Corporate governance in malaysia ; us

Business, Corporate Governance

TheFinanceCommittee Report defined Corporate Governance as “ the process and structure used to direct and manage the business and affairs of the company towards enhancing business prosperity and corporateaccountabilitywith the ultimate objective of realizing long-term shareholder value, whilst taking into account the interest of other stakeholders”. Over the years, corporate governance has received enormous attention as a result of high-profile corporate scandals involving the exploitation of corporate power and alleged criminal activity by corporate officials themselves.

Classic examples include Enron, WorldCom, Xerox and Tyco are some unforgettable foreign exemplary models, and even in Malaysia, we are not totally excluded in these predicaments, cases such as Axis Inc Kenmark, Silverbird, Renong and of course, the infamous Transmile corporate scandal. This report will basically look back into the development of corporate governance in Malaysia and the US while at the same time critically compare the state of corporate governance in these two countries. 2.

0LITERATURE REVIEW 2. 1The development of Corporate Governance in Malaysia Corporate governance has come a long way mainly due to market impacting factors such as corporate failures, corporate losses, scandals, economic turmoil as well as demand from stakeholders. The Asian financial crisis has been an eye opener to policy makers as weaknesses were clearly evident in the corporate governance structure. The crisis has led to the collapse of numerous prominent organizations across the country.

As a result, a number of initiatives have been made by the Malaysian government to restore investor confidence through the strengthening of corporate governance framework and improving the quality of corporate management practice. The High Level Finance Committee was established in 1999 under the Ministry of Finance to review and address the corporate governance issues in the aftermath of the Financial Crisis (Nor Azizah & Halimah, 2007).

According to Das (2000), the Committee has identified weaknesses particularly in requirement transparency and disclosure, corporate monitoring responsibilities and accountability of company directors including the rights of minority shareholders. A report was later issued by the committee that marked the beginning efforts by regulators who worked hand in hand with industry expert to promote sound corporate governance. The Committee recommendations has resulted in significant improvement to the Kuala Lumpur Stock Exchange (KLSE) Listing Requirements (Singam, 2003).

Bursa Malaysia formerly known as KLSE together with Security Commission had imposed that public listed companies were required to disclose their financial status, loan position and shareholders structure on a quarterly basis. Consequently, the Malaysian Code on Corporate Governance (Code) was introduced in 2000, which meant to encourage transparency in company management while providing relevant information to the investors to achieve company's objective.

In 2007, a revision had been made to the Code to address the function of internal audit and to reinforce the roles andresponsibilityof board of directors and audit committee. The Minority Shareholder Watchdog Group (MSWG) was established in 2000 by five government fund institutions namely Employees Provident Fund (EPF), Armed Forces Fund Board, National Equity

Corporation (PNB), Social Security Organisation (SOCSO) and Pilgrimage Board (Lembaga Tabung Haji). The MSWG is part of the initiatives to safeguard the interests of minority shareholders through shareholder activism (MSWG, 2012).

The Securities Commission’s five years Corporate Governance Blueprint was launched in 2011 to provide an action plan in improving the corporate governance standards by strengthening self and market discipline on top of promoting greater internalization of good governanceculture. The Blueprint contains 35 recommendations and is divided into six main areas which consist of Shareholder rights, Role of institutional investors, The board’s role in governance, Disclosure and transparency, Role of gatekeepers and influencers and Public and private enforcement (Blueprint, 2011).

As part of the Blueprint key deliverable, the Malaysian Code on Corporate Governance 2012, which supersedes the 2007 Code was introduced in April 2012 (MCCG, 2012). The updated Code sets a more specific recommendation which organizations should implement as an essential part of the business dealings and culture. Over the years, Malaysia has progressively strengthened the companies’ laws and regulations to protect investors’ interest.

Although numerous efforts have been taken by the government and regulators, good governance can only be achieved through active enforcement of corporate governance culture in listed companies as well as within the entire ecosystem. Stakeholders should take full responsibility of their decisions and actions in order to protect the interests of the shareholders and to promote shareholder value. 2. 2The development of

Corporate Governance in the US History reveals that corporate governance first emerged in the US and only started to gain popularity in the 1970s.

The US is often view as a point of reference for shareholder-oriented corporate governance for many countries around the world. The research by Jackson G. (2010) illustrated that the characteristics of US corporate governance model are widely quoted as best practices or even a global standard for good corporate governance. In the US, audit committees have always been an essential part in assuring greater corporate accountability and it is a requirement for New York Stock Exchange (NYSE), American Stock Exchange, and National Association of Securities Dealers (NASDAQ/NMS issuers).

NYSE has officially issued a white paper in 1973 that strongly recommends each listed company to form an audit committee. Only in 1977, NYSE audit committee policy made it compulsory for each domestic corporation listed on the exchange to establish and maintain an audit committee of outside directors (Audit Committees, 2012). The most severe corporate and financial scandals of the US eroded during the 1990s, and into the new millennium.

The first major indicator occurred in 2001, the Enron Scandal that is considered one of the most notorious and largest bankruptcy reorganization within US history at that time (before being surpassed by Worldcom's bankruptcy the following year). The scandal also leads to the downfall of Arthur Anderson that was once one of the " Big Five" audit firms (Bratton, 2002). In 2002, just six months later after the Enron Scandal, Worldcom an American telecommunication company, filed for Chapter 11 bankruptcy protection which is the largest filing in the US history at that point of time (Wikepedia MCI Inc. , 2012). Scandals surrounding Enron and Worldcom focused considerable criticism on the US corporate governance. The US government reacted to the wave of wrongdoing by endorsing the most comprehensive corporate-reform law, the Sarbanes-Oxley Act of 2002 (SOX) and the modification of the New York Stock Exchange and NASDAQ listing rules which require the boards of listed firms to have majority of independent directors (HOLOPAINEN, 2006).

SOX is required by law, rather than ‘ comply or explain’. Among the areas of focus was the setting up of Public Company Accounting Oversight Board (PCAOB) to provide independent oversight of public accounting firms providing audit services. SOX also established standards for auditor independence and to limit conflicts of interest. It also restricts auditing companies from providing non-audit services (e. g. , consulting) for the same clients.

Despite the implementation of SOX, US Corporate Governance came to question again during the Global Financial Crisis (GFC) of 2008-2009 as more scandals were uncover, including that of Bernard Madoff (Ponzi Scheme) and Lehman Brothers (filed for Chapter 11 due to losses from sub-prime mortgages), Bear Stearns (losses from mortgage backed securities and rescued by JP Morgan) and the mother of all, the US$182 billion bailout of AIG (losses due to credit default swaps related to subprime mortgages).

This called for new global financial market architecture that could provide protection for investors, shareholders and other stakeholders and to avoid the “ too big to fail” syndrome. In addressing this challenges, the Dudd-Frank Act, 2010 was introduced to promote financial stability in the US by improving accountability and transparency in the financial system, to end " too big to fail", to protect the American taxpayer by ending bailouts, to protect consumers from abusive financial services practices. 2. 3The state of Corporate Governance in Malaysia and the US

The history and development of corporate governance, like other historical processes, is path dependent. Malaysia has adopted the shareholder model which is very similar in principle to the US model where the main objective is to protect and maximize shareholder value. The similarity include ‘ the significance of equity financing, the primacy of shareholders as beneficiaries of fiduciary duties, dispersed share ownership among uncommitted shareholders, active markets for corporate control as a mechanism of managerial accountability and flexible labor markets’.

We will now look into the dissimilarity as well as the similarity in corporate governance between Malaysia and the US. 2. 3. 1Corporate Governance Rules In the US compliance to the corporate governance is mandatory and required by law. However, in Malaysia it is 'comply or explain’. Public Listed Companies (PLC) are encouraged to adopt the MCCG recommendations that are constructed based on best practices. Nevertheless if a PLC chooses not to implement the recommendation, the PLC should disclose this in their annual reports together with an explanation (MCCG, 2012).

This approach will allows PLC to be more focus in implementing the controls that is deem suitable to their organization instead of adopting all requirements as required by the US system which may lead to fines and imprisonment penalties if the SOX requirements are violated. This is the most significant distinction between Malaysia and the US corporate governance. 2. 3. 2Independence of the Board To effectively evaluate the performance of an organization, independence of the board is essential in ensuring there is no conflict of interest or undue influence from interested parties.

Board should have sufficient number of independent directors to ascertain that no single team or party can dominate the decision making process. According to Xie and Dadalt (2003) practice of corporate governance improve with the higher percentage of board independence or the greater proportion of outside director. In order to accomplish this, Malaysia Listing Requirements prescribed that there should be at least two board members or one-third of the board members, whichever is higher. As for the US listing rules, it requires that a majority of directors are independent non-executives, excluding the chairman to be on the board.

In term of board tenure in the US, the impact is stronger on the length of non-executive terms than the previous rule. According to Mayo (2003), any director that has served over more than six years will be subject to a thorough review to determine if there is a compromise of independence during the years of service. In addition, to have a limit to the directors' tenure will restrict the directors' ability to use their tenure as a means of power to influence others on the board or the potential to build an empire. There is an emergence of at least 50% or more independent directors in Malaysia over the years.

Nevertheless, some of these independent directors have overstayed their welcome as about 13% of the surveyed companies had these directors serving the board for more than 12 years. This clearly does not reflect well as it is not easy for a director to maintain his independence for a long time. Thus MCCG recommends that independent director tenure must not exceed a cumulative term of nine years. In Sime Darby, the board made up of 13 members comprising all-non executive Directors except the President ; Group Chief Executive.

6 of the Directors are independent as defined under the Bursa Malaysia Securities Berhad Main Market Listing Requirements (Listing Requirements). Most of the board members have served less than 5 years and yearly re-election of the directors as reported in the 2011 annual report. As for Sapura Resources, the board has an effective composition of 8 directors comprising 7 non-executive directors, (including the Chairman) of whom 5 are Independent, and a Managing Director thus they are also in compliance with the MMLR of Bursa Malaysia requirement.

However, Sapura Resources is afamilyowned business where the chairman is also the founder of Sapura Group and has a family relationship (father-son) with the managing director as well as one of the non-Independent Non-Executive Director. Thus to limit the tenure to 9 years in a family owned PLC is not viable. 2. 3. 3Separation of Chairman and CEO Another significant distinction between the corporate governance state in the US and Malaysia is CEO authority and power in listed companies. For a majority of US companies, they have adopted CEO duality where the CEO is

also the Chairman within the board. This however has instilled some doubt on the genuine independence of other board members (Jackson, 2010). On the other hand, in Malaysia majority of listed companies including Sime Darby, Media Prima, Sapura Resources and others, has separated the role of

Chairman and CEO, as recommended by the CG Code. The code however recognizes that where the roles are combined there should be a strong independent element on the board and a decision to combine those roles should be publicly explained and disclosed. 2. 3. 4Composition of the Board

A set of skills, knowledge, competencies including diversity of perspective and experience are crucial to cope with the complexities, competition and changes in order to strengthen the board composition by having the right mix of members. In the US, the Sarbanes-Oxley Act only requires that the listed company disclose if there is an expert or not. As for the audit committee composition, it should be composed completely of independent directors and the company should only disclose whether at least one member of the committee has financial expertise (Jackson, 2010).

In Malaysian context, the boards must ensure the right combination of board members with the sufficient and suitable skills, and experience to cope with the CG code requirements. For example in Sime Darby, the board members are consist of industry experts with vast experience and impressive curriculum vitae ranging from chartered and certified accountants, solicitor advocate, commercial lawyer and many more. Diversity could be sighted in the board composition as it includes gender diversity, race, culture and nationality.

The SDP Board is assisted in its oversight function by Board Committees. These committees comprised of Governance ; Audit Committee, Nomination ; Remuneration Committee, Risk Management Committee, Litigation Committee, Tender Committee, and Investigative Reports Review Committee which operate within its Terms of Reference that clearly defines its functions and responsibilities. Most of Media Prima board members have an extensive experience especially in the advertising, strategic Marketing and corporatecommunication.

On top of that, expertise in finance, accounts, legal and business administration are reflected among the board members. The Media Prima board delegates the term of reference and responsibilities to the board committees which consist of Audit Committee, Risk Management Committee, Nomination Committee, Remuneration Committee and EMPLOYEE’S SHARE OPTION SCHEME (ESOS) Committee. The committees role are only limited to making recommendations where they have no authority to make any decisions (Media Prima, 2011).

Media Prima effort and commitment in instilling good Corporate Governance are proven as they received numerous accolades including Malaysia Corporate Governance Index 2011 from MSWG, Best Overall for Corporate Governance and Best for Disclosure ; Transparency from AsiaMoney’s Corporate Governance Poll 2011 and many more. 2. 3. 4Gender Diversity Board diversity is one of the most debated topics around the world including in Malaysia and the US, focusing on the need to have more women on board.

Even in this era, there is still resistance to the status quo of all-male boards but it is slowly changing. Most of the interviewees agreed that there should be at least one woman on board as lady are more meticulous, have an eye for detail and more cautious in decision making. Sitting on board will definitely help to ensure the reports and business decisions are meticulously reviewed Board diversity in the US is still the same since 2009 and has not moved with women holding approximately 16% of board seats of Fortune 500 companies, where there is only increase of less than 1%.

A study conducted by Corston-Smith Asean-5 on Gender Diversity reveals that more than half of the companies listed on Bursa Malaysia still do not have a single woman director. This shows that women's today are still hitting the glass ceiling despite more of them being better-educated. The study performed a regression analysis to observe the connection between women percentage on boards with company's performance.

The performance indicators include revenue, market capitalisation, earnings per share, net profit, return on equity (ROE) and return on assets. The result interestingly point that all six variables are positively correlated with female representation on boards for listed companies in Malaysia. Similar results have been reported in other countries thus there is clear financial proof that women directors contribute positively to effectiveness of a company's performance. 3. 0CONCLUSION & RECOMENDATION

Although numerous measure has been taken by Malaysian regulators to enhance the corporate governance, level of in-depth study done via comprehensive research is left to be desired as most of the recommendations were made via consultative methods. Even so, level of enforcement and implementation, although improving is still lacking as the arms of the law falls short on scandals after scandals. While Malaysia has come a long way in introducing good corporate governance practices, it can still be said that we lack far behind in terms of implementation as governance policies or recommendation are only in form and not in substance.

Unlike the SOX2002 in the US, Malaysia's MCCG2007 an MCCG2012 lacks bite as adaptation of the recommendations are voluntary. Nevertheless, there are some provisions which were made compulsory via Listing Requirements and amendments to the Company's Act, 1965. Furthermore, unlike the US, where the corporate governance practices evolved via established reports made available for regulators to implement, the Malaysian case was rather short-sighted as only a handful of individuals were consulted in drafting the Code.

Another lacking point in Malaysia is while the Blueprint called for 35 recommendations but only 23 were adopted while 12 others were recognized but will only be decided upon after either a Task Force or a Working Group is able to come up with more concrete proposals. Among the 23 adopted, only 3 of the recommendations were adopted to be recognized via amendments to various governing acts while other were made via Listing Requirement and in the new MCCG2012. Another area of concern remain are level of independence of independent directors.

How independent can they be if they overstay their welcome? In our opinion, independent directors should no longer be appointed by the companies via the Nomination Committee but the task to be hand over to another body (preferably regulatory) to appoint independent directors for listed companies. One of the interviewees suggested that the term of office too should be limited to just 3 years mainly to maintain their independence and these independent directors can be rotated among similar industries.

However, there is also an argument that senior board members with strong personalities with good corporate memory are extremely vital and valuable for corporate continuity especially in a family owned business. To address this, company should consider changing the role from being independent to non independent for people who have been serving on board for a long time. Appropriately, level of independence among advisers including the auditors should be question and to address the shortcoming, a similar institution should be tasked to appoint auditors and advisers for all listed companies.

In term of gender diversity, there should be a buy in from the chairmen and CEOs of Malaysia PLCs where they should include the set of skills required in a women directors in order to join and add value to their companies' board. As of now, there is a positive formation of a women director’s registry and government funding for women directors training after the announcement to have 30% women on corporate board by 2016. We believe important criteria based on values, principles and skills are necessary form of measures that independent directors ought to possess.

A survey done in the UK based on what criteria(s) are important includes the following; integrity, listening skills, motivationof others, persuasiveness, motivation, resilience, decisiveness, determination, sensitivity and energy. All these values should be inculcated and practised. As means of enabling transformation to happen, we feel that the Blueprint 2011 has a sense of noble and just cause in ensuring what is right and good. Change is inevitable and the change of the mindset is perhaps a first step towards embracing the culture of good corporate governance to ensure that our market has high integrity and well regarded by investors.