MINORITY SHAREHOLDERS WATCH GROUP

BADAN PENGAWAS PEMEGANG SAHAM MINORITI BERHAD

(Incorporated in Malaysia – Registration No.: 200001022382 (524989-M)

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OF ETHICS, CULTURE AND SELECTIVE PROSECUTION

The bar set by the Malaysian Code on Corporate Governance is high compared with some regional peers. Yet, there have been numerous scandals and violations. The bottom line? Enforcement.

BY KUEK SER KWANG ZHE

Corporate governance, defined as "the process and structure used to direct and manage the business affairs of a company to promote business prosperity and corporate accountability", has been in the spotlight in Malaysia due to the emergence of several corporate scandals in recent years.

The 1Malaysia Development Bhd (1MDB) scandal saw billions of dollars siphoned off to offshore accounts and former prime minister Datuk Seri Najib Razak sentenced to jail. Then, there was the Littoral Combat Ship (LCS) scandal, in which Boustead Naval Shipyard Sdn Bhd, a subsidiary of Boustead Heavy Industries Corporation, failed to deliver its vessels after multiple delays, even though it had been awarded billions in contracts by the government. The Serba Dinamik Holdings Bhd case was another one that shocked the market. Four of its top executives were each slapped with a RM3 million compound fine by the Securities Commission Malaysia (SC) in April for submitting a false statement involving revenues of RM6 billion for its financial year 2020.

In all three cases, the board of directors failed in their duties and the checks and balances within those organisations did not work. What went wrong? Are the regulators setting the standards too low with regard to corporate governance? Or should the company directors be held responsible?

Industry experts whom ESG spoke to have come to different conclusions. The issue boils down to more abstract notions about ethics and culture, and the need for institutional reforms and enactment of new laws. But the experts all agree that the bar set by the Malaysian Code on Corporate Governance (the Code),

▸ Malaysian artist and activist Fahmi Reza speaks while holding his artwork bearing an image of former Prime Minister Najib Razak, during an interview with Reuters, in Kuala Lumpur

REUTERS

BLOOMBERG

revised on April 28, 2021, is already high when compared to regional peers.

Devanesan Evanson, CEO of Minority Shareholders Watch Group (MSWG), says certain measures laid out by the Code are quite advanced.

"They are on par with regional peers as our regulators, including the SC and Bursa Malaysia, always benchmark [our] regulations against comparable jurisdictions such as Hong Kong, Singapore and Australia. These are the more developed countries."

For instance, the Code recommends that any person who is linked directly to the executive arm of the government, such as those who hold positions as heads of state, heads of government and ministers, should not serve on the board of a company, as it would cast serious doubt on the independence of their judgement. Active politicians are also discouraged from being appointed as company directors.

The Code requires large companies — those on the FTSE Bursa Malaysia Top 100 Index or with a market capitalisation of RM2 billion and above — to have at least 30% of women directors on their boards. Gender diversity could enhance corporate governance as different perspectives can be raised and deliberated by the board.

Beyond the Code released by the SC, Bursa Malaysia announced in January that a person can serve as an independent director for not more than a cumulative tenure of 12 years under the enhanced listing requirement, which is another positive development for corporate governance, says Devanesan.

The overall performance of Malaysian public-listed companies (PLCs) with regard to corporate governance, based on disclosures in their annual reports, has been on the rise in recent years, according to MSWG's Malaysia-Asean Corporate Governance Scorecard Report 2019. The scorecard is a project to assess corporate governance of all PLCs by adopting the Organisation for Economic Co-operation and Development (OECD) principles as its main benchmark. It shows that the overall corporate governance score of 866 local PLCs increased by 19% to 98.4 in 2019 from 2015.

Professor Mak Yuen Teen, who researches corporate governance at the National University of Singapore and runs a blog called "Governance for Stakeholders", concurs with Devanesan.

"In general, the rules and regulations [regarding corporate governance] in Malaysia compare very favourably against those in many other countries, including Singapore. The Malaysian Code of Corporate Governance seems to be willing to introduce rules that other countries find a bit difficult to do at the moment."

For instance, he elaborates, the rule that active politicians should be excluded from a company's board and its chairman should not be involved in the audit, nomination and remuneration committees. "On introducing rules and regulations, Malaysia has always been willing to take the hard steps, and it seems to be able to push them through."

Michele Kythe Lim, president and CEO of the Institute of Corporate Directors Malaysia (ICDM), believes that Corporate Malaysia is on track to achieving good corporate governance, and that the country has a solid foundation and robust framework in place to strengthen it.

"In addition, we see significant efforts by the board of directors and organisations in taking proactive measures to address organisations' needs and ensuring good corporate governance. This is done through upskilling, independent board evaluations and [board] placements.

"The increase in ICDM's membership to 1,018 individual members and 74 corporate members (as at Sept 30) also signifies Corporate Malaysia's readiness to move forward and move up in our pursuit of good corporate governance," she says.

ROOT OF THE PROBLEM

Yet, industry players point out that whatever is written down on paper does not necessarily guarantee proper execution.

Without mentioning names, MSWG's Devanesan says there are companies that win corporate governance awards but end up being involved in high-profile corruption cases and misconduct.

"When it comes to disclosures and structures, these companies have them. They tick all the boxes. But when it comes to execution, they override the processes."

He says it boils down to ethics, morals and integrity. A company can have the best structures and processes for corporate governance in place, but it is up to the people at the top to implement them.

"Corporate governance doesn't measure a person's morality or integrity. You can have the best structures and processes. But if you don't have the requisite integrity, you overwrite them. Many good companies around the world have collapsed, not just locally," he says.

ICDM's Lim has similar view. She says many factors could have contributed to corporate governance issues, but it boils down to one thing: culture. "Culture in this context encompasses leadership, organisational strategy, values, ethics and talents.

"Ultimately, it is about forward-looking leaders, ethical leadership and how senior leaders set the right tone from the top to instil a culture that facilitates development of the right behaviour, so that people will do the right thing."

Are political appointees a main contributor to corporate governance issues locally? Devanesan says there aren't many active politicians sitting on the boards of PLCs. "I don't think there are many. As far as this is concerned, the Code discourages political appointments."

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DEVANESAN

Government-linked investment companies (GLICs) that hold substantial shares in some PLCs do appoint their own people to sit on the boards of these companies, but that should not be considered political appointments, he adds.

"GLICs such as the EPF (Employees Provident Fund) and KWAP (Kumpulan Wang Persaraan) appoint [their people as] directors to safeguard their interest when they hold, say, 30% of shares in PLCs. They are not active politicians."

Political economist Prof Dr Edmund Terence Gomez has a different view. He says local corporate governance issues are related to weak public governance, instead of ethics and culture, which are hard to measure. After all, it is hard to

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tell if Malaysians are less ethical than people in other countries, or that local corporate culture is "inferior" when compared to other nations.

On public governance, Gomez refers to government institutions that have oversight over companies that are truly independent from the influence of the executive arm of the government, mainly the cabinet and the prime minister.

Government institutions that are not independent would lead to selective prosecution, which means influential and well-connected individuals — including those in the corporate world — could avoid being properly penalised or prosecuted when they are involved in corruption cases or misconduct. In other words, enforcement actions from these institutions have to be impartial and effective.

"Even if you have the best corporate governance code in the region, why do we still have all these scandals? It is because we have selective enforcement. It doesn't mean that those institutions are not doing their work, but they are selective.

"If I'm running a company and am without connections, and did something that I should not have, I would be hauled up and charged in court, and even put in jail or fined. What if I'm well connected?" Gomez asks.

Political financing, which refers to corporations providing money to political parties or politicians for political purposes, is not yet governed by any Act. It is an open secret that this leads to corruption cases in the corporate world, he adds.

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MAK

Mak echoes Gomez's view that public governance is a factor that has contributed to local corporate scandals in recent years.

"There are public governance issues that involve the political aspects of things. I think even Malaysians themselves acknowledge it."

However, Mak points out that it is not an issue unique to Malaysia and that some regulators had taken relatively harsh actions against corporate figures who disobey the law. For instance, four top executives of Serba Dinamik were imposed maximum compounds by the SC for providing false statements on the company's revenue.

He understands that some Malaysians were hoping for the Attorney-General's Chambers (AGC) to press criminal charges against the company's directors, which did not materialise.

For comparison, Mak says Noble Group Ltd in Singapore, once Asia's largest commodity trader, was found to have published misleading information in its financial statement and was fined S$12.6 million in August this year by the Singapore authorities.

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LIM

"Some might say that Serba Dinamik's top executives should be charged by the AGC, and that the breach seems more blatant than in Noble. But at the end of the day, the individuals were imposed with the maximum compound whereas in the Noble case, no individuals paid money. The company was fined."

He adds that Bursa Malaysia recently reprimanded and fined independent directors and the chairman of local PLCs who were in breach of the listing requirements, whereas in Singapore, authorities there do not take action against independent directors at all.

"When I look at those kinds of offences and breaches in the listing rules, and the enforcement action taken by Bursa, I feel that the enforcement action in Malaysia is stronger than in Singapore for similar types of cases. In Singapore, authorities don't go after independent directors at all," he says.

INSTITUTIONAL REFORMS

To raise the bar, self-discipline among market players and key individuals is critical for good corporate governance to become intrinsic in the marketplace, says ICDM's Lim.

She points out that further training to enhance the professionalism of the board of directors can be easily conducted.

"Setting the right tone from the top is a crucial component to establish strong corporate governance standards and culture. This is where the board and its directors come into play. Integrity in governance will be ensured in large part by the board's professionalism and effectiveness," she says.

ICDM, whose main role is to support and accelerate good corporate governance, has 876 director candidates thus far — and the number is growing. Some of its notable initiatives include offering the Mandatory Accreditation Programme (MAP), designed to help first-time directors understand the essential principles of good governance and fiduciary duties of a director.

ICDM held the International Directors Summit 2022 in September and was granted in-principle approval by the SC to be the service provider in designing, developing and implementing the Mandatory Leading for Impact Programme (LIP).

"The LIP is Malaysia's newly introduced mandatory onboarding programme on sustainability for directors of companies listed on Bursa Malaysia. Among the first of its kind, it is designed specifically to help Malaysian boards deliver on the sustainability agenda," she says.

Upcoming research studies conducted by the ICDM include a board remuneration study, in collaboration with Bursa Malaysia and WTW (formerly Willis Towers Watson); the Asean Board Trends Report, and the Board Effectiveness Barometer report, which assesses the board's performance from the perspective of different stakeholders.

In a similar vein, Mak says the quality of new directors can be further improved by equipping them with better knowledge to monitor corporate culture. The MAP, which lasts 1½ days, could be replaced by a training programme of a longer duration.

A formal training framework and proper certification for directors can be considered, he adds.

"While Malaysia has a reasonable structure when it comes to [the training] of first-time directors, there isn't a formal framework to get them certified. I think Malaysia should think about professionalising directorship."

Mak also recommends that Malaysia further improve its search and nomination process for directors, which is an important way to ensure board effectiveness.

"I like the fact that Malaysia (referring to the Code) is now saying that you should not just ask for recommendations from your existing directors and major shareholders [for new members to join the board]. That has pushed more companies to cast their net further in search of directors, which is a good thing."

On the bigger picture, Mak says Malaysia's public governance should be enhanced. "A phrase used to be floated around saying that public and corporate governance are two wings of a plane. It means that if you have public governance issues, you are likely to have poor corporate governance too."

For Gomez, public governance is what affects corporate governance the most in Malaysia. His observation can be traced back to the various books he has written, including *Politics in Business: UMNO's Corporate Investments* (published in 1983) and *Minister of Finance Incorporated: Ownership and Control of Corporate Malaysia* (2017). Those books trace and explain the various business relationships between political parties, the government and corporations.

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GOMEZ

He says the nexus between Malaysian politics and businesses runs deep and goes as far back as the 1980s and 1990s. To uphold corporate governance, public governance needs to come into place to effectively penalise and punish people in the corporate world who misbehave or are involved in corruption. Institutional reform is required so that government institutions and regulators are truly independent from the executive arm of the government, such as the cabinet and prime minister.

Gomez says key personnel who helm government institutions and regulatory bodies should not be appointed by the cabinet or prime minister, but by an independent body such as a parliament select committee that includes politicians, professionals and members of civil society.

"There needs to be an independent committee for the selection process. Other countries have it. It is totally independent and its members are subject to public scrutiny, as in how they are selected. This kind of system needs to be in place," he says.

The political financing Act needs to be enacted to regulate and shed light on how political parties and politicians are being funded, he adds.

"Where is the discussion about this when corporate governance is being discussed? We know for a fact that it is a core dimension of our political system [and affects corporate governance]. Political financing is not transparent and accountable in any way [at this moment]," he says.