



MINORITY SHAREHOLDER WATCHDOG GROUP
Shareholder Activism and Protection of Minority Interest



Suruhanjaya Sekuriti
Securities Commission
Malaysia

PUBLIC RESPONSE PAPER

NO. 1/2014

**THE MALAYSIAN CODE FOR
INSTITUTIONAL INVESTORS 2014**

The Securities Commission Malaysia (SC) and the Minority Shareholder Watchdog Group (MSWG) are issuing this Public Response Paper in response to the feedback received pursuant to the Joint Public Consultation Paper on the Malaysian Code for Institutional Investors dated 15 January 2014.

This Public Response Paper is dated 26 June 2014

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1.0 INTRODUCTION

- 1.1 On 15 January 2014, the Securities Commission Malaysia (SC) and the Minority Shareholder Watchdog Group (MSWG) published a Joint Consultation Paper to invite public feedback on the Malaysian Code for Institutional Investors 2014 (Code).
- 1.2 The Code sets out broad principles of effective stewardship by institutional investors (IIs), followed by guidance to help IIs understand and implement the principles.
- 1.3 The Joint Consultation Paper was open for public feedback from 15 January 2014 to 28 February 2014. In addition, the MSWG also held focus group and presentation sessions with the industry which include fund managers, private pension fund providers and insurance companies.
- 1.4 MSWG received feedback from 19 respondents on the Joint Consultation Paper from individuals, academicians, professional advisory firms, legal firm, fund managers, insurance companies, government-linked investment companies as well as international governance organisations and regulators. MSWG and SC would like to thank all respondents for their comments.
- 1.5 Overall, the feedback was positive and the respondents were generally supportive of the Code and the proposed principles, albeit with some reservations on the mechanics of implementation and monitoring.
- 1.6 Feedback from the respondents on the Code, together with MSWG's comments, is presented in the following sections.

2.0 FEEDBACK ON SPECIFIC QUESTIONS

Respondents were asked to give comments on the following questions.

- a) *Are the principles of the Code sufficient to strengthen the accountability of II as envisaged in the CG Blueprint 2011? Are there other areas that should be included in the Code?*
- b) *Are the definitions provided clear and appropriate?*
- c) *Is the guidance provided under the respective principles adequate?*
- d) *The Code encourages its signatories to report annually on their application of the principles of the Code, and where there is non-observance of a principle; signatories are expected to provide meaningful explanation for the departure. Do you agree with this approach?*

Feedback from respondents

Generally, respondents held the view that the Code provided adequate guidance for II to exercise good governance. Their responses indicated that the set of principles were comprehensive and rigorous to further strengthen the accountability of IIs. Suggestions were made for the Steering Committee to consider addressing the themes on 'Independent Oversight', 'Remuneration Structures' and 'Capacity and Effective Management' in the Code.

Respondents were generally satisfied that the definitions were clear and appropriate, albeit with some suggestions for enhancements which will be discussed in the following section.

The guidance for the principles was adequate, although it was expressed that some elements may be too prescriptive and may not be suitable with II's current approaches.

Only one respondent did not agree with the 'comply or explain' approach for reporting on compliance with the Code. The concern raised was that, as long as there is a monitoring body (umbrella body) which will be monitoring the IIs' compliance to the principles of the Code, reporting on non-observance of the principles would be assured.

Additionally, it was proposed that the processes and procedures for II to be signatories to the Code should be described and the implications of not being one should also be addressed. Further, IIs should be given the option on whether to provide explanation on non-compliance in view that the Code is voluntary.

MSWG's Position

Respondents generally viewed that the principles of the Code provided adequate guidance for institutional investors to exercise good governance.

The Code is voluntary, nevertheless, it is expected that institutional investors should apply the principles of the Code in the interest of their beneficiaries. They are expected to explain how they have applied the principles and be guided by the explanations and their own stewardship principles in addition to reporting annually. A good take-up of the Code will encourage good governance and long-term sustainability of their investee companies which will also be expected to spur further development of the capital market.

3.0 FEEDBACK ON THE DRAFT MALAYSIAN CODE FOR INSTITUTIONAL INVESTORS

3.1 Definitions

There were suggestions for improvements on the definitions of certain terms such as “asset owners”, “IIs” and “stewardship”. Respondents also proposed that “investee companies”, “significant holdings” and “policies” should be defined to avoid misinterpretation of the terms as they were being spelt out throughout the Code. Additionally, “takaful operators” should be included as asset owners and “trustees” should be considered as one of the service providers.

The definition of “stewardship” should explicitly include environmental, social and governance (ESG) and sustainability issues along with other matters for IIs to monitor and engage the investee companies where emphasis should be given on the importance of integrating ESG factors in the stewardship activities.

Further, agents working on behalf of the collective investment vehicles, whether they are fund managers, custodians or other service providers, need to be held accountable for their delivery of appropriate services. These services should not be restricted only to areas covered under the Code. Hence, this issue should be addressed in the definition section because it relates to all agents that are potentially involved in the investment chains.

An observation was made on II who are only minority shareholders not holding substantial stake in any investee companies. Such institutional investors are unable to exert significant influence over the investee companies and a suggestion was made to reflect this observation in the definition of “IIs”.

3.2 Role of Institutional Investors

It was highlighted that there is a contradiction between the requirement for IIs to consider various economic considerations and sustainability issues in the investment decision-making process and at the same time indicated that the Code should not be used as an invitation to manage the affairs of the company.

3.3 The Malaysian Code for Institutional Investors

Respondents proposed to state from the outset that the Code is voluntary and implementation of the Code may require additional resources to ensure effective compliance, reporting and monitoring. The document would be more appropriate to be referred to as “Principles” or “Guidance” rather than a “Code”, at least at the initial stage until the document is widely accepted by IIs.

3.4 Application and Reporting

Respondents proposed the following on service providers’ application and reporting of the Code:

- At the initial stage of implementation of the Code, the service providers will not be made signatories but rather should be encouraged to apply, and disclose

how they have applied, the principles or guidance set out in the Code. This would be consistent with the approach taken in the Code where IIs should ensure that the service providers carry out their investment activities in line with the IIs' stewardship policies.

- Service providers should report on how their services enable their clients to achieve the latter's own stewardship objectives, citing a respondent's own experience in the United Kingdom where service providers struggled to report on some aspects of the stewardship code as they do not undertake engagement.

There were concerns on whether the applicability of the Code commensurate with the size of equity holdings in investee companies in view of the additional cost incurred for compliance.

It was proposed for examples to be provided in a separate document to illustrate how signatories may report on compliance with the Code. In addition, respondents sought clarification on the reporting timeline, i.e. the insurance industry associations proposed a moratorium period of two years for the industry to assess its ability to meet the Code's requirement.

3.5 Monitoring and Review

The board of signatories to the Code should be responsible for monitoring compliance with the principles, and any departure from the Code, as this would reinforce the voluntary nature of the Code.

It was proposed that any attempt to monitor compliance with the Code should only be carried out once it is widely accepted and only after further discussions and deliberation with the relevant stakeholders. Additionally, some felt that the monitoring of extent of compliance by licensed intermediaries should be assigned to the SC.

Clarifications were sought on the establishment of a monitoring body (umbrella body), as follows:

- its terms of reference, whether the umbrella body is envisaged to be established as a forum for IIs to exchange views or will it evolve to play a supervisory role to the IIs;
- its composition, whether members of the umbrella body should also include distinguished individuals who are not attached to IIs, to provide a more holistic perspective; and
- whether members of the umbrella body should rotate over a period of time to ensure wider representation and fresh perspectives;

MSWG's Position

Amendments have been made to the definitions to have more clarity. Takaful operators were included in the definition of asset owners while trustees were added as one of the service providers.

Additional resources or cost is expected to be minimal as many institutional investors were already implementing some of the principles.

Institutional investors are encouraged to become signatories and determine the best approach to apply the principles. In addition, institutional investors should also invest in a responsible manner and to the extent that they do not interfere in the day-to-day affairs of the company.

Service providers are not signatories to the Code. They are encouraged to disclose how they carry out the wishes of their clients with respect to each principle of the Code relevant to their activities.

Reporting and disclosure of the application will be in the Annual Report or website effective 2016. The board of signatories are expected to oversee and monitor the application of the principles of the Code. MSWG will report on the take-up of the Code on a broader basis.

3.6 Principle 1

IIs should disclose the policies on their stewardship responsibilities.

Feedback from Respondents	MSWG's Comments
Further guidance should be provided on the disclosure requirements. The form and manner of the policy disclosures should be prescribed.	Noted. Level of details on disclosure of policies is at IIs' own discretion. Nevertheless, further guidance could be provided if necessary.
Insurers sought clarification that meeting the minimum disclosure requirements to policy owners, as prescribed by respective regulatory regime, shall be deemed sufficient to meet compliance with the Code.	Noted. Further engagements with the respective industry associations will be undertaken to discuss implementation issues.
Guidance 1.2 on accessibility of IIs' policies may not be feasible as it suggested that IIs should communicate the policies to investee companies and also monitor the compliance of those policies, which consequently means additional resources are needed. In addition, investee companies may have various policies from various investors to govern them.	Noted. An overall stewardship policy of the organisations could be disclosed as a start.
Whether IIs should have policies in place on how to initiate, act and disclose the appropriate level of outsourcing details.	Yes. Such policies should be put in place by IIs.
There were concerns on disclosing commercially sensitive information when IIs disclose the content of their investment mandates. Explaining the general selection criteria is sufficient.	Agreed. Such explanation would be useful to the ultimate beneficiaries and clients.

3.7 Principle 2

IIs should monitor their investee companies.

Feedback from Respondents	MSWG's Comments
<p>There are concerns that, while undertaking the monitoring process, IIs may be privy to information which may not be publicly available and subsequent actions taken by the IIs based on the information may be construed by others/regulators as insider trading/market manipulation.</p>	<p>Noted. Monitoring should be conducted based on publicly available information only. Policies and internal processes by institutional investors on handling non-publicly available information should be in place to address such issues. Ideally, it should be publicly disclosed.</p>
<p>IIs should be allowed to delegate the monitoring activities to licensed fund management companies.</p>	<p>Agreed. Asset owners can delegate monitoring activities to their asset managers. However, the responsibilities on stewardship matters still lie with the asset owners.</p>
<p>The quality of the management discussion and analysis, financial reporting, risk management and dividend policy should be added into the factors in Guidance 2.2 to make the monitoring process more comprehensive.</p>	<p>Agreed. Guidance 2.2 has been amended as proposed.</p>
<p>Suggestion from the insurance/takaful industry that acceptable minimum monitoring criteria should be discussed with the respective industry associations.</p>	<p>Noted. Further engagements with the respective industry associations will be undertaken to discuss implementation issues.</p>
<p>The requirement to establish a focus list to target underperforming companies is too prescriptive.</p>	<p>Noted. The requirement has been deleted.</p>
<p>The investee company's board should be informed in writing if the IIs do not agree with the position taken by investee companies or their explanation on the application of the <i>Malaysian Code on Corporate Governance 2012</i> (MCCG 2012), together with its reasons.</p>	<p>Agreed. Guidance has been amended as proposed.</p>

<p>Guidance 2.5 should not specify that communication between IIs and investee companies be made '<i>ideally in writing</i>', as it may not always be the most ideal form of communication when informing companies of voting decisions.</p> <p>In addition, IIs should be encouraged to make such communication even when they vote for and should not be limited to when they vote against management or abstain from voting.</p>	<p>Agreed. Guidance has been amended as proposed.</p>
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3.8 Principle 3

IIs should engage with investee companies as appropriate.

Feedback from Respondents	MSWG's Comments
<p>IIs must observe market abuse rules and not seek trading advantage through possession of price sensitive information when engaging with their investee companies. IIs may come into possession of price sensitive information through engagement with its investee companies not only on governance issues but also on matters relating to the performance of the company.</p>	<p>Agreed. The phrase "about governance issues" has been deleted.</p>
<p>Various factors should be considered before engaging with investee companies, particularly the size of equity holdings, to determine the necessity of engagement as an extension to IIs' monitoring activities.</p>	<p>Noted. IIs should apply the principles of the Code based on specific circumstances of individual companies and their markets.</p>
<p>There are certain limitations with regards to the voting rights of unit trust fund managers and trustees as stated in the <i>Guidelines of Unit Trust Funds</i>.</p>	<p>Noted. Further engagements with the respective industry associations will be undertaken to discuss implementation issues.</p>
<p>IIs to have discretion to decide the best approach to its own investment strategies and applicable regulatory regime. For example, in Guidance 3.4, insurers are concerned as the guidance appears to list a few "must do" steps or else the IIs may be deemed as non-compliant with the Code.</p>	<p>Noted. Guidance 3.4 sets out the examples of various actions that IIs could take to make their concerns known to their investee companies and discretion is given to the IIs to decide on the best approach to its own investment strategies.</p>
<p>IIs should have other reporting avenues if the companies do not have a website or do not publish an annual report</p>	<p>Noted. The disclosure could be made on the monitoring body's website.</p>
<p>Guidance 3.5 which reads, "<i>in extreme circumstances, IIs may feel it appropriate to seek damages through legal remedies or arbitration</i>", may not reflect good stewardship.</p>	<p>Noted. This recommendation has been deleted.</p>

3.9 Principle 4

Its should adopt a robust policy on managing conflict of interest which should be publicly disclosed.

Feedback from Respondents	MSWG's Comments
<p>Illustrations on conflicts of interest scenarios and solutions to address such conflicts should be provided in a "Frequently Asked Questions" section/document.</p>	<p>Noted. Illustrations could be provided in the future by the monitoring body.</p>
<p>The policy on managing conflict of interest need not be publicly disclosed and should only be made known internally. Such policy encompasses not just conflict of interest in investments but also internal matters.</p>	<p>The policy should ideally be disclosed for the benefit of beneficiaries and client as regards investor stewardship matters.</p>
<p>A standard guidance should be developed at industry association level on managing conflicts of interest as currently there are different requirements under the <i>Financial Services Act 2013</i> and <i>Islamic Financial Services Act 2013</i>.</p>	<p>Noted. Further engagements with the respective industry associations will be undertaken to discuss implementation issues.</p>

3.10 Principle 5

IIIs should incorporate corporate governance and sustainability considerations into the investment decision-making process.

Feedback from Respondents	MSWG's Comments
<p>The Code should apply ESG issues to all stewardship activities and not just in the investment process.</p>	<p>Noted. We are of the view that that this should be a stand-alone principle to encourage incorporation of CG and sustainability issues into the investment decision-making process for a start, which is part of the stewardship role.</p>
<p>The disclosures under Guidance 5.2, which requires IIIs to assess the quality of disclosures made by investee companies on the application of the MCCG 2012 should include:</p> <ul style="list-style-type: none"> • disclosure of board nomination and performance evaluation • risk management and internal controls • the composition and quality of the board 	<p>Noted. Guidance 5.2 has been amended as proposed.</p>
<p>More details should be provided for each of the ESG factors in the "Frequently Asked Questions" section/document or a separate guide to aid IIIs' understanding on the subject matter.</p>	<p>Noted. Illustrations could be provided in the future by the monitoring body.</p>
<p>The specific industries to be exclusionary screened under Guidance 5.5 should not be listed down as it may be seen as a discrimination against those industries. Disclosures by IIIs on which industries that they do not invest in is sufficient.</p>	<p>Agreed. Guidance 5.5 on exclusionary screening has been deleted.</p>

3.11 Principle 6

IIs should publish a voting policy.

Feedback from Respondents	MSWG's Comments
The policy should only be made known internally.	We believe that the voting policy should be published to give the beneficiaries and investee companies a better understanding of the criteria used to reach the voting decisions.
Clarifications were sought on the implementation of voting policy on fund managers and whether a general voting policy is sufficient for insurance companies.	Further engagements with the respective industry associations will be undertaken to discuss implementation issues.
The most appropriate person to write to with regards to voting decisions would depend on the type of resolution and other factors, which may not necessarily be the chair or company secretary of the investee company.	Noted. Guidance 6.3 has been amended as proposed.
IIs should not need to explain to the investee companies the reasons for voting against or abstaining at the general meetings.	We are of the view that an explanation should ideally be given so that beneficiaries and investee companies have a better understanding of the criteria used to reach the voting decisions.
IIs should be allowed to form their own proxy voting guidelines on resolutions that are deemed relevant for them to vote.	Agreed.
<p>Comments on the threshold for active voting:</p> <ul style="list-style-type: none"> • Definition of 'threshold' is not provided which poses a challenge with regards to the practicality of exercising the voting rights by IIs, particularly with small equity holdings who might not be able to influence the decisions in the general meetings. • The recommendation on setting a threshold for active voting may be too prescriptive. It should be up to investors whether to set such threshold or not. 	Noted. Guidance 6.4 has been amended to include that threshold for active voting would be at the IIs' discretion.

<ul style="list-style-type: none"> • IIs should not be required to have a policy on threshold for active voting. 	
<p>Guidance 6.5 should be strengthened to encourage not just a summary of voting activities but actual disclosure of each vote.</p>	<p>Agreed. For a start, IIs are encouraged to disclose a summary of their voting activities.</p>
<p>An example or a scenario on IIs' work with other relevant parties to remove barriers of voting should be provided in a "Frequently Asked Questions" document or its equivalent.</p>	<p>Noted. Illustrations could be provided in the future.</p>
<p>A guidance which requires IIs to demand for voting by poll for all resolutions should be included.</p>	<p>Agreed. We are of the view that this should be determined by IIs.</p>
<p>The term more commonly referred to in Malaysia should be used in place of "<u>stock</u>" lending or recall lent "<u>stock</u>" in Guidance 6.8, such as "<u>securities</u>" or "<u>shares</u>".</p>	<p>Noted. Guidance 6.8 has been amended as proposed.</p>

3.12 Principle 7

ILs should consider acting collectively with other investors where appropriate.

Feedback from Respondents	MSWG's Comments
<p>Those who were not in favour of the principle argued that:</p> <ul style="list-style-type: none"> • Acting collectively with other investors could be deemed as acting in concert to manipulate the market. • Clear policies on collective engagement are difficult to establish as it is done on a private and case-by-case basis. • An II's investment objectives may not be aligned with the objectives of other IIs. Hence, collective engagement may not be relevant in all circumstances. • Guidance may be required from bodies such as the Malaysian Competition Commission to ensure to what extent a collective engagement may be considered anti-competitive. 	<ul style="list-style-type: none"> • Based on further deliberation at the Project Steering Committee and Working Group levels, Principle 7 is now deleted and instead moved to the Preamble of the Code. • While this is no longer a principle in the Code, the fact remains that IIs must be aware and cognisant of market regulations with regard to acting in concert and market manipulation.
<p>Regulatory authority should be given the power to exercise discretion to waive compliance to the principle of collective engagement if it could affect market efficiency or fairness.</p>	<p>Noted.</p> <p>IIs must be aware and cognisant of market regulations with regard to acting in concert and market manipulation.</p>
<p>For information only – the European Securities Market Authority has recently issued a statement setting out a “white list” of issues on which investors can usually engage collectively without raising concerns that they are acting in concert.</p>	<p>Noted.</p>

3.13 Principle 8**IIs should engage in the development of relevant policies and best practices.**

Feedback from Respondents	MSWG's Comments
This principle may not be feasible as it may be beyond the IIs' control.	Agreed. Based on further deliberations at the Project Steering Committee and Working Group levels, Principle 8 is now deleted and instead moved to the Preamble of the Code.

APPENDIX**LIST OF RESPONDENTS**

NO.	ORGANISATIONS
1.	BPA Australasia Sdn Bhd
2.	Bursa Malaysia Bhd
3.	CorpGov.net
4.	Eastspring Investments Bhd
5.	Employees Provident Fund (EPF)
6.	Federation of Investment Managers Malaysia (FIMM)
7.	Financial Reporting Council, United Kingdom (FRC)
8.	Great Eastern Takaful Sdn Bhd
9.	Hermes Equity Ownership Services
10.	International Corporate Governance Network (ICGN)
11.	Kenanga Investment Bank Bhd
12.	Kumpulan Wang Persaraan (Diperbadankan) (KWAP)
13.	Lembaga Tabung Angkatan Tentera (LTAT)
14.	Lembaga Tabung Haji (LTH)
15.	Messrs Jeff Leong, Poon & Wong
16.	Organisation for Economic Development and Co-operation (OECD)
17.	Persatuan Insurans Am Malaysia (PIAM)
18.	Prof Dr Aiman Nariman Mohd Sulaiman (IIUM) & Assoc Prof Dr Shanty Rachagan (Monash University Malaysia)
19.	The Malaysian Institute of Chartered Secretaries and Administrators (MAICSA)

LIST OF ORGANISATIONS WHICH ATTENDED THE FOCUS GROUP SESSIONS

NO.	ORGANISATIONS
1.	Amanah Saham Nasional Bhd
2.	BIMB Investment Management Bhd
3.	CIMB-Principal Asset Management Bhd
4.	Federation of Investment Managers Malaysia
5.	Hwang Investment Management Bhd
6.	KAF Investment Funds Bhd
7.	Kenanga Investors Bhd
8.	Malaysian Association of Asset Managers
9.	Pheim Unit Trust Bhd
10.	Phillip Mutual Bhd
11.	Private Pension Administrator
12.	Public Mutual Bhd
13.	UOB Asset Management Bhd
14.	AXA Affin Life Insurance Bhd
15.	AIA Insurance Bhd
16.	Etiqua Insurance Bhd
17.	Prudential Assurance Malaysia Bhd
18.	Tokio Marine Life Insurance Malaysia Bhd
19.	UNI.Asia Life Assurance Bhd
20.	Zurich Insurance (M) Bhd