

## Client Alert

July 2016

### Proposed Draft of the Malaysian Code on Corporate Governance 2016

The Malaysian Securities Commission (“SC”) released a draft of the Malaysian Code on Corporate Governance 2016 (“**2016 Code**”) for public consultation. It is intended that the 2016 Code will supersede the Malaysian Code of Corporate Governance 2012 (“**2012 Code**”). The 2016 Code, if adopted, will herald a shift towards a greater emphasis on raising the standards of good practice in relation to board leadership and effectiveness, remuneration, risk management, accountability and relations with shareholders.

Under the 2016 Code, two categories of practices are identified, namely *Core* and *Core+* practices. These practices are classified under 4 broad principles:

- Supporting board leadership and effectiveness;
- Safeguarding the integrity of financial and corporate reporting;
- Managing risks to preserve and create value; and
- Strengthening relationship with shareholders.

#### Compliance with the 2016 Code

In contrast to the 2012 Code which operates on a ‘*comply or explain*’ basis, the 2016 Code adopts the ‘*apply or explain an alternative*’ approach. Going forward, where companies will be required to provide clear and meaningful explanation on how they have adopted the *Core* practices, and achieved the intended outcome of each practice. Companies which do not adopt the *Core* practices must provide clear explanation for the non-adoption of the practice and an alternative which is able to fulfill the intended outcome.

The adoption and implementation of the *Core+* principles are encouraged.

#### Key Changes

The 2016 Code introduces the following new recommendations to enhance the corporate governance framework.

##### Nomination, Election and Assessment

The cost in identifying suitable candidates to take office as directors looks likely to increase. The 2016 Code encourages the board to appoint an external independent service provider or advisor to identify candidates for the nomination of non-executive directors.

For appointment and re-appointment of directors, the company should disclose in the Notice of General Meeting reasons for the board's support of the appointment or reappointment of the particular director and how the skills and experience of the director contributes to the needs of the company. Any appointment or re-appointment of directors would no longer be undertaken as a matter of process, but will require deliberation and reflection by the

Nominating Committee and the board as to the "value add" that the candidate will bring to the board. The evaluation will also be supplemented by results of the regular assessments that are to be undertaken on the performance of the board, its committees and individual directors.

#### Remuneration

Consistent with the global scrutiny on remuneration, companies will need to establish policies and practices regarding the remuneration of directors and key senior management. These policies and practices will need to be able to withstand scrutiny as the remuneration of individual directors on a named basis will be made public. This dovetails with the requirement under the Companies Bill (which is anticipated to come into force at the end of 2017) where the service contracts of directors will be open for inspection by substantial shareholders.

#### Shareholder Participation

The constructive participation of the shareholders at meetings is regarded as an important element in improving governance. Shareholders will going forward be provided with 28 days to review the Notice for the Annual General Meeting. Similarly, with the requirement for all listed entities to have a dedicated investor relations function, it is anticipated that shareholders will have greater access to the company.

### **Core+ Practices**

In addition, the 2016 Code introduces several *Core+* recommendations on companies to:

- inform shareholders in advance of general meetings on potential vacancies of directorships and allow shareholders to nominate a candidate to the Nominating Committee for consideration;
- disclose the relationship between 'pay and performance' for the remuneration packages of executive directors and senior management;
- engage professional and independent parties to conduct a formal board evaluation at least once every three years;
- establish a policy of rotating its external audit firm;
- adopt integrated reporting based on a globally recognised framework (e.g. the Integrated Reporting Framework by the International Integrated Reporting Council); and
- adopt the elements embodied in internationally recognised risk management standards or frameworks (e.g. ISO 31000:2009).

While not compulsory, companies are also strongly encouraged to adopt the *Core+* practices and disclose in the annual report how practices are being undertaken or implemented.

### **Conclusion**

The 2016 Code enhances the existing recommendations (relating to the nomination, election, remuneration and assessment of directors) contained in the 2012 Code. The introduction of a new principle designed to strengthen the relationship between the company and its shareholders is in line with the SC's commitment to promoting investor confidence in the capital markets.

Notwithstanding that the SC has not provided any indication on the expected timeframe for finalisation of the 2016 Code, listed companies in particular are encouraged to take note of the proposed changes to the framework so as to facilitate the transition to the new principles once in force.