.

The code is addressed in the first instance to those firms who manage assets on behalf of institutional investors. However, the FRC is also hoping that foreign investors will commit to the code. Given that they are believed to own around half of all UK shares, their more active engagement could have a significant impact.

The question is therefore whether the code will prove to be effective. However, supporters feel that it is a step, even if only a small one, in the right direction and sends out a clear message that the UK is committed to the highest standards of good governance throughout the investment chain. Nevertheless, the FRC is likely to face a significant challenge in achieving comprehensive take-up of the code.

**Where next for governance?**

Good governance is a journey, so the debate will continue to evolve. The UK is built a reputation as a world leader in governance development over a number of years, so these new codes will be keenly studied across the world.

CIMA has long taken an active interest in governance development. From our perspective, management accountants have a vital role to play in providing high-quality financial and other information, covering strategy, performance, risks and opportunities to the decision makers at executive and board level. We have welcomed the new code as a considered and measured response to the governance challenges posed by the global financial crisis and we are hopeful that they will contribute to continuing improvements in corporate governance.

Ultimately we believe that the effectiveness of the code should be judged against whether the following desirable outcome is achieved: Boards should be focused on the long-term sustainability of their business. They should be confident that their business models will deliver this – with appropriate risk mitigations as necessary – and that performance indicators and incentives reinforce the desired behaviours.

So we particularly welcome the emphasis on long-term success in the new code.

CIMA’s boardroom leadership model shows all the key ingredients needed to restore boardroom leadership and clarifies that both behavioural and pro-
cess issues are important. We believe that the new UK Corporate Governance Code has successfully captured the spirit of this model.

We think that it would now be useful to attention to focus on case studies which would provide examples of best practice and answer the question ‘what does good governance look like?’ CIMA is involved in a number of governance projects to develop further best practice on such issues as governance reporting and the board’s role in strategy. In addition, the FRC has commissioned additional guidance on implementing the code. This will be published at the end of 2010 under the title Improving board effectiveness.

It is absolutely essential that the board is connected effectively to the business in terms of delivering successful performance as we are of the view that it was a lack of such connectivity that contributed to some of the recent corporate failures – this is an area that we will continue to focus on. Other key areas are:

- The ethical and sustainable dimension of business and how this can be fully embedded.
- Learning from governance practices across the world. CIMA has been comparing Western and Asian governance practices as part of its work for the World Congress of Accountants in Malaysia in November 2010 and we believe that there are valuable lessons to be learnt.

So the governance journey continues. But as Stephen Green, Chairman of HSBC pointed out at a recent lecture co-hosted by CIMA, the key challenge is to keep learning lessons and to find a way forward. And although regulation is necessary, it is not sufficient. It is simply not possible to devise rules to create good behaviour. Boards therefore have a particular responsibility to model the right ‘tone from the top’ and to demonstrate ethical leadership with a clear understanding of the company’s purpose.

For more background about the UK Corporate Governance Code and the Stewardship Code, take a look at the FRC’s website at www.frc.org.uk.

CIMA has produced a number of publications on governance. Some of these are listed below.

- Corporate governance – developments in the UK, 2010
- Enterprise governance – restoring boardroom leadership, 2010
- Incorporating ethics into strategy: developing sustainable business models, 2010
- Executive bonus schemes and their alignment with business sustainability, 2010
- Report Leadership – tomorrow’s reporting today (with PricewaterhouseCoopers and the communications consultancy, Radley Yeldar), 2006

All are available from www.cimaglobal.com/resources

By Gillian Lees, Enterprise Governance Specialist, CIMA
CG momentum in Asia slows in recent crisis years

“The investor relations function of a company has evolved and the IRO has become indispensable in safeguarding the company’s most critical and intangible asset”

CLSA Asia-Pacific Markets (‘CLSA’), Asia’s leading, independent brokerage and investment group, has released its Corporate Governance (CG) Watch 2010, the 8th survey of corporate governance in Asia since 2000. Produced in collaboration with the Asian Corporate Governance Association (ACGA), the report examines 580 Asia-listed companies and 11 countries, including Japan, to produce the most comprehensive assessment of corporate governance performance, issues and trends in Asia.

The report title ‘Stray not into perdition’, suggests that while corporate governance (‘CG’) standards have improved in Asia over the past decade, even the top performing markets remain far from international best practice. Regulators make it too easy for companies to box-tick and markets still lack effective rules on fundamentals such as independent directors and audit committees. Meanwhile, most institutional investors are yet to invest sufficiently in voting, engagement or stewardship.

Commenting on the overall findings, CLSA Head of Thematic Research, Amar Gill said: “The 2008 global financial crisis was a wasted opportunity. Rather than using it to push reform forward, most governments have taken a complacent view, happy that the crisis this time did not start in Asia. Not enough has been invested to make best practices work and the negative trends we see may lead to a build-up of governance risk for the coming years.”

“The structures and processes of good CG may not obviously boost the performance of a business, but without them investors face the risk that the economic value created may be hijacked. In the worst case scenario, lack of CG demolishes a stock. Now with a CG score in place, investors have the opportunity to reduce risk and achieve higher returns by avoiding the worst CG companies,” said Gill.

The overall analysis of companies shows that large-caps tend to have better CG scores. Corporations were reviewed in relation to discipline, transparency, independence, accountability, responsibility and fairness. In addition, environmental practice was surveyed to provide the CLSA Clean & Green (‘C&G’) score and for the first time, Corporate Social Responsibility (‘CSR’) activities were also assessed.

Asia now accounts for more than 20% of global CSR reports versus just 12% five years ago. Even Chinese companies are encouraged to publish CSR reports to improve the country’s branding and competitiveness. CLSA Head of Sustainable Research, Simon Powell said: “We find that overall, more stringent environmental laws have been implemented in the region. However, many companies mix up contributing to charities as CSR, which is no substitute to proactively engaging with society for better outcomes.”

Among the country rankings, Singapore replaces Hong Kong at the top in 2010 while Thailand, Japan and Indonesia stand out this year as they were often seen as underperforming in the past. Malaysia and China also deserve merits whose scores rose by three and four percentage points. The Philippines, Indonesia and Korea are at the bottom of the market rankings, with The Philippines coming last.

Author of the CG Watch 2010 country analysis, Secretary General of the ACGA Jamie Allen said: “The reality is that most Asian markets are starting to lag behind global standards. The private sector has to undertake governance reforms proactively and see this as in their own self-interest. Markets that do this well will likely sustain their regulatory reforms more effectively and efficiently.”

The ACGA assessed 11 markets across Asia, asking 90 questions in four categories: CG rules and practices; enforcement; political and regulatory environment; accounting and auditing.
Corporate governance in Malaysia

Malaysia has made strides in improving its standards of corporate governance, but more are needed to be done to bring them at par with the international practices.
Evolution of corporate governance in Malaysia

The Asian financial crisis in 1997-1998 was a watershed for corporate governance in Malaysia. It galvanized the country’s efforts to reform and improve its corporate governance practices that included the introduction of a Code of Corporate Governance (Code) in March 2000, the formulation of a ten-year master plan for capital markets in 2001, the demutualization of the stock exchange Bursa Malaysia, and the changes in the composition and the role of the board of directors.

Compliance with the Code is not mandatory. However, the listed companies are required under the listing requirements of Bursa Malaysia to include in their annual reports a narrative account of how they have applied the principles and best practices set out in the Code, and to identify and provide reasons for areas of non-compliance, together with alternative practices adopted, if any.

In line with the Budget 2008, the revised Code contains key amendments aimed at strengthening the roles and responsibilities of the board of directors and audit committee, and ensuring that they discharge their duties effectively.

In particular, the revised Code spells out the eligibility criteria for the appointment of directors, the composition of the board and the role of the nominating committee. Independent non-executive directors are expected to provide a more meaningful and independent oversight function.

The nominating committee, in their role as the gatekeeper for a director’s appointment and reappointment, are expected to evaluate the professionalism and integrity of a proposed director, in addition to ensuring the basic requirements that he/she possesses the necessary skills, knowledge, expertise and experience to discharge his/her duties and responsibilities as a member of the board of directors.

To ensure that the audit committee serves as an effective check on the management of a company, the revised Code details the composition of the audit committee, the frequency of meetings and the need for audit committee members to attend continuous training to keep abreast with the developments in relevant financial and other related developments. In addition, the executive directors will no longer be allowed to become members of an audit committee in order to preserve the independence of the committee.

The efforts and the ensuing reforms were laudable but weaknesses remain, including the government’s high level of equity ownership, low free float, weak protection of minority shareholders and lack of directors’ accountability. In 2007, the government adopted the Capital Markets and Services Act to strengthen the regulatory framework for capital markets and to boost investor protection. In the following year, Bursa Malaysia provided a much-needed shot in the arm when it established a corporate governance department to implement and monitor corporate governance policies of listed companies. In addition, a government-related watchdog group, the Minority Shareowners Watchdog Group, was established as part of the reform process in order to improve the shareholder engagement process.

The key responsibilities of Bursa Malaysia’s corporate governance department are as follows:

- Formulate short, medium and long-term corporate governance policies to achieve high standards of governance practices and to elevate the country’s corporate governance rating at the international level
- Strategize and implement appropriate measures to enhance the standards of corporate governance among the listed issuers
- Lead all corporate governance-related initiatives across divisions of Bursa Malaysia to achieve high standards of governance
• Monitor the standards of corporate governance, review existing plans and execute changes to raise their standards

The legislative and regulatory framework for corporate governance in Malaysia is primarily contained in the Securities Industry Act and the Securities Commission (SC) Act. In addition, the Companies Act of 1965 empowers the Malaysian shareholders to participate in company meetings and shareholder ballots. The Companies Act also allows shareholders to remove board members at any time during their term of office.

Indeed, Malaysia has made strides in improving its standards of corporate governance, but more are needed to be done to bring them at par with the international practices. This year, the SC has commenced work on a new blueprint on corporate governance to map out a new course of action for the next five years to 2015. The blueprint will be comprehensive and forward-looking and encompasses strategic priorities from board governance to active shareholder participation.

The SC has put together a high level committee – the International Corporate Governance Consultative Committee – which will provide strategic direction, views and advice on key areas and policy recommendations towards the formulation of the blueprint, which will outline various initiatives to be implemented during the five-year period.

The committee comprises 11 senior industry participants and experienced professionals from Malaysia and overseas. They include Dr Wan Abdul Aziz bin Wan Abdullah, secretary-general of the Ministry of Finance; Tun Mohamed Dzaidin Abdullah, chairman of Bursa Malaysia; Tan Sri Azlan Zainol, CEO of Employees Provident Fund; Nazir Razak, group managing director and CEO of CIMB Group; Dato Johan Raslan, executive chairman of Price-waterhouseCoopers Malaysia; Tan Sri Megat Najmuddin Khas, president of Federation of Public Listed Companies Malaysia; Dato Azmi Ariffin, CEO of Companies Commission of Malaysia; Charnchai Charuvast, president and CEO of Thai Institute of Director Association; Fiana Jesover, senior policy manager, corporate governance for Organization for Economic Cooperation and Development (OECD); and Peter Elston, strategist at Aberdeen Asset Management Asia. SC chairman Tan Sri Zarina Anwar acts as the chair of the committee.

The committee is being supported by the corporate governance working group, consisting of senior regulators and market professionals. In addition, the SC will also be consulting other relevant stakeholders and industry groups in the adoption of the new corporate governance blueprint.

The development of the new blueprint is critical given the significant changes in the corporate landscape as well as new corporate governance-related issues that have emerged in Malaysia and globally.

As the frontline agencies on corporate governance issues, SC and Bursa Malaysia have joined hands to further promote good corporate governance practices among public listed companies through the holding of Corporate Governance Week, which started in 2009. This event provides a major platform for regulators and capital markets practitioners to deliberate on various key corporate governance issues such as the evolving roles of the board of directors, effectiveness of independent directors, quality of the boardroom, board oversight over management and risk management.

As SC points out, the participation of regulators, key market institutions and professional associations in the CG week underscores the continuing need for collaborative efforts to strengthen the country’s corporate governance standards. Recent developments, as exemplified in the global financial crisis, have again brought to the fore issues such as board accountabilities as well as the role of advisers, auditors and other professionals.

Corporate governance is paramount to listed companies and the broader economic development. This is even more important at the present time as stakeholders and investors demand company directors to be more transparent, practice sound governance practices and not merely pay lip service to compliance statements.

In another collaborative effort, the SC and Bursa Malaysia also hosted in May this year the working group meeting of the OECD Asian Roundtable on Corporate Governance (ARCG) in Kuala Lumpur. The senior policy makers and market practitioners from various Asian countries, multilateral agencies and regional associations tackled strategies in developing a new roadmap for Asia’s corporate governance landscape. They also reviewed existing efforts in corporate governance in the region since the establishment of the ARCG in 1999.

At the top of the SC corporate governance agenda this year is to get the directors of the listed companies to comply with the substance rather than just the form of the Code. One of its priorities, therefore, is the focus on improving the quality of the boards as an avenue to strengthen the practice of corporate governance. It will undertake extensive discussions with the boards of selected public listed companies to discuss the SC’s concerns on corporate governance issues.

Such concerns came about from a study undertaken by SC, which showed that a significant number of listed companies had independent directors who were related with each other. Doubts over their true independence was also raised as the study found out that half of the independent directors had sat on the boards for more than nine years. In fact, some 20 companies had independent directors who had tenures of more than 30 years.
Independent directors are tasked to play a significant role in upholding governance and a lot of attention had been called lately to improving the quality and enlarging the pool of independent directors to mitigate the concerns. Another issue is serving on multiple boards, which reduces their focus and attention that should be given for each individual company. In many cases, they also fail to exercise their independence which should be demonstrated by challenging or participating in the board deliberations.

Others issues include the relationship between the chairman and the CEO, as well as the sizeable number of executive directors found in some boards. The most ideal setup is the separation of the role of the chairman and the CEO to better serve their shareholders and other stakeholders.

The SC will be working closely with the Minority Shareholders Watchdog Group and the Malaysian Alliance of Corporate Directors to explore ways to centralize and populate the repository of competent and qualified people who can serve as directors.

Elsewhere, Malaysia has recorded improvements in terms of rule enforcement as both SC and Bursa Malaysia have been putting more resources in their investigation and enforcement units in the past few years. But while the market applauds the efforts of the regulators in bringing cases against the offenders, they need to register meaningful achievement in prosecuting insider trading and other market manipulating cases.

In July this year, the SC revoked the license of SJ Asset Management (SJAM) to undertake fund management activities. The move came after the SC found that SJAM breached regulatory requirements in relation to the safeguarding of clients’ assets and the company had engaged in deceitful and improper business practices.

The SC also found that SJAM had furnished false and misleading information and documents to the regulator. It has issued various guidelines and circulars on conduct expected of asset management firms and all firms are reminded to ensure strict compliance.

In another case earlier this year, the Kuala Lumpur Sessions Court has convicted a former managing director of a company for submitting false statements to the SC as part of the application for an initial public offering (IPO). While the listing did not materialize, SC stressed that the person had known of the false figures at the time the information was submitted and that was a serious breach of law.

The SC urged the court to impose a deterrent sentence as the false information had resulted in the SC being misled into approving the listing proposal based on the inflated revenue and profit figures. It called upon the directors who attest to the accuracy of information submitted to the SC, for purposes of listing, to take their obligations under the law very seriously as the veracity of such information is critical to the process of fund raising.

Bursa Malaysia, on the other hand, is closely monitoring the trading activities on a real time basis using state-of-the-art surveillance information system technology. The surveillance system is able to detect a wide range of possible market misconduct situations on real-time basis. It laid down clear and comprehensive rules and guidance on types of trading violations, enabling Bursa Malaysia to act swiftly to curb any potential market misconduct. For them, investor protection is the main priority.

In another joint initiative, SC and Bursa Malaysia put forward two more consultation papers in July this year. One of them is looking at proposals designed to enhance the continuing disclosure and financial reporting obligations of the listed companies, enhance corporate governance requirements and review the framework of share schemes for employees.

The second consultation looks at the proposal by Bursa Malaysia to issue a corporate disclosure guide that could clarify and illustrate how the requirements should be applied in practice. As Bursa Malaysia points out, it sets the best practices for establishing internal policies and procedures to enable listed companies to fulfill their disclosure obligations. ■
Governance in The Boardroom

“The view of outright disbelief that corporate governance practices, as we know them in listing requirements for public listed companies, is of any good to the organisation”

Board performance can make or break a company. It is therefore important to know if Board members believe in the Regulators mantra that it should be getting the right balance of skills. That putting in place the right procedures and processes, practicing constructive disagreement, protecting the environment and such would be in the interests of the organization.

This is the arena of business, the cat eat cat, dog eat dog and diamond cut diamond world. Only the toughest survive. This is where we talk about profit maximisation and me mine and I.

Governance in the Boardroom is not about espousing management theories on how leaders should get into trenches with their people and how good you should be at filling up forms, ticking boxes and meeting the Regulators dateline.

This view says that governance is about how Board members can conduct, protect and expand the business. It is about building business empires.

How did talk arise about philanthropy, environment, employee share option schemes, board evaluation?! That must be a private enterprise, not within the scrutiny of investors, regulators and Marx and Friedrich Engels on how wealth is created before talking again about how Boards can govern corporations involved in its creation.

Karl Marx spoke of surplus value and argued that it is unpaid surplus labour performed by the worker for the capitalist, and that this surplus-value is the primary basis for capital accumulation.

Friedrich Engels a german 19th century social scientist [1820 – 1895] had questioned cynically:

“Whence comes this surplus-value? It cannot come either from the buyer buying the commodities under their value, or from the seller selling them above their value.

For in both cases the gains and the losses of each individual cancel each other, as each individual is in turn buyer and seller.

Nor can it come from cheating, for though cheating can enrich one person at the expense of another, it cannot increase the total sum possessed by both, and therefore cannot augment the sum of the values in circulation.

If this problem must be solved, and it must be solved in a purely economic way, excluding all cheating and the intervention of any force — the problem being: how is it possible constantly to sell dearer than one has bought, even on the hypothesis that equal values are always exchanged for equal values?”

Engel’s probing analysis is disturbing. What he is saying is how can we increase surplus value if we “exchange equal values for equal values” and “exclude cheating”?

Does it explain then why in an unspoken way, cheating is preferred
amongst some? Until the Regulators came in, of course, to be the real spoil sports, made cheating illegal and punishable by imprisonment and heavy penalties. Of course most of us know that Regulators intervened because cheating, increasing one’s wealth at the expense of another by fraudulent means, cause widespread pain and misery which is not good for anybody.

What then is good corporate governance [CG] in wealth creation and how can Boards ensure it?

Is governance good when a corporation is compliant with the regulatory requirement? Or is it “good” only when it is producing “desirable” outcomes? If it is the latter, what then are these outcomes?

If these outcomes can be defined, then Boards can better focus their role on the outcomes and more readily commit to performance for this outcome.

It is perhaps because many don’t know about what is the “good” outcome of governance that Boards swim around regulatory requirements, paying it lip service. The irony being that perhaps the regulatory requirement itself was conceived without understanding the real meaning of good corporate governance making some of these requirements stiffer to genuine businesses everywhere.

So we have the terrible consequence of how on the one hand, the regulatory requirements stifle genuine businesses, whilst on the other hand is ineffective in preventing further corporate failures which has in recent years increased in numbers, in size and even in glamour. Many think that the Nick Leesons and Bernard Madoffs of this world rather glamorous not to mention those highly paid CEOs who presided over the titanic subprime failures!

Let’s get back to the definition of good corporate governance. I personally believe that in its fullness “good” outcomes are too large to be defined. Nevertheless, let me attempt the impossible.

“Regulators should offer a model definition of what good governance means so that it can bring this conversation forward”

A corporation can be said to practice good governance or be well governed only when it has in place a system of governance that can ensure the continuous well being of shareholders who in turn have a willingness to expand its circle of stakeholders.

For that outcome to happen, Boards should have the ability to pursue wealth, to protect it and to multiply it.

This would mean it must put in place whatever is necessary for both defensive and active competition: the human resources, the business network, the technology, the brand management framework, the risk management template, the internal harmony the strategic alliances the internal audit the right talent mix, even the right core values in the Board to quote a few – without the need for a Regulator to say so.

Boards should also have the honest intention to pursue this wealth in compliance with local regulatory requirements, its interest being to create wealth with legitimate means.

And Boards should also have the conviction of core values that will manifest itself in business policies and practices as in its willingness to expand its circle of stakeholders for a share of its surplus value.

Each Board should therefore be asked to define for itself, the values that have meaning to them and the meaning of good governance for its organisation. This exercise will help them to pause and reshape its business practices, policies and habits giving governance a real connectivity between theory and implementation, between form and substance.

Regulators should offer a model definition of what good governance means so that it can bring this conversation forward. The Regulator being the best educator should provide this “wholesome” education of values and business.

Perhaps a Greed Mitigation Program GMP can be put in place for directors.

A program that will speak of life, its needs and its sufficiencies, as much as teach case law on the consequences of greed and share success stories of companies who grow legitimate businesses. And share experience of how surplus value have been used for the common good of the environment in which we each live and work and play. GMP could also be taught in business schools, to start education at the cradle.

Greed is most unnecessary if we believe Milton Friedman [1912 – 2006] when he alluded to a wrong belief system – “ a belief in the fallacy that there is a fixed pie, that one party can gain only at the expense of another”. This fallacy creates a sense of desperation, a need to grab. It brings out all that is terrible and ugly in the organisation. Regulators could make a point to correct this fallacy to help increase good corporate governance.

Apart from lack of education, there are two other causes of failure - firstly the UGLINESS in organisations and then what I call the “Triple A” culture. UGLINESS, to me stands for fraud negligence recklessness.

A fraudulent Board never meant to fail but sometimes its action is caught by factors beyond its control. The corporation fails. Some observe that failure here is “an act of God”.

Other times, a Board can be negligent, preferring to use lower paid employees or specialist resources who could not perform the level of diligence, analysis and wisdom required. The corporation fails. Failure here is from “an act of silliness”.

Yet other times a Board is besei-
ged by recklessness, a stirring in the gut to be brave without regard to the risks. They just plunge for that “acquisition, diversification, investment or scheme”. The corporation fails. But recklessness could be due to hormonal imbalance... so failure here is from “an act of nature”.

Meanwhile, the triple A of corporate failure is affluence and arrogance addiction.

These are people who probably have empathy for others who want large pay packets, who aspire to be affluent and arrogant like them. They understand the people’s addiction to affluence and arrogance.

As Board members, triple A types [the affluent, the arrogant and the addicted] willingly approve golden goodbyes. It must be them. How else do we explain how Bob Mendlessohn, former CE of insurers Royal and SunAlliance received 1.4m GBP presiding over a 90% fall in share prices or the case of Robert Nardelli, ex CEO of Home Depot who was awarded $210 m for being booted out of the top job. The contract was signed 6 years before his exit.

As professionals, Regulators and public guardians, triple A types stress a soft refined language: the combined code of corporate governance, which essentially took up 48 out of 50 of the recommendations of the Higgs Report 2003 [Derek Higgs], attempted to manage the matter of golden goodbyes by calling on companies “to avoid rewarding poor performance” and “take a robust line on reducing compensation to reflect departing directors’ obligations to mitigate loss”.

Certainly a very soft and civilised language which of course had little effect in preventing the subprime ceos from receiving their hefty golden goodbyes.

Given the presence of such UGLINESS & the triple A types, what else can be done to prevent corporate failures?

On 28 May 2010, the Financial Reporting Council (FRC) in the UK published the final version of the UK Corporate Governance Code which replaces the Combined Code. The new Code applies to accounting periods beginning on or after June 29, 2010. In the new Code, the FRC focused on a change of ‘tone’ to encourage a greater emphasis of BOARDROOM behavior.
Four new Principles in the Code now requires the following:

- The chairman’s responsibility for leading the board;
- The non-executive directors’ role in challenging and developing strategy;
- Boards to have a balance of skills, experience, independence and knowledge of the company; and
- Directors to have sufficient time to discharge their responsibilities effectively.

In addition, the following new features were added:

- To improve risk management, the company’s business model should be explained and the board should be responsible for determining the nature and extent of the significant risks it is willing to take;
- Performance-related pay should be aligned to the long-term interests of the company and its risk policy and systems;
- To increase accountability, all directors of FTSE 350 (large companies) companies should be put forward for re-election every year.
- To encourage boards to be well balanced and avoid “group think” there are new principles on the composition and selection of the board, including the need to appoint members on merit, against objective criteria, and with due regard for the benefits of diversity, including gender diversity.
- To help enhance the board’s performance and awareness of its strengths and weaknesses, the chairman should hold regular development reviews with each director and FTSE 350 companies should have externally facilitated board effectiveness reviews at least every three years.

At the end of the day, all we need are “neds who are the voice of dissent. Their most important role is to ask rigorous questions while understanding the business issues and sharing ethical values.”① [Jan Fiona Cumming director article 13].

"Investors who pursued a value strategy and invested in undervalued or stable companies were willing to pay for good governance"

Reassuringly, a survey carried out many years back, found that investors pursuing a growth strategy did not worry about corporate governance, while investors who pursued a value strategy and invested in undervalued or stable companies were willing to pay for good governance (Agrawal et al., 1996 as cited by Kakabadse et al., 2001)

There are investors who hold the belief that a company with good governance will perform better over time and/or that good governance can reduce risk and attract further investment. Also they insist that good corporate governance, can apparently serve as a tool for attracting certain types of investors as well as influencing what will be paid for stock; the average premium which investors are willing to pay for good governance being between 11 and 16 per cent.

Regulators will do what they have to do. Investors will prefer what they want to prefer.

Boards have to make sure the failures do not come to their doorstep.

For that perhaps this 8 point CG guide will be helpful:

- define for our organisation what values are meaningful to us, the meaning of good corporate governance - is it in our willingness to invite others to our banquet – admit stakeholders?
- make sure people resources and systems are aligned to our definition of good corporate governance to give it meaning and to make the definition work.
- do not be $ driven by saving every penny, pay generous [as distinct from “ridiculous”] remuneration packages or professional fees if it will get the best people to work for the organisation.
- in addition to using a skill matrix, compose the Board by a value matrix. Leave the prima donnas and such out side.
- keep the person(s) who demonstrate the talents and values you have adopted. Don’t let them be rotated out of the system. Relook the matter of annual elections if it is giving bad outcomes. If Boards are to perform an effective oversight role its members need to be around for a longer term rather than a shorter term
- Resize the Boards, be an effective strike force not a large dinosaur. There are not so many good chefs around, in any case too many cooks spoil the soup,
- ensure that the UGLINESS and the triple A types do not enter our Boards.
- start by ensuring that the values of UGLINESS and triple A types do not enter our own soul.

I leave you to ponder the 8 point for adoption in your organisation, it may turn out to be very “auspicious” for you – bringing you prosperity without running foul of the Regulators and with the blessings of the stakeholders who now have a happy share of your surplus value. Someone like the Company Secretary could facilitate its implementation.

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Writer is the Principal Adviser of BUSINESS MATCH Management Consultants and the President of The Malaysian Institute of Chartered Secretaries And Administrators (MAICSA). All views expressed are those of the writer alone.Whilst every effort is made to ensure the accuracy relevance and timeliness of facts, no undertaking is given as to accuracy, relevance and timeliness of facts quoted. No advice is intended, each opinion is to be examined prior to adoption by readers for applicability in your own organisations.

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Corporate governance developments in Malaysia

Background

Corporate governance in Malaysia has come a long way since the Report on Corporate Governance, commissioned by the High Level Finance Committee, was launched a decade ago. The report was very much influenced by the events of the Asian financial crisis which hit the region back in 1997/1998. The Malaysian Code on Corporate Governance (Code), issued in March 2000, marked a significant milestone in Malaysian corporate governance reform.

Since then, Malaysia has made significant strides in improving corporate governance standards. The year 2007 saw significant enhancements to laws and regulations, and revisions of the Code to strengthen the regulatory framework of the capital market.

Enhancements to the CG Framework

Capital Markets and Services Act 2007 (CMSA)

The CMSA came into force on 28 September 2007, consolidating the Secu-
rities Industry Act 1983, the Futures Industry Act 1993, and Part IV of the Securities Commission Act 1993, which deals with fund-raising activities. The CMSA provided for better safeguarding of investor interests and further enhancement of corporate governance. The CMSA introduced provisions which widened the enforcement powers of the Securities Commission (SC). These include the ability to take civil action, and to obtain compensation of up to three times the monetary gain made (or loss avoided) for a range of offences, including false trading, stock market manipulation, and the use of manipulative and deceptive devices.

Companies (Amendment) Act 2007
The Companies (Amendment) Act 2007 introduced several amendments, including:
- Expansion of the duty of directors to disclose interests.
- Prohibiting interested directors from voting.
- Clarification of directors’ functions and duties.
- Widening the scope of duty of care, skill, and diligence.
- Clarification of the functions, duties, and responsibilities of nominee directors.
- A prohibition on related party transactions except where there is prior approval by disinterested shareholders.
- Allowing companies to conduct shareholders’ meetings electronically.
- Requiring public companies to establish a system of internal control.
- Requiring auditors of public companies to report on serious offences involving fraud and dishonesty, and affording protection to auditors on genuine reports made in good faith.
- Requiring auditors to report to the Registrar, and to Bursa Malaysia (if auditing a public listed company), the grounds of their removal, resignation or declaration of re-appointment.

“The roles and responsibilities of the board of directors, particularly independent directors and the audit committee, were strengthened to ensure that they discharge their duties effectively”

- Introducing the statutory derivative action to facilitate redress against oppression of the minority under Section 181 of the Companies Act, 1965.
- Introducing a whistle-blowing provision to afford protection to officers who report on contraventions or serious offences involving fraud and dishonesty.

Revisions to the Malaysian Code on Corporate Governance (Code)
The Code was revised in 2007 to improve the standards of corporate governance, especially in the area of board quality. The roles and responsibilities of the board of directors, particularly independent directors and the audit committee, were strengthened to ensure that they discharge their duties effectively. A majority of audit committee members must be independent, and all must be financially literate. In order to preserve the independence of the committee, Executive directors are no longer allowed to become members of the audit committee. The revised Code spells out the eligibility criteria for the appointment of directors, the composition of the board, and the role of the nominating committee. All public listed companies were also required to have their own internal audit functions.

Bursa Malaysia Listing Requirements
In line with amendments to the regulations and the Code, Bursa Malaysia Listing Requirements were also amended to raise governance standards amongst listed issuers and enhance investor confidence. The amendments included enhanced disclosure requirements in the annual report, expansion of the mandate of the audit committee to include reviewing the adequacy and competency of the internal audit function, setting out the functions and composition of the audit committee, and mandating the internal audit function.

Recent Reforms
More recently, in 2009 and 2010, efforts to enhance investor protection have been stepped up. These efforts include strengthening regulations, facilitating dispute resolution mechanisms, empowering investors through education, promoting shareholder activism, and encouraging swift and appropriate enforcement action by regulators.

Enhanced enforcement powers of the SC
Two new provisions of the CMSA, which accord better protection to investors, were passed by Malaysia’s Parliament in December 2009. They enable the SC to take effective enforcement action against errant directors and officers of public listed companies and their related corporations. Section 317A enables the SC to take enforcement action against anyone who does anything (or causes anyone to do anything) with the intention of causing wrongful loss to the listed corporation or its related corporation. Section 320A makes it an offence for directors and officers of listed corporations to influence any person who prepares or audits the financial statement of a listed corporation to cause the financial statement to
be false or misleading. Both provisions carry a maximum term of 10 years’ imprisonment and a fine not exceeding RM10 million.

Amendments were also made to Section 368 and 371 of the CMSA to make it an offence for anyone to falsify or destroy any accounting records or books of a listed corporation or its related corporation(s).

Launch of the Unified Board and the ACE Market
In order to enhance the quality of listed companies on Bursa Malaysia, the new Unified Board and the ACE Market were launched on 3 August 2009. This marked an important milestone in the development of the equity fund-raising market in Malaysia. The new structure is designed to make Bursa Malaysia a more attractive listing venue and to enhance competitiveness and efficiency in the Malaysian capital market. It accomplishes this by streamlining rules and processes in order to provide greater certainty, shorter time-to-market, and lower regulatory costs. The enhanced framework also facilitates foreign listings by assimilating the requirements for domestic and foreign companies.

Bursa Malaysia is also expected to take on a more active role as the frontline regulator for secondary equity fund-raising and aims to increase efficiency of the market. The development of the equity market has also been accompanied by the transformation of the bond market, leading to the rapid development of the debt securities and sukuk markets.

Establishment of the Audit Oversight Board
In line with global trends, Malaysia has established the Audit Oversight Board (AOB) to strengthen the independent oversight of auditors. The AOB was established under Part IIIA of the Securities Commission Act 1993.

“The AOB is tasked with registering auditors of public interest entities, and to inspect and monitor auditors to assess the extent of their compliance with recognised auditing and ethical standards”

The AOB’s mission is to assist the SC in overseeing the auditors of public interest entities and to protect the interest of investors by promoting confidence in the quality and reliability of audited financial statements of these entities. The AOB is tasked with registering auditors of public interest entities, and to inspect and monitor auditors to assess the extent of their compliance with recognised auditing and ethical standards. The AOB is also empowered to sanction any registered auditors for failure to comply with the provisions of Part IIIA of the Act. It is now in the first phase of promoting good governance of the auditing profession, and is in the midst of registering auditors engaged by public interest entities.

In September 2010, Malaysia was admitted as a member of the International Forum of Independent Audit Regulators. This was a formal recognition of Malaysia’s AOB as a well-structured, independent audit regulator on par with agencies of other jurisdictions. Malaysia’s AOB is only the second such body in ASEAN to be admitted.

Establishment of an Alternative Dispute Resolution mechanism
Work is also in progress on the establishment of an alternative dispute resolution body, to be called the Securities Industry Dispute Resolution Centre (SIDREC). The Centre will act as a mediation and dispute resolution forum to deal with small monetary claims filed by individuals with respect to their dealings in securities and capital market products through market intermediaries.

New investor protection initiatives in progress
The SC is also reviewing investor protection initiatives such as the sophisticated investor framework, sales practices, and enhancing the Malaysian Code on Takeovers and Mergers. The SC and Bursa Malaysia had, earlier in the year, proposed changes to the mergers and acquisitions rule using the assets and liabilities route. The proposed changes include raising the threshold to require the approval of shareholders holding at least 75% of target company shares for a deal to proceed. Currently, mergers and acquisitions using the assets and liabilities route only require the approval of shareholders holding a simple majority of target company shares.

Promoting Shareholder Activism
One of the important capital market institutions is the Minority Shareholder Watchdog Group (MSWG), a body set up in 2000 on
the recommendation of the High Level Finance Committee. Currently, MSWG is substantially funded by the Capital Market Development Fund.

MSWG has been actively encouraging minority shareholders to play their role in ensuring that Boards and management are running the business in the best interest of the company, and to voice their concerns should it be otherwise. MSWG’s primary approach is to proactively engage with the Boards and management of public listed companies on issues related to financial performance, corporate governance, and corporate responsibility. This is done through attendance at annual general meetings, where questions or concerns are raised to the Board for the benefit of minority shareholders.

MSWG’s annual Malaysian Corporate Governance Index creates awareness of, and encourages, corporate governance best practices among PLCs in Malaysia. The inaugural MCG Index 2009 revealed that the corporate governance score of the listed companies in Malaysia had shown improvements over the previous few years. Nevertheless, the following areas were identified as those that could be further improved to raise the CG bar:

- The role of independent directors.
- The separation of powers between the Chairman & CEO.
- Directors’ remuneration.
- Board performance appraisal.
- Risk management • Poll and proxy voting.

Role of Institutional Investors

Institutional investors in Malaysia are also playing a more active role to enhance corporate governance. The single largest institutional investor in Malaysia, the Employees Provident Fund (EPF), is actively advocating CG best practices in its investee companies. The EPF recently launched its Corporate Governance Principles and Voting Guidelines to promote corporate governance, transparency, and integrity within its own organisation as well as in its investee companies.

“Institutional investors in Malaysia are also playing a more active role to enhance corporate governance”

Strengthening the Role of Directors

On the boardroom front, MSWG has launched its Independent Directors’ Pool to increase and complement the existing pool of independent directors in Malaysia for the benefit of the capital market. The Malaysian Alliance of Corporate Directors (MACD) was also formed to promote corporate strategic performance, best practices in corporate governance, and the development of corporate directors with a high level of entrepreneurship.

Directors’ training on awareness of best practices, and the development of Bank Negara Malaysia’s Financial Institutions Directors’ Education (FIDE) programme for directors of banks and other financial institutions, have also been given greater emphasis.

New Initiatives Moving Forward

Moving forward, there is much more in store for corporate governance development in Malaysia.

The publication “Statement on Internal Control: Guidance for Directors of Public Listed Companies”, which was issued in year 2000, is currently under revision by The Institute of Internal Auditors Malaysia. Following the Prime Minister’s 2011 Budget announcement regarding private pensions, a private pension framework is being developed by a task force led by the SC. The framework is expected to lead to greater transparency and accountability in the pension fund landscape, and create a more robust capital market as Malaysia moves towards its goal of becoming a developed, high-income nation.

A new five-year blueprint on corporate governance is expected to be unveiled in 2011. The International Corporate Governance Consultative Committee (ICGCC), has been formed to provide views on corporate governance developments and trends, and to advise on key focus areas and policy recommendations in the formulation of the blueprint. The Committee is chaired by the SC Chairman, and is comprised of 10 other senior industry participants and experienced professionals from Malaysia and abroad.

Work is currently in progress, led by a high-level working committee and various sub-committees. As one of the working committee members, MSWG will be providing input on improvements to corporate governance that should be incorporated into the framework.

Conclusion

Malaysia has a robust corporate governance framework which compares favourably to international standards. In addition, a lot of effort and resources have been deployed by both regulators and market players to strengthen and raise the bar on corporate governance.

Nevertheless, changes in the corporate landscape and new corporate governance issues in Malaysia and at the global level demand that regulators and market players look at improving the existing corporate governance framework and practices. This will ensure that they remain robust, current, and able to encourage high standards of corporate behaviour to protect the integrity of the capital market.

Notwithstanding these efforts, the challenge to embrace corporate governance in substance, and not just in form, still remains.

Rita Benoy Bushan Chief Executive Officer Minority Shareholder Watchdog Group (MSWG) 28 October 2010.
How effective is your Board?

“From the mailroom to the boardroom, everyone should adhere to the same high standards of ethical behavior and commitment to compliance”

In today’s highly regulated and risk-aware business environment, organizations are constantly searching for the best corporate governance practices that can help their boards of directors to be more successful in carrying out their duties. At Deloitte, we are constantly asked by clients about what they should - and should not - be doing.

The following is a list of ten activities boards should avoid in order to improve their effectiveness in the boardroom. This list is not exhaustive, and there may be other considerations for the board, however it’s a good starting point to see where your organization might be going wrong.

1. Avoid presentation overload

Presentations should not dominate board meetings. If your board meetings consist of a scripted agenda packed with one presentation after another, there may not be sufficient time for substantive discussions. The majority of board meetings should be focused on candid dialogue about the critical strategic issues facing the company. The advance meeting materials should comprise information that provides the basis for the discussions held during the meeting. Management should feel confident that the board will read these pre-meeting materials, and the board must commit an adequate amount of time in advance of the meeting to do so.

2. Avoid understating the importance of compliance

3. Avoid postponing the CEO succession discussion

CEO succession planning is one of the primary roles of the board. With the changing governance landscape and new and proposed regulations, the board has a full agenda these days. However, it is important to occasionally take a step back to ensure the board is addressing this important responsibility. During this time of rebuilding and prior to the implementation of new regulations, boards should assess where time is being spent and perhaps redirect focus on succession. It is important to note that the succession planning process is continuous and doesn’t end when a new CEO is selected. As the company evolves, its needs change, as do the skills required of the leadership team. The board needs to ensure that a leadership pipeline is developed and that its members have ample opportunity to connect with the next generation of leaders.

4. Avoid the trap of homogeneity

The topic of board composition and having the “right” people on the board continues to receive much attention. The shift to independent board members facilitated a move away from a “friends on the board” approach to a new mix. However, the board needs to assess whether this new mix translates into a positive and productive board dynamic. Boards should take a closer look at the expertise, experience and other qualities of each member to ensure the board can provide the right expertise. Diversity of thought provides the perspectives needed to effectively address critical topics, which can contribute to greater productivity and ultimately a stronger board.

5. Avoid excessive short-term focus

Perpetual existence is one of the principal reasons for the initial development of a corporation. However, recent history offers many examples of modern corporate entities managing to reach short-term results at the expense of long-term prosperity. The board can demonstrate its leadership by being the voice of reason and openly discussing the sustainability of strategic initiatives. This can result in a well-governed company with a greater chance of achieving long-term, sustainable success.

6. Avoid approvals if you don’t understand the issue

Steven Lim: As the company evolves, its needs change, as do the skills required of the leadership team.

There is no room for a culture of complacency when it comes to compliance with laws and regulations. Building a culture of ethics and an effective compliance program within an organisation is a business imperative. From the mailroom to the boardroom, everyone should adhere to the same high standards of ethical behavior and commitment to compliance.

Steven Lim
Complex issues can have significant implications for the survival of an organisation. It is up to directors to make sure that they understand issues that can alter the future of an enterprise before a vote is taken. This doesn’t require dissecting every detail, but it should consist of a thorough investigation and assessment of the risks and rewards of proposed transactions. If you don’t adequately understand the issue, ask for more education from management or external experts. It comes down to being able to ask the tough questions of management and probing further if things do not make sense. Consensus doesn’t mean going along with the crowd. True consensus results from a thorough debate and airing of the issues before the board, resulting in a more informed vote by directors.

7. Avoid discounting the value of experience

8. Avoid stepping over the line into management’s role

A board that makes management decisions will find it difficult to hold the CEO accountable for the outcome. A director’s role is to oversee the efforts of management rather than stepping into management’s shoes. Directors must make a concentrated effort to ensure that they have clarity on management’s role, which is to operate the company. The distinction between the board and management is often blurred by directors who forget that they are not charged with running the day-to-day operations of an enterprise. This doesn’t prevent a director from getting into the details of an issue facing the company, but it does mean that directors should avoid stepping over the line.

9. Avoid ignoring shareholders

A company’s shareholders are among the most important and potentially vocal constituents of the enterprise. Concerns can sometimes be addressed by providing shareholders an audience with the board to air their concerns. Directors should engage in shareholder dialogue and meetings.

10. Avoid a bias to risk aversion

With the recent focus on excessive risk-taking and its impact on the credit crisis, there is concern that companies and boards may become risk-averse. At many organisations, risk governance and value creation are viewed as opposed or even as mutually exclusive, when in fact they are inseparable. Every decision, activity, and initiative that aims to create or protect value involves some degree of risk. Hence, effective risk governance calls for Risk Intelligent governance — an approach that seeks not to discourage appropriate risk-taking, but to embed appropriate risk management procedures into all of an enterprise’s business pursuits. By treating risk as intrinsic to the conduct of business, Risk Intelligent governance elevates risk management from an exercise in risk avoidance to an essential consideration in every decision, activity, and initiative. Such an approach can provide companies and boards the ability to remain nimble and agile in times of distress, while continuing to focus on how to extract value from the opportunities presented to the company.

Now that we’ve identified some of the problems a board can have, what are the key areas that boards should address to improve their effectiveness in the boardroom? For the purpose of addressing these key areas, we will share with you the questions that directors may ask to further explore the issues with their own boards. Again, this list is not exhaustive, and there may be other considerations that the board must consider. So what questions should you be asking?

1. Risk Management

Do we have a risk-intelligent culture? Is risk management considered to be part of everyone’s responsibilities, or just those of the risk management department?

What is our organisation’s risk appetite and how do we manage and mitigate its risks? Do we link risk and reward in our strategic planning? Is the organisation’s risk appetite communicated to and understood throughout the organisation?

Have we identified all of the risks facing the organisation and do we keep that list of risks updated regularly? Do we fully understand those risks? How well does the board and management factor the understanding of those risks into their decision-making process?

2. Strategy

How much time does our board spend on strategic discussions? Should we have a retreat with management to discuss strategy? Do we set aside enough time on our agenda for discussions about strategy?

Does management provide the board with the right information, the right amount of information, and in the right format to enable the board to effectively and productively challenge the short and long-term strategic objectives and ultimately approve the organisation’s mission?

Is our strategic plan aligned with the organisation’s risk appetite and profile?

3. Liquidity

How well do we understand liquidity and the fundamental characteristics of our funding instruments? Do we know how these may change under different kinds of pressure?

How can we develop prediction models or scenarios to assess possible liquidity problems? Do we know how many sources of liquidity the organisation has and how quickly they could dry up in a crisis? How long can we survive without normal sources of liquidity?

What are our assumptions about our sources of liquidity and when did we last test them? Have we reviewed the stress testing performed by management?

How well do we understand the impact of changes to the company’s credit rating on operations and liquidity?
4. Executive Compensation
How are our compensation policies developed? Are the policies aligned with the short and long-term goals of the organisation?
Are our compensation packages adapted to different scenarios? Do we actively conduct scenario analyses to test our executive compensation packages?
Are we complying with all the relevant regulatory requirements? How aware are we of the latest legislation? Are we running any unnecessary legal risks?
How independent are the members of our compensation committee? Do the board and the organisation’s human resource department employ the same or different compensation advisors? How knowledgeable are our compensation committee members about pay and incentives?

5. Financial Reporting
Have we reviewed an IFRS conversion plan? Is it comprehensive? Have we identified any obstacles to implementation?
Do we have a communication strategy in place to address reporting issues arising under IFRS?
Have we obtained assurances from our external auditors on our opening balance sheet under IFRS?

6. Succession Planning
Is succession planning included in the board’s agenda? Are the succession planning objectives well defined and aligned with the organisation’s strategic objectives?
How prepared is the organisation for an unexpected resignation or retirement of the CEO? Has the board evaluated the risks that the organisation would face if the CEO had to step down suddenly?
Does the board have an up-to-date understanding of the skills and knowledge required of the CEO? Are there candidates within the organisation that meet this profile? Is the board aware of the processes management has implemented to attract, develop and retain talent in the organisation?

7. Shareholder Engagement
Do we have a strategy for communicating with our shareholders and stakeholders?
Are we aware of any legal or regulatory restrictions affecting the way in which the board communicates with stakeholders?
What steps can the board take to better understand the expectations of its stakeholders?

8. Board Chair
Have we clearly defined the roles of the CEO and board chair? What is the optimal balance of power, and has this been affected by changing economic circumstances?
How do we effectively maintain the balance between independence and knowledge?
How do we divide the ownership of issues between management and the board, and especially the board chair? How do we determine who is responsible for financial performance, stakeholder management and shareholder value?

9. Board Composition
What changes have occurred in our organisation, its industry and regulatory and legislative environment? How have these changes affected our organisation’s direction, markets, operations and other activities? Does the board have the necessary knowledge and expertise to provide effective oversight of the organisation and its activities in this changed environment?
How often do we review the composition of our board? Has our review identified any skill gaps among the directors? Are there directors whose skills are no longer applicable to the organisation’s needs?
Do we have a structured review and rotation plan that enables the board to adjust its membership in a way that revitalizes the board without disrupting continuity? Do we provide a mechanism for past directors to continue to act as advisors to the board?

10. Board Assessments
How do we assess the performance of the board and its committees? Does our evaluation process provide the board with useful, focused feedback that enables us to improve performance?
Do we update our evaluation criteria to reflect the changing demands placed on the board and the organisation? Does our process effectively identify directors’ education and development needs? Do we follow through with appropriate learning programs?
Does our assessment process help us improve communication and interaction between board members, and strengthen the board’s ability to work effectively as a team?

The views expressed in this article are those of the author and not necessarily those of Deloitte.
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Value proposition of Malaysia’s capital market

Over the past 10 years, there has been tremendous growth in trade and investment between Malaysia and China. And as alluded to by Mr Guo, Malaysia’s total trade with China exceeded USD36 billion. Malaysia’s exports to China in the first five months of this year rose by 82.2% to USD19.1 billion compared with the same period last year, making China Malaysia’s largest trading partner.

However, the level of cross-border participation and investment in the capital markets between China and Malaysia remains relatively low. With the recognition of Malaysia as a QDII investment destination, it is our hope that Chinese participation in the Malaysian capital market and vice versa will show a step jump in improvement.

Malaysia’s capital market offers a unique value proposition and can be an attractive investment destination for Chinese investors. We have an active market for corporate transactions and we have high levels of foreign participation in our financial and capital markets.

With 962 companies listed on it, our stock exchange, Bursa Malaysia, offers the widest and largest selection of companies in ASEAN1. Investors can therefore have access to an extensive selection of stocks across diversified industries for broader and deeper investment portfolios. Dividend yields in Malaysian equity are attractive and supported by sustained corporate earnings and dividend payouts. At the end of December 2009, the average dividend yield for companies listed on Bursa Malaysia was recorded at 3.3%, a relatively attractive yield compared to other regional markets.

Bursa Malaysia is home to several of the world’s largest plantation companies and is the world centre for price discovery of crude palm oil.

The liberalisation of our Equity guidelines two years ago have seen the listing of several Chinese companies on Bursa Malaysia, and we hope that this new phase in the development of the relationship between our two markets will see greater

Kuala Lumpur: Dividend yields in Malaysian equity are attractive and supported by sustained corporate earnings and dividend payouts.
interest from Chinese companies seeking to raise funds in the Malaysian market, complemented by deeper and more sustained interest in Chinese companies by Malaysian investors.

One of the fastest growing segments of the Malaysian capital market is our investment management industry. Malaysia has the largest unit trust industry in ASEAN and a fund management industry that has been the fastest growing segment of our capital market over the past few years. As at 30 June 2010, the total net asset value of unit trust funds stood at RM207 billion (USD63.34 billion), representing almost 20% of Bursa Malaysia Securities market capitalization. The creation of new products to facilitate diversification of investment portfolios by investors and fund managers is an important feature of our market. This year, Malaysia has seen a number of milestones in the collective investment scheme industry. In July this year, 2 new ETFs, namely CIMB FTSE ASEAN 40 Malaysia and the CIMB FTSE Xinhua China 25, both being Malaysia’s first offshore invested ETFs, were listed on Bursa Malaysia thus providing investors access to the top stocks in ASEAN and China. In the same month, the Sunway REIT, one of the largest REITs in South East Asia, made its debut on Bursa Malaysia with a fund size of 2.78 billion units, valued at RM3.7 billion (USD1.13 billion).

Our bond market is another important segment of the Malaysian capital market. With current outstanding bonds of RM704 billion (USD215.29 billion), Malaysia has one of the largest bond markets in Asia; and certainly the largest in ASEAN. Notable institutions, including the World Bank, Asian Development Bank and International Finance Corporation, have all raised funds through our bond market and we have seen foreign companies seeking both primary and secondary listings for their bonds on Bursa Malaysia. As a percentage of GDP, the Malaysian bond market is the second largest market in Asia (ex Japan).

Very significantly, Malaysia has, over the years, developed one of the largest and certainly, the most comprehensive Islamic capital market in the world - offering the broadest range of Shariah compliant products and services on an end-to-end basis.

The recognition of Malaysia as an approved QDII investment destination will certainly bring a wealth of benefits to both markets

Currently, 88% of the stocks listed on Bursa Malaysia making up 64% of total market capitalization are shariah-compliant. Our Sukuk market has experienced unprecedented growth over the years. In 2009, over 59% of all bonds approved by the SC were Sukuk. More than 60% of global sukuk outstanding originated from Malaysia2. (RM261 billion (USD79.82 billion)).

In May this year, the Malaysian government raised a USD1.25 billion sovereign sukuk; the largest US dollar sovereign sukuk globally to date, attracting more than 270 investors from around the world. The Malaysian sukuk market subsequently saw another landmark transaction in July this year when Cagarnas Berhad, the national mortgage corporation launched the innovative Sukuk al-Amanah Li al-Istithmar (Suuk AIm), under its RM5 billon (USD1.53 billion) Islamic Commercial Paper (ICP) and Islamic Medium Term Note (IMTN) Programmes.

The Islamic unit trust industry has also made significant progress. Malaysia currently has 151 Islamic unit trust funds with a total NAV amounting to RM22.69 billion (USD6.94 billion). The Islamic fund management industry constitutes the fastest growing segment of the Islamic capital market with an annual compounded growth of more than 25% over the past 5 years. The Islamic fund management segment has been fully liberalised with attractive tax incentives as well as mandates to foreign players. With the liberalisation in 2009, we now have 14 fully-fledged Islamic fund managers operating in Malaysia’s Islamic capital market.

We believe the strong demand for Islamic capital market products globally and the strong interest shown by international financial markets to develop their own Islamic finance industry will help push the boundaries of the Islamic capital market further. Certainly this is a rich area to be explored in developing demand between the Chinese and Malaysian investors.

Over the course of the past decade, Malaysia has been able to develop a broad based capital market that has become a significant player in the regional landscape. We have an internationally benchmarked regulatory infrastructure that has been assessed to be highly compliant with international standards, and our investor protection framework has been rated consistently by the World Bank as being among the top four in the world. We continue to be mindful of the need to strengthen our regulatory framework and ensure appropriate supervision and oversight. We must heed the lessons of the global financial crisis and ensure that we continue to pay attention to investor protection.

The recognition of Malaysia as an approved QDII investment destination will certainly bring a wealth of benefits to both markets. I hope that investors and intermediaries from both sides will pursue the opportunities available to them with great vigour. As regulator, we will continue to facilitate and support the private sector to identify and exploit the opportunities to create value.

I believe this Forum is merely the first step towards strengthening the ties between our two markets. I hope the introductions and the networking that the Forum will facilitate will encourage more extensive engagements between capital market players from both sides and will lead to the conclusion of substantive transactions and enhanced flows of funds between our two markets. The SC will continue to strive to be facilitative and we encourage issuers and intermediaries to pro actively engage and consult with us.

Investor relations in Malaysia

In the current climate, where investors demand timely and quality information from companies and attach a premium to high standards of corporate governance, good investor relations practices both in substance and form, can no longer be considered optional but rather a necessity in any well run company.

The SC has always held investor relations to be an important factor in facilitating investor protection and a responsible and transparent market environment. This was reflected in our Capital Market Master Plan in the emphasis placed on the need for meaningful and timely disclosure, responsible promotion practices as well as improved communication and engagement with investors, including, the setting up of investor relations units by PLCs to deal with investors and analysts.

Indeed, the SC ourselves have a dedicated department tasked with addressing investor concerns. Its role is to not just look into and where possible address concerns or enquiries raised by investors but also to increase investor awareness of their rights and responsibilities and of the capital market and the products offered. We also receive extremely valuable market intelligence through this channel that feeds into our regulatory function and the development of our policies and regulations.

Similarly, the Investor Relations Officer in any company plays a critical role in ensuring the meaningful engagement of different investor segments and their respective needs and concerns. It allows for a two way flow of information. For investors it allows the communication of information, addressing their concerns and facilitating the ease of their engagement with the company as shareholders. And from the company’s perspective, it provides an avenue for invaluable feedback that can then be used to analyse the market, develop effective business strategies and assist companies in making the right decisions particularly during times of crisis. The IR professional, with a holistic grasp of the company’s objectives, strategic direction and understanding of its financials, provides the company an effective channel of communication of key corporate developments and information that it needs to convey to investors and the market at large.

Companies often underestimate the positive impact of good investor engagement and transparent disclosure practices on the company’s reputation and ultimately its market value. One of the goals of investor relations and is to create a loyal shareholder base which will in turn enable a company to approach its capital management exercises with confidence. The information received by shareholders might not always be what they want to hear, but what is important is for them to feel that they are being treated fairly and that there is full disclosure on the company’s part. Through this process, companies can foster a climate of favourable opinion that would build a body of investor support and confidence and help achieve a fair market valuation for their securities.

It is heartening to see that this imperative has been embraced by MIRA in raising the profile and importance of investor relations as well as setting best practice standards for investor relations professionals and, judging from the long list of companies that are represented here today among the graduates, increasingly by the industry as well.

From CFOs to Executives, all of you will play a crucial role in being the direct link between investors and your respective companies. Investor relations is a vital component of our capital market because it not only has a direct impact on the reputation of PLCs or market intermediaries, but also on the market as a whole. As Malaysia’s capital market matures and progresses, investors will be better informed and will hold companies accountable when making their investment decisions.

The investor relations function of a company has evolved and the IRO has become indispensable in safeguarding the company’s most critical and intangible asset: its reputation with shareholders and other stakeholders. Indeed, according to a 2010 survey of 144 IROs in Fortune 500 companies, an overwhelming majority -81 percent-report directly to the CEO or CFO of the company, demonstrating the critical value of the role.

Today, in a disclosure based regime, the onus is on investors to evaluate the merits of investments in the capital market. In this regard, it is crucial for corporations and capital market intermediaries to be fully aware of their responsibilities in the provision of full, accurate and timely disclosure of information to investors. Programmes like the Certificate of Investor Relations will clearly help inculcate greater awareness among corporate players, of the bottom line imperative of meeting their obligations to their shareholders and hopefully, concretise the culture of good corporate governance into the DNA of the board and management of PLCs and intermediaries alike.

Keynote Address by YBhg Datuk Ranjit Ajit Singh
Managing Director, Securities Commission Malaysia at the Inaugural Graduation Ceremony of Certificate in Investor Relations (CIR) Thursday, 5th August 2010 Kuala Lumpur, Malaysia
SC names members of the International Corporate Governance Consultative Committee

The Securities Commission Malaysia (SC) announced last August 26, 2010 the members of a high-level committee which will provide strategic direction, views and advice to the SC in the development of a new five-year corporate governance blueprint outlining an action plan to further raise the standards of corporate governance in Malaysia.

The Malaysian government had in 1999 published a comprehensive report on corporate governance with the High Level Finance Committee Report on Corporate Governance which brought about far-reaching changes such as the introduction of the Malaysian Code on Corporate Governance, amendments to the relevant laws and the introduction of mandatory training for directors.

The International Corporate Governance Consultative Committee (CGCC), chaired by SC Chairman Tan Sri Zarinah Anwar, comprises 11 senior industry participants and experienced professionals from Malaysia and abroad. The CGCC will provide views on corporate governance developments and trends and advise on key focus areas and policy recommendations towards the formulation of the blueprint, which will outline various initiatives and recommendations to be implemented between 2011-2015.

“The development of the new blueprint is critical given the significant changes to the corporate landscape as well as new corporate governance-related issues that have surfaced in Malaysia and internationally,” Tan Sri Zarinah said.

A holistic review of the Malaysian corporate governance is timely since most of the recommendations made in the Finance Committee Report have been implemented over the past 10 years.

The new blueprint will be a comprehensive and forward-looking document covering strategic priorities to further enhance Malaysia’s corporate governance standards and identity.

The Committee will be supported by the Corporate Governance Working Group (CGWG) comprising senior regulators and market professionals. The SC will also be consulting other relevant stakeholders and industry groups in the preparation of the blueprint.

The development of the new corporate governance blueprint was first announced by Tan Sri Zarinah at the SC-Bursa Malaysia Corporate Governance Week 2010 in June this year.

The other CGCC members are:

1. Tan Sri Dr Wan Abdul Aziz bin Wan Abdullah, Secretary-General, Ministry of Finance
2. Tun Mohamed Dzaidin Haji Abdullah, Chairman, Bursa Malaysia Berhad
3. Tan Sri Azlan Zainol, Chief Executive Officer, Employees Provident Fund
4. Dato’ Sri Nazir Razak, Group Managing Director/Chief Executive Officer, CIMB Group
5. Dato’ Johan Raslan, Executive Chairman, PricewaterhouseCoopers Malaysia
6. Tan Sri Megat Najmuddin Khas, President, Federation of Public Listed Companies Malaysia
7. Dato’ Azmi Ariffin, Chief Executive Officer, Companies Commission of Malaysia
8. Charshai Charuvastra, President and Chief Executive Officer, Thai Institute of Directors Association
9. Fianna Jesover, Senior Policy Manager, Corporate Governance, Organisation for Economic Co-operation and Development (OECD)
10. Peter Elston, Strategist, Aberdeen Asset Management Asia Limited
Colaborative governance and the sustainability revolution

Over the last 150 years, two great revolutions – the Industrial Revolution, and the Information Revolution – changed entire markets, industries, products, services, and manufacturing processes. They went even further – changing entire economies and lifestyles, and with it the way countries developed and were governed.

We have not seen the full implications of the Information Revolution, yet the next great era – the “Sustainability Revolution” – is already upon us. The most widely quoted definition of sustainability and sustainable development is that of the Brundtland Commission of the United Nations, which states, “Sustainable development is development that meets the needs of the present without compromising the ability of future generations to meet their own needs.” Whereas the Industrial and Information Revolutions allowed companies to do more with more, the unique feature of the Sustainability Revolution is that it demands companies do more with less.

The urgent requirement for business success in the Sustainability Revolution is to understand the central issues – among them climate change, water depletion, renewable energy, food security, access to health, biodiversity conservation, poverty, access to technology, and age-based demographic shifts – that will change the goods and services we need, what and how we produce them, and how we succeed in making our enterprises live long and profitable lives.

A root cause of the Sustainability Revolution is inadequate public and corporate governance. This is no surprise. Governance systems have evolved to catch up to and support the technologies and processes of the Industrial Revolution. While they are not perfect, individual nations and inter-governmental systems have created the rules, regulations, safeguards, and approaches to support trade, commerce, finance, entrepreneurship, and innovation.

At the same time, Western corporate governance systems evolved to promote economic efficiency. They do so by ensuring management makes decisions in the interests of shareholders. Corporate governance in many Asian countries and some European take a more expansive view by seeking to harmonize the interests of owners, managers, and labor.

Yet both governments and corporate boards have failed to address the requirements of sustainable development. Governments have done little to respond to global challenges such as rapidly depleting fish stocks, growing inequality, water shortages, and greenhouse gas emissions.

Corporate governance systems are not designed to hold business to account for sustainable development. This would entail harmonizing financial performance with the complex dimensions of environmental and social performance.

One observes growing arguments among policy-makers and thought leaders of whether a model of democratic capitalism (or in some countries, socialist capitalism) is naturally adaptable to cope with the Sustainability Revolution. There is a growing collection of influential voices that suggest it is not. Increasing numbers have begun to champion an approach called Collaborative Governance.

Think of Collaborative Governance as a new, emerging invention. Its design and application remain in flux. It generally lacks legal structure and definition. Its prospects to emerge as a true, widely adopted innovation are uncertain. Yet
it is advancing. Every day it gains more champions and investors. At the same time the resistance of skeptics stays strong.

AccountAbility defines Collaborative Governance as the process by which different institutions – including business, government, civil society organizations (and even individuals) cooperate to improve collective decision-making. It aims to make sustainable development decision-making more reciprocal, participatory and inclusive. This cooperation requires governance systems where different institutions share roles and responsibilities, and where there is a clear understanding of accountability among them.

For business there are three emerging forms of Collaborative Governance summarized in Figure 1.

**I. Partnership**
The first type of Collaborative Governance is partnership. Businesses have a long history of working in partnership to advance sustainable development projects. Typical projects bring companies and civil society organizations together to address a specific problem for mutual benefit. The last decade has seen great creativity for project-based partnerships. The Hitachi Corporation, for example, has used its network of Foundations to create partnerships to support skill building for lower-income and less educated members of the work force. This is a tool to help individuals escape poverty. It also provides the company and its suppliers with a larger pool of skilled workers.

The second stage creates a joint venture. This is a significant relationship that creates a long-term, larger scale initiative designed to produce outcomes at scale. Financial institutions have built joint ventures with civil society organizations to design new business models that provide access to finance to the poor. Pharmaceutical companies like Merck, Pfizer, and NovoNordisk create joint ventures to develop new drugs for neglected tropical diseases. In these examples, formal legal arrangements define how partners share both risk and assets such as intellectual property and income.

The third stage creates a new enterprise. An example is the Global Alliance for Vaccines and Immunization. Partners from foundations, NGOs, and business come together to form a new enterprise that combines public and market-based approaches to encourage the innovation of distribution of new vaccines. Each partner is, in a sense, a “shareholder” of the new enterprise.

Embracing partnerships is vital for surviving the Sustainability Revolution. The challenges of sustainable development are too complex for any single company to manage alone. Companies need partners to spark ideas, bring additional investment capital, deliver intellectual and human capital, provide technology, and engage networks.

These partnerships can be extraordinarily innovative and complex. Yet they can also be difficult to manage. Success is certainly not guaranteed and often hard to achieve. Yet their potential knows no boundaries. The legal requirements for setting up partnerships are generally (relatively speaking) low.

**II. Stakeholder Governance**
Stakeholder Governance makes two arguments. First, it suggests that current modes of corporate governance lead to perverse consequences that undermine sustainable development and with it the long-term viability of the corporation. Second, and related, it suggests that companies will only be able to avoid these consequences if they are accountable to stakeholders and shareholders alike.

For example, consider the issue of climate change. Accounting and financial management discourages companies to assess indirect costs imposed on communities, eco-systems, and long term markets viability from greenhouse emissions. As a result, responsible Board members and investors should discourage companies to use anything but the cheapest forms of energy – i.e., fossil fuels. Yet climate change will harm the long-term viability of numerous industries.

Proponents of Collaborative Governance argue that the only way out of this trap is to encourage companies to become accountable to a broad array of stakeholders that will – in this case – harmonize the interest of shareholders with those that seek to mitigate climate change.

The first stage of Stakeholder Governance is to engage stakeholders as advisors. This is the approach described by Melco in the previous issue of Corporate Governance Asia. Melco seeks the opinions of stakeholders on corporate performance and impact on sustainable development. It produces annual reports that disclose sustainability performance. The company is under no formal obligation to respond to stakeholder concerns.

The second stage is to expand the composition of the Board to allow stakeholders to participate. Asian companies have experienced this with employee councils. Some companies, such as Lafarge, Nestle, and Siemens, create Stakeholder Advisory Panels that advise the Board on issues of sustainability performance. Other companies like 3M and Sodexo appoint as a voting member of the Board one or more representatives
with great knowledge and influence in certain communities related to sustainable development.

The third stage revises the terms of incorporation. In the United States, certain states now permit companies to incorporate as “B” or Public Benefit corporations. These companies are obligated to deliver results along a triple bottom line of economic, social, and environmental.

Stakeholder Governance is a highly contested area of Collaborative Governance. Opponents suggest it threatens to disable the ability of companies to serve as economic engines of growth, employment, wealth creation, and innovation. Proponents argue the opposite.

Extensive and sophisticated activism increasingly demands that companies embrace at least a Stage One approach. Companies that see threats of heavy sustainable development regulation and activism increasingly see the necessity of adopting Stage 2 approaches. Certain visionary companies see Stage 3 as part of the key to building new “responsibly competitive” strategies for growth in the Sustainability Revolution.

III. Partner in Public Governance

The third type of Collaborative Governance seeks to engage the private sector as a partner in public governance. This may not sound new. Many have advocated for the privatization of public services. Proponents argue that business can deliver public goods more cost-effectively than public institutions. What makes this new is the effort to link businesses arm-in-arm with civil society organizations. This collaboration tries to combine market-based drivers for quality, efficiency, and innovation, with civil society’s accountability, creativity, expertise, and service-capabilities in sustainable development.

The first stage is a variant of privatization, where provision of public goods is outsourced to businesses and civil society organizations. In the United States one finds growing examples of this in public education. In Asian and some European countries, one sees examples in worker training.

The second stage creates consultative mechanisms. In Asian societies, there is comfort and experience building public policy in deep consultation with the private sector. Once again, this approach brings business and civil society to the table together to advise and shape public policy. One increasingly sees such efforts happening without the blessing of governments. Business and NGOs together form strange bedfellows to advocate for example, carbon cap-and-trade systems, or fair treatment for women in the workforce. Multilateral Organizations such as the United Nations and the World Bank Group are now consulting more and more with business and NGO partners.

The third stage sees business and civil society form, in effect, alternative public governance systems. The most prominent examples are the proliferating number of multi-stakeholder governed voluntary standards systems. These include organizations like the Forest Stewardship Council, the Rainforest Alliance, and Social Accountability International.

Engaging business and NGOs as partners in public governance has captured the imagination of some advocates as a means to address the failures of the public sector. Yet this approach remains largely unproven. Opponents worry that these approaches could undermine democracy. Proponents argue that it will strengthen democracy and effective governance.

Final Thoughts

In the past, the design of governance systems has trailed the progress of major Revolutions. Over time, OECD countries have built approaches that use governance systems to support professional systems, controls, accounting, and performance to underpin the massive changes of the Industrial Revolution.

The Information Revolution is currently rocking the boat with its ability to create radical transparency. Its influence over corporate governance is still evolving, but one can predict it will be profound.

Among the unique qualities of the Sustainability Revolution is that it requires governance systems to lead the Revolution, not follow. Governance must help change the incentives that shape the choices of how individuals use resources. Collaborative approaches seek to balance interests in ways that encourage creativity and innovation to do more with less. It does not represent the only means to reform governance to suit the demands of the Sustainability Revolution. However, its orientation towards giving actors fair and equal voice make it more appealing than other alternatives one might imagine.

Many companies, through their adoption of Corporate Responsibility approaches, have unknowingly adopted features of Collaborative Governance. It is at the moment a bit exuberant to suggest that businesses have no alternative but to embrace Collaborative Governance. Some can preserve a business as usual approach and will do fine – at least for a few more years. Certainly some businesses managed to hold out and avoid the changes of the Industrial and Information revolutions. The question then as it is now is that with the massive opportunities and associated risks of the Sustainability Revolution, why would one want to?

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98% of companies in China hit by fraud

Kroll’s Annual Global Fraud Report reveals that fraud in China is up almost 10% compared with last year, and that it is more common and varied than anywhere else in the world.

China has overtaken Brazil as the top market in which companies suffered fraud, according to the latest edition of the Kroll Annual Global Fraud Report. This year’s study shows that 98% of the respondents in China suffered at least one type of fraud in the last year, while 90% of respondents in Brazil, which was in the top spot in 2009, said the same. Last year 89% of companies in China had experienced fraud, compared with Brazil’s 92%. The findings are the result of a study of more than 800 senior executives worldwide, commissioned by Kroll with the Economist Intelligence Unit.

The Global Fraud Report also found that the types of fraud experienced in China are more varied than any other market in the world. Nine of the 11 frauds covered in the survey affected at least one out of five companies, including management conflict of interest (30%), IP theft, piracy, or counterfeiting (26%), theft of physical assets or stock (22%), regulatory or compliance fraud (22%), financial mismanagement (22%), market collusion (22%), corruption and bribery (20%), vendor, supplier or procurement fraud (20%), and money laundering (20%). Respondents noted that high staff turnover (34%) and weak internal controls (34%) have increased their exposure to fraud.

The report found that like China, Southeast Asia has a number of significant fraud issues. 90% of respondents in Southeast Asia experienced fraud in the last year, positioning the region, along with Brazil, as the markets with the third highest incidence of fraud. Respondents in Southeast Asia reported one of the highest rates of theft of physical assets or stock (32%), while the incidence of IP theft (16%) was surpassed only by China. Respondents in Southeast Asia also face above average levels of management conflict of interest (26% compared with a global average of 19%).

Tadashi Kageyama, senior managing director, Kroll Hong Kong: “Given the large amount of family run businesses in Asia, management conflict of interest is a significant challenge in the region. A successful entrepreneur in Asia rarely has only one business; he usually has several similar or complementary businesses which may be in his name, the names of nominees, or his family members. For a company looking to do business in emerging Asia, it is important to map out those relationships, be aware of them and ensure that there are either no conflicts, or that potential conflicts are addressed and resolved ahead of time.”

The Global Fraud Report shows that companies operating in China are starting to broaden their approach to fighting fraud. The number of respondents planning to invest in financial controls (52%) is above the global average (45.8%), although is down from 73% in 2009. On the other hand, the number of those intending to put money into staff training (54%) and staff background checks (42%) has risen noticeably (from 35% and 31% respectively in 2009). This makes sense given that employees were identified as the key perpetrators of 42% of frauds experienced by respondents in China.

Violet Ho, managing director for Kroll in China said: “We are seeing an increasing amount of sophisticated and complex fraud schemes in China, which can cause much more financial, legal and reputational damage than the isolated kickback and bribery incidents common in the past. Motivated by greed, today’s schemes involve numerous departments, vendors, offshore entities, and have the potential to go undetected for years. Kroll has seen companies lose millions of US dollars in China to such situations because they failed to recognize the warning signs.”

While these numbers are promising, the report also shows that some areas are being overlooked. 44% of the frauds in China were perpetrated by vendors, suppliers and customers, however the number of companies in China that have partner, client, and vendor due diligence in place is significantly below the survey average (38% compared with a global average of 50%), as is the number intending to invest in this area in the coming year (32% compared with the global average of 41%).

Global key findings include:

Information theft has surpassed all other forms of fraud on a global level: Theft of information and electronic data has overtaken physical theft to become the most common type of fraud for the first time. 27.3% of respondents globally reported incidences of theft of information and electronic data over the past 12 months, compared to 18% in 2009. The amount lost by businesses to fraud rose from US$1.4m to US$1.7m per billion dollars of sales in the past 12 months – an increase of more than 20% from the previous year.”
PUBLIC BANK AD