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Your Ref: Please advise
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16 October 2015

MEMORANDUM

To : Prof. Robert Eccles / UN Global Compact
From : Dato' Azmi Mohd Ali, Nur Sabrina Musfirah Mohamed Nazri,
Yeoh Yee Chieh

Legal Perspective on an Annual Board “Statement of Significant Audiences and Materiality” – Draft Malaysian Legal Perspective

The information contained in this memorandum is based solely on the laws and regulations of Malaysia effective as of the date hereof and does not consider the laws and regulations of any other jurisdiction.

Setting the legal landscape

1. Briefly explain the broader legal landscape regarding the obligations that a company has to its stakeholders or with regard to its impact on stakeholders, and in particular whether its primary duty is or is not to shareholders over all other stakeholders.

In Malaysia, a company’s primary duty is to direct and manage the business and affairs of the company towards enhancing business prosperity and corporate accountability with the ultimate objective of realising long term shareholder value. The obligations owed to stakeholders are not enshrined in any legislation. Despite so, we observed that there is an increasing trend whereby companies are encouraged to acknowledge the interest of other stakeholders (shareholders, employees, the society or community) in their decision-making process in circumstances where it is not fully reflected in the legal framework.

Regulatory Framework

2. To what legal tradition does the jurisdiction belong, i.e. civil/common law, mixed?

The law of Malaysia is mainly based on the common law legal system. This was a direct result of the colonisation of Malaya, Sarawak, and North Borneo by Britain from early 19th century to 1960s.

3. Are corporate/securities laws regulated federally, nationally, provincially or both?

The corporate and securities laws in Malaysia are regulated federally and nationally. The Ninth (9th) Schedule Federal List Paragraphs 7 and 8 of the Federal Constitution relates to finance trade, commerce and industry which places securities capital market regulation and law of corporations under the Federal jurisdiction. Acts governing corporate and securities will then be passed by the Parliament in Malaysia.

The federally legislated Acts currently in place are but not limited to the *Companies Act 1965* (“CA”), and the Capital Markets and Services Act 2007 (“CMSA”).

4. Who are the government corporate/securities regulators and what are their respective powers (in summary only)?

(i) Companies Commission Malaysia (“CCM”)

Companies Commission of Malaysia (CCM) is a statutory body formed as a result of a merger between the Registrar of Companies and the Registrar of Businesses in Malaysia which regulates companies and businesses (including foreign corporations doing business in the country).

CCM is the main body who regulates matters relating to corporations, companies and businesses in relation to laws administrated as well as to provide company and business information to the public. As the leading authority for the improvement of corporate governance, CCM fulfills its function to ensure compliance with business registration and corporate legislation through comprehensive enforcement and monitoring activities so as to sustain positive developments in the corporate and business sectors of the Nation. The Ministry of International Trade and Industry has a role in assisting in the governing and providing licenses to certain industries if they are of a certain threshold in size of investment and employment.

(ii) Securities Commission (“SC”)

The SC is the main regulator for listed corporations. Established under the Securities Commission Act 1993 on 1 March 1993, the SC is a self-funding statutory body with investigative and enforcement powers. It reports to the Minister of Finance and its accounts are tabled in Parliament annually. The SC’s many regulatory functions include:

- Supervising exchanges, clearing houses and central depositories;
- Registering authority for prospectuses of corporations other than unlisted recreational clubs;
- Approving authority for corporate bond issues;
- Regulating all matters relating to securities and derivatives contracts;

- Regulating the take-over and mergers of companies
- Regulating all matters relating to unit trust schemes;
- Licensing and supervising all licensed persons;
- Encouraging self-regulation; and
- Ensuring proper conduct of market institutions and licensed persons.

Underpinning all these functions is the SC's ultimate responsibility of protecting the investor. Apart from discharging its regulatory functions, the SC is also obliged by statute to encourage and promote the development of the securities and derivatives markets in Malaysia.

(iii) Bank Negara Malaysia ("BNM")

As Malaysia's central bank, BNM main purpose is to issue currency, act as banker and adviser to the Government of Malaysia and regulates the country's financial institutions, credit system and monetary policy. It is also empowered to approve the issue of securities by financial institutions licensed under the *Banking and Financial Institution Act 1989* and the Insurance Act and the control of the shareholding and management of licensed financial institutions and licensed insurers.

(iv) Bursa Malaysia ("BM")

The Bursa Malaysia is the front line regulator for listed corporations. BM is an exchange holding company approved under Section 15 of the CMSA. It operates a fully-integrated exchange, offering the complete range of exchange-related services including trading, clearing, settlement and depository services. Its main governing powers are derived from the Bursa Listing Requirements.

Minority Watchdog Shareholder Group ("MWSG")

In addition to all of the regulators above, Malaysia has various bodies that articulate views on behalf of minority shareholders. This group is primarily funded by the Capital Market Development Fund.

5. Does the jurisdiction have a stock exchange(s)?

Yes. Malaysia has a single, fully-integrated exchange operated by the Bursa Malaysia Berhad. Companies are either listed on:

- The Bursa Malaysia Securities Main Board: for larger capitalized companies; or
- The Second Board: for medium sized companies; or
- The ACE Market: for high growth and technology companies.

Incorporation and listing

6. Do the concepts of “limited liability” and “separate legal personality” exist?

Limited Liability

The concepts of “limited liability” do exist in corporate laws in Malaysia. There are three types of limited companies and they are:

1. A company limited by shares: This is the most common type of company where the company is formed on the principle of having the liability of its members limited by the memorandum of association to the amount (if any) unpaid on their shares respectively held by them.
2. A company limited by guarantee: This type of company is formed on the principle that the members’ liability is limited by the memorandum to a nominated amount which the members respectively undertake to contribute to the assets of the company in the event of its being wound up.
3. A company limited by share and guarantee

Separate Legal Personality

Once a company is incorporated under the CA, the law shall regard it from the date mentioned in the certificate of incorporation to be a body corporate. In other words, it will be regarded as an independent legal entity separate and distinct from the members who constitute it. However, there are numerous occasions where the statutory provisions and the Court have sometimes recognised that it is necessary to go behind the corporate veil. In spite of this, it is important to note that this principle is not a general principle of law.

7. Did incorporation or listing historically, or does it today, require any recognition by the company or its directors of a duty to society, an obligation to take account of the company’s social or environmental impacts, or to respect its stakeholders?

[For these purposes, the term “stakeholders” is distinct from “non-shareholder” and from “shareholder” in that it encompasses both “material audiences” (the providers of financial capital, both debt and equity), as well as “significant audiences” (non-financial stakeholders, such as employees, customers, suppliers, contractors and subcontractors, regulators etc. some of whom may be material to a firm at an entity specific level)].

No, there are no express provisions or statutory requirement at incorporation recognising a duty to society more generally.

For listed companies, there is a requirement for a company to have good corporate governance which encourages company to recognise their obligations towards society in general.

8. Do any stock exchanges have a responsible investment index, and is participation voluntary? (See e.g. FTSE4Good, Dow Jones Sustainability Index, the Johannesburg Stock Exchange's Socially Responsible Investment Index.)

Bursa Malaysia ("BM") does not have a responsible investment index.

However, it was reported last December 2014, BM is launching its Environmental, Social and Governance (ESG) Index. The FTSE4Good Bursa Malaysia (F4GBM) Index was developed in collaboration with FTSE as part of the globally benchmarked FTSE4Good Index Series and is aligned with other leading global ESG frameworks such as the Global Reporting Initiative and the Carbon Disclosure Project. All Malaysian companies listed on the Bursa Malaysia Main Market and ACE Market are eligible for inclusion, subject to meeting FTSE's international standards of free float, liquidity and investability.

The F4GBM Index is used to measure the performance of companies demonstrating strong Environmental, Social and Governance practices. Constituents of the new index must meet internationally benchmarked criteria that measure such things as efforts in environmental conservation, the impact of social responsibility initiatives on the community and the practice of good governance through responsible and ethical decision making.

Bursa Malaysia's initiative on sustainability started almost a decade ago with the introduction of the Bursa Malaysia Corporate Responsibility framework in 2006, which was subsequently followed by the Syariah-based indices and corporate governance guidelines for listed companies in 2007.

Directors' Duties

9. To who are directors' duties generally owed?

Director of a company generally has a duty to act bona fide for the benefit of the company as whole.

S. 132 (1) of CA states that a director shall at all times exercise his powers for a proper purpose and in good faith in the best interest of the company. The concept of "best interest" follows the common law position that it is the interests of shareholders and not other stakeholders that is primary.

10. What are the duties owed by directors – please state briefly.

Please indicate if there are express or implied duties to avoid damage to the company's reputation?

The CA provides the statutory duties of company directors. The statutory duties will be further supplemented by the common law principles on directors' duties. The duties of directors include the following:

- To act bona fide in the interests of the company;
- To exercise powers for their proper purpose;
- To exercise reasonable care and diligence;
- To retain their discretionary powers; and
- To avoid conflicts of interest.

Express or implied duties to avoid damage to the company's reputation

There are no specific statutory requirements or duties to avoid legal risk and damage to the company's reputation. Nonetheless, the directors do have a fiduciary duty to act honestly in the best interest of the company. This may include a duty not to do any act or omission which will bring damage to the company's reputation.

11. More generally, are directors required or permitted to consider the company's impacts on non--shareholders, including impacts on the individuals and communities affected by the company's operations? Is the answer the same where the impacts occur outside the jurisdiction? Can or must directors consider such impacts by subsidiaries, suppliers and other business partners, whether occurring inside or outside the jurisdiction? (See e.g. s. 172 UK Companies Act 2006)?

A director as provided in the CA, do not specifically have a duty to consider the company's impacts on non-shareholders nor impacts on individuals and communities affected by the company's operations inside or outside the jurisdiction.

Nevertheless, provided that it is in the best interests of the company to do so, this does not prevent directors from considering such impacts as part of their oversight duties. If ignoring such impacts could put the company at risk, it is possible that the directors have a duty to consider such impacts.

Furthermore, other laws may prescribe a duty to play an oversight role in this regard. For instance: requirements for certain companies operating certain types of production to obtain certain environmental licenses under environmental laws.

12. If directors are required or permitted to consider impacts on non--shareholders to what extent do they have discretion in determining how to balance different factors including such impacts?

If directors are required to consider impacts on non-shareholders, the discretion exercised by them would be within the boundary of serving the interests of the company. Within that boundary, the directors will have discretion to address such impacts and manage tradeoffs between immediate return and medium to longer term interest of the company.

13. What are the legal consequences for failing to fulfil any duties described above; and who may take action to initiate them? What defenses are available? Can these issues given rise to other causes of action or regulatory routes whereby a stakeholder can exert pressure on a company with regard to its actions?

Legal consequences

Failure to fulfill statutory duties under the CA may entail criminal liability where provided, which includes substantial fines or terms of imprisonment. In more serious cases, a director could incur both imprisonment for up to 5 years and pay a fine of up to RM 30,000 upon conviction. In certain cases, the CA also provides that a director could be personally liable for the loss or damage suffered by the company. The members of the companies as well as companies and third parties affected by the directors' breach of duties may commence civil proceedings against them.

Defences

Defences that are available to a director in Malaysia with regards to breach of fiduciary duty would be defences that will affect his or her ability in the decision making for the best interest of the company. For example: undue influence, coercion, duress and etc.

Other causes of action or regulatory routes whereby a stakeholder can exert pressure on a company with regard to its actions

S. 181A and 181B of the CA provides that on application, a Court may give leave to a complainant to bring, intervene in or defend an action on behalf of the company as long as he or she:

- is acting in good faith; and
- if it appears *prima facie* that he or she is acting to be in the best interest of the company.

A "complainant" in this section means:

- (a) a member of a company, or a person who is entitled to be registered as member of a company;

- (b) a former member of a company if the application relates to circumstances in which the member ceased to be a member;
- (c) any director of a company; or
- (d) the Registrar, in case of a declared company under Part IX

14. Are there any other directors' duties which are relevant to the interests of stakeholders?

There is no specific legislation on directors' duties that are relevant to the interests of stakeholders. However, in the Malaysian Code on Corporate Governance, as stated above it is provided that the boards and management of a public listed company must be mindful of their duty to direct their efforts and resources towards the best interest of the company and its shareholders while ensuring that the interests of other stakeholders are not compromised.

15. For all of the above, if these exist in your jurisdiction, does the law provide guidance about the role of supervisory boards in cases of two tier board structures.

There are no two tier board structures for Malaysian companies, only single-tier boards.

Section 131B of the CA provides guidance on the role of supervisory boards in case of single-tier boards in Malaysia. The section provides that:

- (1) The functions and powers of the board which are inclusive of the business affairs of a company must be managed by, or under the direction of, the board of directors.
- (2) The board of directors has all the powers necessary for managing and for directing and supervising the management of the business and affairs of the company subject to any modification, exception or limitation contained in this Act or in the memorandum or articles of association of the company.

What obligations are owed by senior management who are not board directors? Is this determined by law if no specific contractual provision applies?

There is no specific legislation on obligations that are owed by senior management who are not board directors. The articles of association of a company may contain provisions on the obligations of the senior management. However, fiduciary duties can also be imposed on senior officers, who may be considered as de facto directors.

A de facto director is a person who has not been formally appointed but who in effect acts as if he were a director.

Reporting

16. Are companies required or permitted to disclose the impacts of their operations (including stakeholder impacts) on non--shareholders, as well as any action taken or intended to address those impacts? Is this required as part of financial reporting obligations or pursuant to a separate reporting regime? Please specify for each reporting route whether it is mandatory or voluntary.

Private companies unlike Public Listed Companies (PLCs) are not required to disclose the impacts of their operations on non-shareholders as well as any action taken or intended to address those impacts.

The Corporate Social Responsibility (CSR) Framework of Bursa Malaysia encourages PLCs to voluntarily disclose their CSR related issues. In this regard, PLCs are urged to disclose their CSR activities or practices (and of their subsidiaries) and if there are none, a statement concerning CSR will be needed. The Framework aims to give PLCs clear guidelines and actionable ideas for implementing their own CSR initiatives. The intention is to raise the awareness of CSR and encourage PLCs to integrate the practice of CSR as part of the way they work and think.

Please describe any mandatory reporting requirement, major voluntary initiative or trend towards voluntary reporting with regard to transparency (for example, payments to government or state owned entities, reports on government orders to undertake surveillance or interception, reports on tax payments etc.).

The CA embraces the principles of disclosure and transparency. The Act requires companies (both private and public listed companies) to hold an annual general meeting to approve audited profit and loss account and balance sheet as well as reports of the auditors and directors.

There is a further mandatory reporting requirement for PLCs (Chapter 9 in the Bursa Listing Requirements).

Para 9.02 discusses on the corporate disclosure policy:

1) A listed issuer must, in accordance with these Requirements, disclose to the public all material information necessary for informed investing and take reasonable steps to ensure that all who invest in its securities enjoy equal access to such information.

2) There are 6 specific policies concerning disclosure that a listed issuer must adhere to:

- a) Immediate disclosure of material information;
- b) Thorough public dissemination;
- c) Clarification, confirmation or denial of rumours or reports;
- d) Response to unusual market activity;
- e) Unwarranted promotional disclosure activity; and
- f) Insider trading.

Malaysian Code on Corporate Governance 2012 acts as reference to PLCs and not to private companies. Disclosure and transparency are essential for informed decision-making to PLCs.

17. Do legal reporting obligations extend to such impacts outside the jurisdiction; to the impacts of subsidiaries, suppliers and other business partners, whether occurring inside or outside the jurisdiction?

There is no legal requirement for reporting on impacts on non-shareholders under this rubric. Nevertheless, as mentioned above, Para 9.02 of Chapter 9 of the Bursa Listing Requirements has provided certain public disclosures to be made by PLCs and this would cover both foreign and domestic investors.

18. Who must verify these reports? Who can access reports? And, what are the legal or regulatory consequences of failing to report or misrepresentation?

In general, the reporting rules together with the consequences of misrepresentation and failing to report are enforced by Bursa Malaysia.

There is a provision in the CA that states about reporting which is Section 174(1):

Every auditor of a company shall report to the members on the accounts required to be laid before the company in general meeting and on the company's accounting and other records relating to those accounts and if it is a holding company for which consolidated accounts are prepared shall also report to the members on the consolidated accounts.

The legal consequences of misrepresentation are in Section 364A of the CA on false reports.

An officer of a corporation who, with intent to deceive, makes or furnishes or knowingly and wilfully authorizes or permits the making or furnishing of, any false or misleading statement or report that relates to the affairs of the corporation shall be guilty of an offence against this Act. A penalty of imprisonment for ten years or two hundred and fifty thousand ringgit or both will be imposed.

Is there a regulator tasked with investigating complaints of misreporting?

In the case of misreporting of financial report of a company, the relevant authority can either be Bursa Malaysia and SC for public listed companies and CCM for private companies. The investigating complaints of misreporting can only be found in Section 306 (4) of CA where any report is made, the Minister may, if he thinks fit, investigate the matter and may, if he thinks expedient, apply to the Court for an order conferring on him or any person designated by him for the purpose with respect to the company concerned all such powers of investigating the affairs of the company as are provided by this Act in the case of a winding up by the Court, but if it appears to him that the case is not one in

which proceedings ought to be taken by him, he shall inform the liquidator accordingly, and thereupon, subject to the previous approval of the Court, the liquidator may himself take proceedings against the offender.

19. What is the external assurance regime for reporting on a company's impacts on stakeholders? Please specify any mandatory requirements and also where reporting is voluntary what the current market practice is as regards third party assurance.

There is no external assurance regime for reporting in Malaysia. Nevertheless, if a company is carrying business as an audit firm the oversight body will be the Malaysian Audit Oversight Board ("AOB"). The AOB's aim is to promote and develop an effective audit oversight framework and to promote confidence in the quality and reliability of audited financial statements in Malaysia. The registered audit firm and auditor will be subject to inspections by the AOB to assess the degree of compliance with the auditing and ethical standards by the auditor and the quality of the audit reports prepared by the auditor relating to the audited financial statements of the public interest entities.

Please summarise any regulatory guidance on reporting that relates to impacts on non-shareholder stakeholders.

As mention in the paragraph 16, there are no regulatory guidelines available on reporting that relates to impacts on non-shareholder stakeholder.

Stakeholder engagement

20. Are there any restrictions on circulating shareholder proposals which deal with impacts on non- shareholders, including stakeholder impacts?

There are no restrictions on circulating shareholder proposals but there is a corporate disclosure policy which can be found in the Malaysian Code on Corporate Governance.

As mentioned earlier, para 9.02 in Chapter 9 of the Bursa Listing Requirements provides that a listed issuer must, disclose to the public all material information necessary for informed investing and take reasonable steps to ensure that all who invest in its securities enjoy equal access to such information. However, one risk which may arise from such requirement is that some controlling shareholders may use defamation suit threats to reduce any strong news that places corporation in a negative situation.

21. Are institutional investors, including pension funds, required or permitted to consider such impacts in their investment decisions? What is legal duty that pension funds owe with regard to investment decisions in this regard?

One of the key institutional investors in Malaysia is the Employees Provident Fund (“EPF”). The EPF is governed under the Employees Provident Fund Act 1991 and is a national social security organization operating through a provident fund scheme in Malaysia. Its principal members are the private and non-pensionable public sector employees.

There is however no distinct requirement for EPF to consider the impacts on non-shareholders, including human rights impacts. Unlike certain Pension Fund counterparts in other countries, EPF has not adopted explicit CSR principles in their investment portfolio decisions.

In relation to its legal duty with regards to investment decisions, Section 10 of the *Capital Markets and Services (Private Retirement Scheme Industry) Regulations 2012* specifies that its legal duty is on the duties and responsibilities of private retirement scheme provider approved under section 139Q of the Act.

The duties and responsibilities are:

- At all times exercise its powers for a proper purpose and in good faith in the best interest of the members as a whole;
- Exercise the degree of care and diligence that a reasonable man would exercise if he was in the private retirement scheme provider’s position;
- Keep records of all transactions relating to the private retirement scheme and ensure that all accounts and records kept are complete and accurate;
- Carry out any other responsibilities as may be specified by the Securities Commission;
- Make available for inspection a copy of the deed without charge to any member of the public.

How does the legal duty of the fund align with term and contractual performance criteria of fund managers – does this facilitate or deter consideration of such impacts?

The legal duty of the pension fund stated above is as a provident fund. It should be noted that the EPF is taking a portfolio risk and not a business risk based on the time-tested principles of portfolio management. Hence, the skills and resources at its disposal are better at managing portfolios (either directly or indirectly through fund managers) than at managing a diverse range of operating businesses which does not facilitate such impacts in their investment decisions.

22. Can non--shareholders address companies' annual general meetings? What is the minimum shareholding required for a shareholder to raise a question at a company's AGM?

No, unless such attendance is permitted by the Chair and is not refused by the shareholders.

There is no minimum shareholding required for a shareholder to raise a question at an annual general meeting as stated in the below provision:

Section 148 of CA: As to member's rights at meetings.

(1) Every member shall notwithstanding any provision in the memorandum or articles have a right to attend any general meeting of the company and to speak and vote on any resolution before the meeting.

Other issues of corporate governance

23. Are there any other laws, policies, codes or guidelines or standards applied in the context of particular contractual relationships (for example project finance) or through adherence to particular sustainability principles (for example the Global Compact, the OECD Guidelines for Multinational Enterprises etc.), related to corporate governance that might encourage companies to consider in a structured way their impacts upon and the interests of their wider stakeholders including through a stakeholder engagement process?

In the Malaysia Code on Corporate Governance, the boards of companies are required to take into account a wide range of constituents for longer term considerations and their interests. This is so in order to comply with the strategies of sustainability and stakeholder interest.

The fast growing businesses and their impact on the environment and the community in which they operate are attributable to the boards. The aspects that the boards should recognize as stated in the code are the environmental, social and governance as this will benefit both the company and its operating environment.

24. Are there any laws requiring representation of particular stakeholder constituencies (i.e. employees, representatives of affected communities) on company boards?

There is no specific legislation requiring representation of particular stakeholder constituencies on company boards.

25. Are there any laws requiring gender, racial/ethnic, religious or other stakeholder representation; or non--discrimination generally, on company boards?

There is no specific legislation which states that a stakeholder should be of any gender, race or religion. Malaysia does not have any discriminatory issues especially on company boards.

26. In your jurisdiction is there any legal route whereby a parent company can incur liability with regard to the impacts that one of its subsidiaries has had on stakeholder groups? Are there any serious proposals to impose such responsibility?

There is no specific legislation requiring a parent company to incur liability for its subsidiaries as the two are separate entities.

27. Are you aware of any incoming law or proposals that are relevant to the issues raised in this questionnaire? If so please describe, providing an indication of the anticipated date the legislation will come into force or be adopted.

The CCM has completed the drafting of the proposed Companies Bill that sets out the new legal framework to replace the Companies Act 1965. The proposed provisions were drafted primarily based on policies which have been approved by the Cabinet on 18 June 2010. It is anticipated that the Companies Bill 2013 will be enforced this year which is 2015, therefore, there are no further declaration on the exact date. The Bill consists of 631 clauses and 12 schedules as compared to the Companies Act 1965 ("CA") which is made up of 449 sections (including those sections that are identified by a number and a capital alphabet) and 10 schedules. The Bill will usher in many changes to the principal legislation that governs the formation, operation and regulation of companies in Malaysia.

Prepared by;

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