

Proposing a Solution to the Issues of Acquiring Transparent Information on Corporate Governance Practices in Malaysia

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Abstract

Corporate governance in Malaysia has been a relatively new topic with only having established its first code in the year 2000. Efforts were made to improvise the local corporate governance code in 2007 & 2012. However, greater efforts are needed so that the interests of the shareholders are well protected and hence are able to make better investment decisions. Looking towards the western countries and the neighbouring countries, corporate governance has been a vigorously practiced phenomenon and companies have to be very transparent about their operations, especially the on-goings of the Board. Organisations were established to provide data and information to the general public about the above and their efforts of measuring governance practice of corporations has been welcomed by the majority of investors. However, when looking into the Malaysian context, there are hardly any organizations that follow a similar duty. Information can only be found in annual reports and Bursa Malaysia, which, apart from experts, is useless to the naïve investor. This paper discusses a concept to bring about a solution to this issue and adapts, to a certain extent, the better ideas realised in the west and improvise and fit them into the local scenario. The solution shall provide information and detailed analysis of corporations in Malaysia and their corporate governance practices. To achieve this, previous systems and tools shall be analyzed in a broad perspective to conceptualize the main framework of the solution.

Keywords: Corporate Governance, Malaysian Public Listed Corporations, Information Systems, System Analysis and Design

INTRODUCTION

Corporate Governance has been evolving throughout the ages of industrialization. From the start of the first companies, corporate governance has been the quintessential form of running a company and managing it. With the introductions of new financial and economic models, corporate governance has become an essential part of the framework of corporations. With the market economy system and capitalism in place as first brought about the likes of Adam Smith and other economists during that era, companies have

expanded from sole proprietorships to fully fledged corporations, in other words known as public listed companies.

With the rise of opportunities to acquire greater wealth by the already wealthy, a certain group of individuals whom discovered ways to acquire such wealth went on to make headlines in the 90s and during the new millennium. Those are the C-class executives and managers delegated by the wealthy owners to expropriate the money of the average shareholder and make multitudes of green notes in any way possible. That is what really happened with the likes of Enron, Arthur Anderson, Tyco and many other notable, and once respectable, organisations (Colley Jr, Doyle, Logan, & Stettinus, 2005) and (Solomon, 2010). For the more responsible corporations, these opportunities meant that every shareholder gets a portion no matter what social status that persons belongs to. These turn of events caused upheaval throughout the business world and even the public whom were directly and indirectly involved were affected. With media bringing these scandals into the spotlight and publicly defaming the corporations, governments and regulatory bodies had to work to curb the chances of such happening again. Increased suspicions in the day to day operations of corporations had raised questions as to whether the whole corporate system was to blame for the failures of a few. Even investors grew weary of giving good confidence votes to their own investments (Colley et al., 2005). With that, *Corporate Governance* was finally brought out into the open for the world to see and stringent measures were placed upon corporations to abide by the codes and acts formulated to keep such scandals at bay and increase transparency of corporate operations.

In order to ensure that Malaysian investors be able to access information related to corporate governance as practiced by listed corporations in Malaysia, this study focuses on the issue of accountability and transparency of corporations by acquiring information from annual reports of listed companies and placing it in a system whereby it will compute the scores of corporate governance quality of the listed companies. Since the tool is aimed at institutional investors, the need to understand the investor's outlook on corporate governance has become an important sector as wise investment decisions can only be made when one knows fully about whom they place their money with.

As of date, there is a lacking in information that can be extracted from literature on the factors that institutional investors in Malaysia weigh in relation to corporate governance prior to investing. This gap will be addressed in this study as it is a necessity to understand end-user requirements.

CORPORATE GOVERNANCE

Corporate governance has been observed and defined from various angles and has been refined over the years due to the dynamic nature of the marketplace and therefore, of corporate governance itself. Based on the Cadbury Report (Committee, 1992) corporate governance is merely about directing and controlling the company. However Keasey and Wright (Keasey & Wright, 1997) have expanded that idea further by bringing in the terms of 'supervision' and 'monitoring' the performance of the management so as to improve the overall performance of the firm and in turn, also being accountable to shareholders and stakeholders.

Colley *et al.* (Colley et al., 2005) mentioned that the whole system, from the election of the board to the appointment of the CEO and then the CEOs responsibility in maintaining firm performance and is accountable to the shareholders, this whole 'government' and its operations is known as corporate governance. Solomon suggests the following definition of corporate governance; "*the system of checks and balances, both internal and external to companies, which ensures that companies discharge their accountability to all their*

stakeholders and act in a socially responsible way in all areas of their business activity” (Solomon, 2010).

Dissecting the given definition, one can understand that corporate governance is not specifically just about the internal control but about both, the macro and micro-environment and that in order to be accountable to the shareholders, management must also consider the stakeholders and drive the operations accordingly.

Principles of corporate governance were formulated by the Cadbury Committee and also the OECD Committee on Corporate Governance and they had been mainly aimed at the board. The principles that have been introduced are as follows:

- **The responsibility of the board and its role in the governing of the company:** how the board manages and monitors the company and its role in providing strategic directions. The board is also accountable to both the company and the shareholders (Cadbury Committee, 1992) and (OECD, 2004).
- **Disclosure and transparency:** how open the company is to revealing its operations builds confidence in shareholders and stakeholders for the company (Cadbury Committee, 1992) and (OECD, 2004).
- **Integrity:** the reporting of financial statements by the company must reflect its true performance, and the individuals involved in the process of drafting should have good ethical background. The board itself has to have this aspect for the whole system to be ethical (Cadbury Committee, 1992) and (OECD, 2004).
- **Rights of shareholders:** the board must ensure that the company safeguards the rights of the shareholders and that their corporate governance framework be a means to allow shareholders to exercise their rights (Cadbury Committee, 1992) and (OECD, 2004).
- **Equitable treatment of shareholders:** whether it's a minority shareholder or major, the board must ensure that shareholders of any class are treated equally and have the necessary freedom to raise their concerns. This weighs greatly upon voting rights too (OECD, 2004).
- **The role of stakeholders and their rights:** the stakeholders are a vital part of the company whether they are directly involved, or indirectly affected (e.g. those living around the company's operation areas) and the company and board must ensure they recognise the rights of these stakeholders. The company should be socially responsible too to ensure that the stakeholders are in positive correlation (OECD, 2004).

The reports suggest that a proper corporate governance framework be structured by the company in line with its operations and business, at the same time incorporating the above principles into the framework (Cadbury Committee, 1992) and (OECD, 2004).

This paper aims to focus on the principle of disclosure and transparency as its main purpose is to propose a solution to resolve the issues that investors and shareholders face when trying to acquire the right information about their investee corporations. Transparency and disclosure have become vital factors in determining the integrity of a corporation and investors rely on this prior to making their decisions of whether to gamble on corporate shares. Transparency has only one meaning known to investors; the accessibility of all information about the corporation. As Khas, Keong and Anandarajah suggest, investors prefer companies whom portray transparency and disclosure in their operations and are accountable in terms of objectives and performance (Khas, Keong, & Anandarajah, 2002).

CURRENT SYSTEMS

Thorough research into past and available systems has resulted in obtaining a few implementations of corporate governance systems around the world. The most notable are

those in the United States, particularly one known as the ISS Governance Quickscore, under the hood of Morgan Stanley Capital International (MSCI). The company itself is a machine which tracks financial markets, investment portfolios, share price listing and provides statistical analysis and indices of equity, hedge funds and fixed income. MSCI had ventured out to create the Institutional Shareholder Services, ISS, which created methods of managing governance risk and providing other similar solutions to the financial community to help them make wiser investment decisions.

The main concern of this study is with ISS Governance Quickscore, as that is a system already being implemented and used by various companies worldwide. The system is accessible online on the ISS website and an individual just has to search their company of interest into the search box for them to see the score. Figure 1 below depicts a sample of the result given after searching for a governance score of a company (ISS).

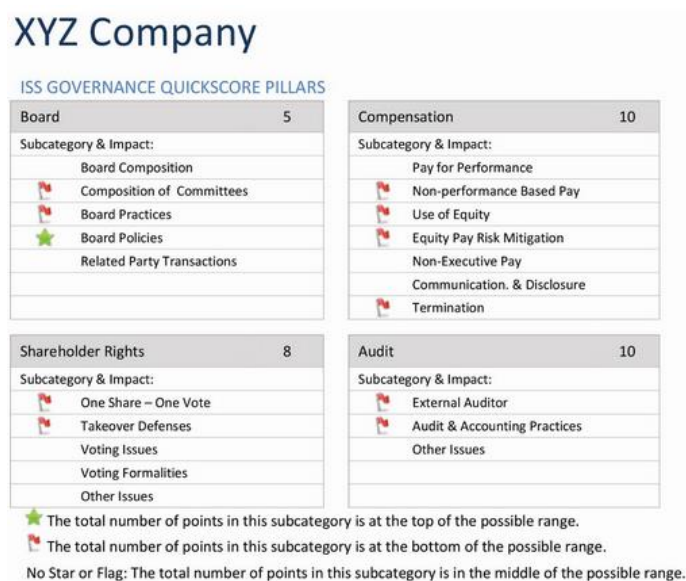


Figure 1: ISS QUICKSCORE

As seen in Figure 1, there are four main aspects that ISS Governance Quickscore measures, namely; Board, Shareholder Rights, Compensation and Audit. In totality, there are 181 factors covered under the aforementioned aspects and each of the factors is listed in one of the related subcategories that are under the specific aspect as shown in Figure 1. Raw scores are given to the factors then tallied up into the subcategories and from there, given a relative measure of 1-10 which gives the final score. In this case, 1 denotes as a highest raw score and hence lower governance risk and vice versa for 10 (ISS, 2014).

Another organisation in the United States known as the GMI Ratings, a merger between Governance Metrics International, The Corporate Library and Audit Integrity, was created in order to provide statistical analysis and scoring of corporate governance practices in 5500 companies around the world. They created a system called the GMIAAnalyst and the system focuses on the following areas/metrics; Corporate Events, Board, Pay, Ownership and Control, Environmental and Social. The reporting method is similar to that of ISS Quickscore where they provide the client with a report of their findings and portray red flags on the lower scored areas. They also provide the client benchmarking tools, portfolio and risk assessment tools and accounting risk ratings. However their system is much more complex than that of the ISS Quickscore.

In the Malaysian market, potential investors and shareholders rely on Bursa Malaysia to provide the information and advice of their target company, apart from the company itself. Minority Shareholder Watchdog Group (MSWG) has been a vital player in ensuring that the rights of the minority shareholders are protected and the group also provides information to a certain extent to these shareholders about their target investees. However, none provide a hands-on, assessment or measurement system whereby the institutional investor may access to review detailed analysis of corporate governance practices of their target corporation.

METHODOLOGY

The first step was to conduct a needs-analysis in order to determine the possible factors of corporate governance and functionalities of the proposed system. Semi-structured interviews were carried out with seven organizations to fulfil this objective. The sample was based upon convenience sampling method where 20 companies were chosen based on qualitative measures and 7 had responded. Table 1 below lists the organizations and the designation of the interviewees respectively.

Table 1: Interview List

No.	Organization	Designation
1	Malaysian Institute of Corporate Governance	Chief Operating Officer
2	RAM Ratings	Chief Compliance Officer
3	Malaysian Ratings Corporation Berhad	Acting Head, Ratings
4	Employees Provident Fund	-CFA, Head of Research -Head of Corporate Surveillance Unit -Head of Corporate Governance Unit -Analyst in Corporate Governance Unit
5	Tabung Haji	-Head, Fund Investment and Outsourcing -Research Head -Head, Foreign Equity Portfolio
6	Companies Commission of Malaysia	Head of Law Reform, Policy & International Affairs, Corporate Development
7	Bursa Malaysia Berhad	VP Corporate Governance

A brief introduction about the study was initially provided by the interviewer. A number of areas were probed into when conducting the interviews; these were mainly in a semi-structured format that guided the direction of the interview. The questions that concern this paper are listed in the Table 2 below. The questions may seem like being directional or

leading, however they were used as topic starters to delve into the particular areas as posed in the questions.

Table 2: Interview Questions

No.	Question
1	Do you think that the government has a good channel to monitor corporate governance practices? If no, do you think there is a need to develop a channel/system?
2	Do you think that corporations in Malaysia are transparent enough? If no, what would you suggest should be done?
3	Do you think such a system would be beneficial for companies to use as a benchmarking tool?
4	What factors would you like to see in such a system that could determine for an investor whether the corporation is practicing good governance?

Based on the transcribed results a model was created to depict the interface and functions of the system. This process, better known as Systems Analysis and Design, is the most effective way in designing a platform for the development of a system. Figure 2 shows a diagram of the process as a whole.

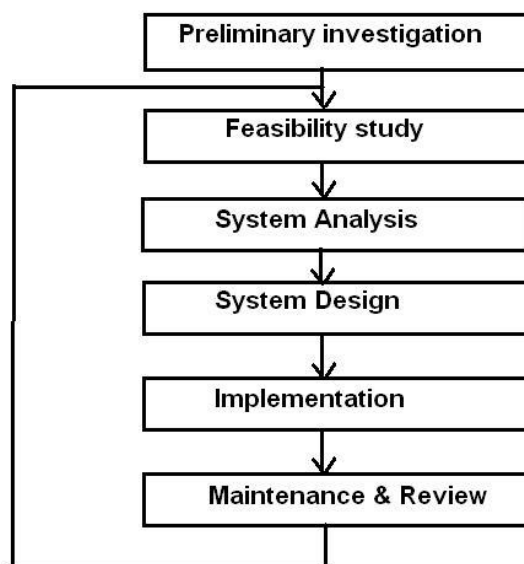


Figure 2: System Analysis and Design

This paper aims to propose a concept system whereby the objective is to reach the system design phase.

RESULTS

A number of keywords were identified based on the interviews regarding the functionalities. First, the usefulness and need of the system is addressed. According to all seven interviews, no such system is currently available in Malaysia and in fact, a few of them have been looking forward to such systems similar to the ISS and GMI systems. This also answers the first question in Table 3.

To the second question, a majority of the interviewees agreed that the companies are relatively transparent and that disclosure is at 90%. The Malaysian Code of Corporate Governance and the Companies Act of 1965 ensures that companies comply with disclosure; however, the amount of disclosure is questionable. As three of the seven mentioned that majority of the companies only disclose the minimum required in order to be in compliance with the Code and the Act. The only disclosure is also through annual reports and financial statements released by the company. For investors and shareholders, this multitude of data means a time taking process in order to classify and then proceed to making a decision.

With regards to the third question, each of the interviewees had agreed on the usefulness of benchmarking for companies whom had not reached the disclosure level and transparency level of those practicing corporate governance on a higher scale. Lastly, the Table 3 below lists a number of keywords that are the main functions and areas that the interviewees would prefer to see in the system.

Table 3: Interview Results

Functions	Areas
Cross-analysis of directors	Board details
Searchable board members	Audit committee information
Comparison of companies' corporate governance quality	Market capitalization details
Summarized reports	Transaction cost history
	Risk management details

With the above results from interviews, a conceptual model of the system was designed. Figure 3 below displays the design.

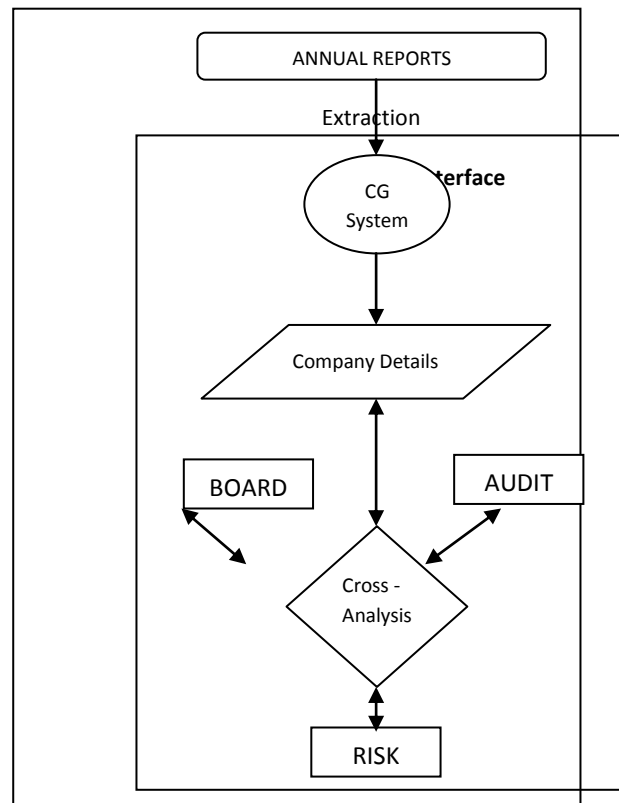


Figure 3: Conceptual Design of System

This design is merely a concept and drafted in accordance with end-user needs rather than a venture between industry and academics. The interface will be the main desktop system which will extract information from a pool of annual reports of the companies. This information will be fed into the background database whereby the coding will allow the functional interface to perform the processes of cross-analysis and user-oriented functions. The CG system shall encompass a variety of tools allowing the end-user to evaluate each company in a holistic manner based on their Board, Audit and Risk categories.

CONCLUSION

With the study of the literature and the needs-analysis conducted, this paper has proven firstly that there is no system in Malaysia that acquires information of corporate governance practices of companies. Based on interview results, a concept system was designed in order to address the issue of transparency and accessibility of information.

For future works, the system must place a value added feature, where one can look at the significance of corporate governance measurement and firm performance indicators to place greater emphasis on the quality of the practices. In this manner, the system would be utilized as a decision support for investors that would provide insight into credible investment opportunities. At the same time it may be used by corporations in order to benchmark their better players so as to emulate higher quality corporate governance.

Reemphasis on the fact that this model was created solely on the basis of end-user requirements, the academic factors have yet to be tapped into and the combination between industry and academics would provide versatility and broadness into the system which can be further developed to provide valuable functionalities. However, for such a concept to be codified, an in-depth survey is required with more potential end-users.

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