

“Apply or Explain” Under the Main Market Listing Requirements

IN THIS ARTICLE, WONG DING SHENG PROVIDES A SUMMARY OF THE NEW APPROACH TO CORPORATE GOVERNANCE DISCLOSURE REQUIREMENTS ON LISTED COMPANIES.

Introduction

The Malaysian Code on Corporate Governance (“MCCG”) was issued by the Securities Commission Malaysia (“SCM”) on 26 April 2017 and took effect immediately. On 29 November 2017, consequent to the issuance of the MCCG, Bursa Malaysia Securities Berhad (“Exchange”) undertook various amendments to the Main Market Listing Requirements (“MMLR”) including amendments to reflect the new corporate governance approaches and principles set out in the MCCG (“CG Amendments”).

Prior to the CG Amendments, a company listed on the Main Market (“listed company”) had only to provide a narrative statement of how it had applied the corporate governance principles set out in the 2012 edition of the Malaysian Code on Corporate Governance (“Previous Code”)¹ or the alternatives adopted, if any, in its annual report (“Previous CG Statement”). The MCCG and the CG amendments have changed the approach adopted and introduced new corporate governance disclosure requirements which must be observed and complied with by listed companies.

This article provides a summary of the new approach and the current framework of corporate governance disclosures under the MMLR applicable to listed companies in general. This article, however, will not cover any requirements on corporate governance practices and/or disclosures applicable to companies involved in specific industries.

New approach

One of the purposes of the CG amendments is to align the corporate governance disclosure requirements under the MMLR with the MCCG.

Under the Previous Code, the approach was “*comply or explain*” where listed companies only needed to explain reasons for any non-observance of a “*recommendation*” set out in the Previous Code without providing any alternatives it may have adopted.

The new approach taken by the MCCG is the “*apply or explain an alternative*” approach². Under this approach, listed companies are required to confirm their compliance or explain how they have otherwise applied each practice set out in the MCCG.

Where there is a departure, a listed company must provide an explanation for the departure, disclose the alternative practice it has adopted and how the alternative practice achieves the intended outcome set out in the MCCG. Further, there are additional requirements for companies on the FTSE Bursa Malaysia Top 100 Index or companies with a market capitalisation of RM2 billion and above who have departed from a practice, which is to disclose:

- a. actions which they have taken or intend to take; and
- b. the timeframe required to achieve application of the prescribed practice³.

For the purpose of applying the practices in MCCG, listed companies should and are encouraged to refer to the Corporate Governance Guide issued by the Exchange⁴.

The “*apply or explain an alternative*” approach is now reflected in the new corporate governance disclosure requirement under the MMLR⁵. Accordingly, listed companies who fail to apply the practices set out in the MCCG and disclose an alternative practice will be in breach of the MMLR⁶.

New corporate governance framework

Post-CG Amendments, the key corporate governance disclosures for a listed company are as follows:

- a. an overview of the application of the principles set out in the MCCG by the board of directors of the company is to be included in the company’s annual report (“CG Overview Statement”);
- b. the application of each practice set out in the MCCG during the financial year is to be disclosed to the Exchange in a prescribed format (“CG Report”) and announced together in the announcement of the annual report;
- c. a statement explaining the board of directors’ responsibility for preparing the annual audited financial statements is to be included in its annual report; and
- d. a statement about the state of risk management and internal control of the listed company as a group is to be included in its annual report (“Risk Management and Internal Control Statement”)⁷.

The CG Overview Statement, CG Report and Risk Management and Internal Control Statement must be approved by the board of directors of the listed company⁸. To avoid repetition, the MMLR states that any matter required to be disclosed in the annual report under the MMLR which relates to a practice set out in the MCCG will be deemed made if the information is disclosed in the CG Report⁹.

CG Overview Statement

As mentioned above, the Previous CG Statement only required listed companies to provide a statement describing the corporate governance practices adopted with reference to the Previous Code and explain any alternatives taken. The purpose of such statement was to allow shareholders to make an informed assessment on the corporate governance practices adopted. However, there was no specific requirement on the content to be included.

Under the CG Overview Statement, the board of directors of listed companies must provide an overview of how the principles set out in the MCCG have been applied. In addition, the CG Overview Statement must include a summary of its corporate governance practices during the financial year with reference to the three principles set out in the MCCG, namely:

- a. board leadership and effectiveness;
- b. effective audit and risk management; and
- c. integrity in corporate reporting and meaningful relationship with stakeholders.

Further, the key focus areas and future priorities in relation to its corporate governance practices should be highlighted¹⁰.

Though the purposes of both statements are similar, the CG Overview Statement has clearly placed greater disclosure obligations on listed companies, as compared to the Previous CG Statement.

CG Report

The CG Amendments have introduced an additional corporate governance disclosure to be made by listed companies in the CG Report, which is in the format prescribed by the Exchange explaining how the practices set out in the MCCG had been applied during the financial year.

Listed companies must provide specific disclosures on its application of each practice in the CG Report and adopt the “*apply or explain alternative*” approach which has been described above. Listed companies must carefully consider and be closely guided by the guidance set out in the MCCG when making the disclosures in the CG report.

Further, listed companies must also ensure that the CG Report covers the practices for the whole financial year. If a practice had only been in place for part of the financial year, the listed companies must expressly specify the period during which it had been in place¹¹.

Once the CG Report is completed, it will need to be disclosed in the prescribed format to the Exchange and announced together in the announcement of the annual report. Listed companies will also need to state in its annual report the designated website link or address where such disclosure may be downloaded¹².

Additional considerations

The MMLR has also provided a list of additional considerations to be taken into account by listed companies when making the CG Overview Statement and the CG Report, which are briefly set out below:

- a. Ensure that the CG Overview Statement and the CG Report contain adequate information to enable an informed assessment by shareholders and potential investors of its corporate governance practices;
- b. Ensure that key messages on governance are clearly set out and avoid taking a mechanical or legalistic approach in making the disclosures;
- c. Report how the practices set out in the MCCG have been applied, having regard to the listed company’s particular circumstances and business;
- d. Provide a balanced report by describing key issues and incidences of failure, and explaining how the issues were managed, actions that were taken to remedy the failures and lessons learnt;
- e. Ensure that the information is easy to understand; and
- f. Use the listed company’s website to add depth to the governance reporting and keep shareholders updated throughout the year¹³.

Risk Management and Internal Control Statement

The Risk Management and Internal Control Statement is not a new corporate governance disclosure obligation. However, post-CG Amendments, listed companies are required to address the practices set out in the MCCG relating to risk management and internal control framework in the Risk Management and Internal Control Statement¹⁴.

Conclusion

The CG Amendments have undoubtedly raised the standards of corporate governance for listed companies. This should be welcomed by all parties as they promote transparency and accountability,

which will create long term value for the shareholders and boost investors' confidence in listed companies and Malaysia in general.

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- ¹ Which was superseded by the MCCG.
 - ² Paragraph 5, page 8 of the MCCG.
 - ³ Paragraph 6.3, page 9 of the MCCG.
 - ⁴ Paragraph 3.7(a) under Part I of Practice Note 9.
 - ⁵ Paragraph 3.0 under Part I of Practice Note 9.
 - ⁶ Paragraph 2.08(3) of the MMLR.
 - ⁷ Paragraphs 15.25 and 15.26 of the MMLR.
 - ⁸ Paragraph 2.3 of Practice Note 9.
 - ⁹ Paragraph 2.2A of Practice Note 9.
 - ¹⁰ Paragraphs 3.1A and 3.1B under Part I of Practice Note 9.
 - ¹¹ Paragraph 3.4 under Part I of Practice Note 9.
 - ¹² Paragraph 15.25(2) of the MMLR.
 - ¹³ Paragraph 3.7 under Part I of Practice Note 9.
 - ¹⁴ Paragraph 4.0 under Part II of Practice Note 9.

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