Study on Non-Executive Directors 2013 - Profile and Pay

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The position of the non-executive director ("NED") is one that is increasingly in the limelight. Every time an NED, especially an Independent Director, resigns from a public-listed company under dubious circumstances, waves are created in the media and speculation abounds as to the real reason for the departure.

The NED has come a long way from being a bench-warmer, as it were, to being a progressive and equal member of the board. This expectation comes not only from the regulators but is also increasingly being expressed by shareholders and other concerned stakeholders. Whilst still uncommon in corporate Malaysia, it is not rare nowadays to see directors (including NEDs) on the defensive whilst being questioned by agitated shareholders during the company’s general meeting.

The NED provides the relevant “check and balance” to the executive on the board. This oft-repeated mantra has become an accepted corporate governance concept. Having said that, the concept can also be misconstrued with the NED needing to be antagonistic, aggressive and constantly second-guessing the executive directors. This sort of counter-productive behaviour is in no way the correct interpretation; instead the phrase “antagonistic, aggressive and second-guessing” would be better replaced by “cajole, support, but validate”. In particular, the term ‘validate’ implies a strong emphasis on the NED exercising an effective oversight role, tempered with a judicious dose of “healthy scepticism”.

Given the increasing burden on the NED, it is only right that he is reasonably and adequately compensated for his efforts. So what is the “market value” of the NED on a listed issuer? Obviously, there is not a “one-size-fits-all” answer as the quantum varies depending on the company’s size, industry segment, complexity of operations and other internal factors. Nevertheless, it is hoped the context of this study will shed light into the profile and remuneration of the NED, and provide relevant insights to assist companies in their quest to remunerate fairly and responsibly, going forward.
The first edition of this study, covering the top 300 market-capitalised (“ranked”) companies on Bursa Malaysia Securities Berhad (“Bursa Malaysia”), was conducted in 2009. In the same manner, the top 300-ranked companies were selected for this year’s study. These companies comprise the cream of corporate Malaysia, and collectively generated close to RM734 billion in revenue and RM124 billion in profits before taxation in their most recent financial years (2012-2013).

In the four years since we first launched this study, a multitude of changes in the corporate landscape has occurred. The 2009 study was conducted in the wake of the 2007/2008 global financial crisis (“GFC”), which debacle was quickly overshadowed by the 2011/2012 European sovereign debt crisis. As one crisis moved to another, regulators have reacted by tightening the screws on directors as well as the corporate “gatekeepers”, namely the auditors. As an example, in July 2013, the U.S. government proposed that auditors give an explicit endorsement of the company’s system of internal controls.

Over in Malaysia, the focus has been comparatively less on the auditors than on the directors. Recent and industry-specific legislation, such as the Financial Services Act 2013 and amendments to the Capital Markets and Services Act, 2007 have resulted in increased penalties on delinquent directors for failing in their fiduciary duties. Broader ranging legislations such as the Whistleblower Protection Act, 2010, and the Personal Data Protection Act 2010, have also come into play.

To top it all, the Companies Bill 2013 was issued for consultation in July 2013, and the proposals contained therein, if passed by Parliament, may present another milestone for corporate Malaysia from the corporate governance perspective.

What implications do all these changes hold for directors and, in particular, the non-executive director? Instead of feeling crushed by the onslaught of legislation, with more to come, all these changes could be seen as merely formalising the directors’ ethical and, some may hasten to add, moral obligations to act in the best interests of their companies at all times.

Whilst this publication is primarily a remuneration study for non-executive directors in listed issuers, the results therein cannot be seen or discussed in isolation without considering all the developments mentioned above. On this basis, we have structured the study along 7 important questions, with one leading to the next. We open the study with a discussion on the non-executive director (“NED”) and where he stands now. We examine the current remuneration received and we ask: Is the burden on the NED actually increasing? What would drive the trajectory of NED remuneration? Finally, we conclude with a somewhat controversial topic in questioning whether the NED should be remunerated in line with his company’s performance.

We hope that NEDs in Malaysia will find this study useful and thought-provoking.
WHERE DO OUR NEDs COME FROM?

OVERSTAYING YOUR WELCOME

A CUSHY JOB OR A TICKING TIME BOMB?

SO WHAT CAN THE NED BRING TO THE TABLE?

WHAT IS THE TRUE MARKET VALUE OF THE NED IN MALAYSIA?

WHY SHOULD THERE BE AN UPWARD TRAJECTORY IN NED REMUNERATION?

SHOULD PERFORMANCE-BASED REMUNERATION BE INTRODUCED?
It can be said that the categories of directors and their roles are not often completely understood, particularly by those outside of the corporate world. On this basis, it is useful to set out the different types of directors found on the board of a listed issuer or public-listed company (“PLC”):

Without going into too much detail, the non-executive director (“NED”), being a key part of the board, plays a critical oversight role and he can often be the last line of defence against decisions that go against the best interest of the company.

The two NED groupings are the independent NED (“INED”) and the non-independent NED (“NINED”). Bursa Malaysia Securities Berhad regulates the definition of the INED through a set of criteria outlined in its Listing Requirements. The intent of these criteria, commonly in use by other stock exchanges, is to guard against relationships and transactions that may impair the director’s independence.

Close to 60% of INEDs in our study have an accounting, commerce, economics or legal background. This implies that their skills and knowledge, being financially inclined or legally conversant, are a sought after aspect of their directorships.

As for a NINED, in the Malaysian context, he typically comes with the following background:

- the founder (or co-founder) of the company but has taken a back seat after many years of actively running the company and its subsidiaries; or
- is related to the founder, controlling shareholder or managing director of the company; or
- is a representative of the substantial shareholder.

**NED titbits**

- The average age of the 1,821 NEDs included in our study: 60 years old
- The oldest male NED: 88 years old (there are two). One is with a plantation company and the other sits on the boards of a construction PLC and construction equipment PLC.
- The youngest male NED: 26 years old, from an East Malaysia-based PLC.
- Oldest female NED: 85 years old. She sits on the board of a well-known financial services PLC.
- Youngest female NED: 27 years old. She is from a prominent family of business tycoons.
THE HEADLINE NUMBERS

1,821 non-executive directors
641 non-independents
1,180 independents

RM122,000 p.a.
per NED for the top 300 market-capitalised companies on Bursa Malaysia

+37%
increase over year 2009

RM239,000 p.a.
Financial institutions: top payers

11%
women directors
Our study reveals that a fairly large proportion of NEDs come from the above-mentioned backgrounds. Zooming into the group of board chairmen of the top 100-ranked companies (a total 81 NEDs), we find that nearly half (45%) are retired civil servants or former politicians. In the case of these NEDs, it seems that it is not ‘what’ one knows but ‘who’ one knows that makes them attractive to PLCs. This group of NEDs can make the key introductions, advise on the nuances of dealing with government red tape and guide companies in navigating the myriad of agencies that one often encounters when trying to run a business.

Given the propensity for PLCs to appoint NEDs who are related to the incumbent directors or have ‘connections’, where does that leave the pure, professional NEDs? What about those directors who may be brilliant in their fields but lack visibility in the business or political arenas?

There have been efforts to increase the profile of these professional NEDs, called ‘outside directors’ in the US. For example, the National Association of Corporate Directors (in the US) has created a registry of professional directors that companies may refer to when searching for suitable candidates. A similar platform, sponsored by the national stock exchange, exists in India.

On the local front, nascent steps are underway to build a pool of professional NEDs. The Malaysian Alliance of Corporate Directors uses its website to invite aspiring candidates willing to serve as directors. The Non-Aligned Movement Institute for the Empowerment of Women ("NIEW"), meanwhile, has created a registry of its own focusing on women directors.

Speaking of women NEDs, Corporate Malaysia has a lot of catching up to do. Our study indicates only 11% of NEDs are women. This is, however, a significant improvement compared to the 2009 study of 6% women NEDs.

The agenda for increasing women participation on boards has gained traction in recent years. In November 2012, the European Commission proposed a mandatory quota of 40% board representation, failing which companies may be liable to penalties. In Norway, the 40% quota is already binding (see sidebar). The United Kingdom, meanwhile, has proposed a voluntary quota of 25% for all FTSE100 companies by 2015.

In Malaysia, the Cabinet has formalised a target of 30% women representation in “decision-making positions” by 2016. Given the current low proportion of women NEDs in our study, this indeed appears to be a tall order.

In summary, whilst it doesn’t appear in the near term that PLCs will change their approach towards NED recruitment, it would be beneficial for boards to look beyond the traditional pool of directors, and certainly the right steps are underway to widen the pool of professional NEDs available for selection, including women directors.

**The Norwegian experiment**

The Nordic country of Norway passed a law in 2006 requiring 40% of boards of public companies to comprise women directors.

This quota system achieved its intended goal, but some commentators argue that the achievement is merely superficial, based on the fact that a similar proportion of women participation did not materialise at the management level.

On this matter, the UK’s Guardian in January 2013 published an interview with a pioneer woman director from Norway who, at one point, sat on the boards of 185 companies! She went on to say that many public-listed companies had simply delisted themselves to avoid complying with the quota.
By and large, the NEDs in our study had no prior relationship with the company before coming on board. A small minority, though, were previously executive directors or held senior management positions with the company or its subsidiaries before being appointed to the board.

Our study indicates that the NED has on average served about 7 years on the board. This can be further segmented into INEDs with 7.5 years and NINEDs with 6.5 years.

An interesting outcome of our study is that about one third (33%) of the independent directors, i.e. close to 390 of them, have served on their boards for more than nine (9) years.

The tenure of the INED can be a controversial topic indeed. Many economies have attempted to legislate the independent element of the board. In Malaysia, the INED is the only director clearly defined in Bursa Malaysia’s Listing Requirements.

In the United Kingdom, the national corporate governance code requires the board to explain why it considers its independent directors as still independent after nine (9) years. This is also the stance taken by Singapore. The Malaysian Code on Corporate Governance 2012 (MCCG 2012), however, goes a step further by re-designating the director to be non-independent after nine (9) years. However, the board would need to seek approval from shareholders should it retain that director as independent after nine (9) years (Recommendation 3.3, MCCG 2012). Hong Kong SAR is another country taking the same approach as Malaysia.

**NINEDs vs. INEDs**

It was somewhat unexpected that in our study, the independent NEDs recorded a higher average tenure (7.5 years) compared to the non-independent NEDs (6.5 years).

A small number of NEDs were observed to have been on the board for decades. The usually limited information disclosed in the annual reports makes it difficult to ascertain if the director’s entire tenure related to his role as an NED only, or whether this included an executive role.
Why is there so much fuss on the limit of tenure for independent directors? Clearly, if regulators are seeking to bolster the independent element of the board, something must have been lacking in the first place. This could be indicative of a lingering feeling that NEDs (both independent and non-independent) may not be carrying their weight and see their positions on the board as ‘just reward’ at the end of a long career. On the other hand, empirical evidence gleaned from our interactions with high-performing NEDs over the years indicates that tenure isn’t necessarily the best indicator of an NED’s independence and behaviour. After all, an NED could be non-performing from very first day of his appointment!

There is a challenge that corporate governance advocates may not have considered in their push to limit the tenure of independent NEDs. Given Bursa Malaysia’s requirement that at least a third of the board or 2 directors, whichever is higher, must be independent, a question that remains to be answered is, “would the automatic re-designation of independent directors after nine (9) years cause a company to breach this requirement by falling short of the independent proportion?” Given the relatively small pool of truly independent professional directors, coupled with Bursa Malaysia’s limit of five (5) directorships for each director in listed issuers, will this not pose a challenge on the supply side and lead to an upward push on director’s remuneration? Or will we witness a supply of newly-minted ‘independent’ directors into the market, with little inkling of the liability that their position entails (see next section)?

Rather, we strongly feel that a carefully thought out recruitment process will go a long way towards expediting and strengthening the independent element on the board. Recruiting principled NEDs, who are not financially beholden to controlling shareholders, is a key imperative towards building an effective board.
When it’s time to go

It’s somewhat common to hear about under-performing employees being counselled out of the company, but how does one approach the rather more delicate situation involving a director?

A director could be considered under-performing when he:

■ has over-committed himself to other directorships, his personal affairs and business, or both. He is thus unable to devote the time required to serve effectively on the board and usually turns up for board meetings under-prepared;
■ cannot or does not want to keep up with current issues confronting the company;
■ is painfully unaware of his roles, duties, rights and obligations; and/or
■ is literally a silent attendee at board meetings.

In reality, there isn’t an easy way to ease a director out of office. There is often no simple solution, and some companies impose term limits to get around this. A director serves a fixed term and thereafter is done with the company.

Unfortunately, there are two disadvantages – this can be an extremely slow way of removing a director, and may have the tendency to remove high-performing directors too.

Boards may want to consider the following options:

■ agree on minimum performance standards required from each director (i.e. roles and responsibilities which could be written in the director’s appointment letter/service contract);
■ agree on a process to handle situations when a director may be required to leave on the basis of non-performance; and
■ have a succession plan in place, not only for the board chairman and committee chairmen, but for all directors. This would signal that the director’s position is not permanent.
A CUSHY JOB OR A TICKING TIME BOMB?

From our regular interaction with board members, we have probably seen the good, the bad, and the very average ones. We’ve encountered long-serving independent directors who still manage to keep management on its toes, while at the other end of the spectrum we’ve observed NEDs snoozing their way through board meetings. This brings us to an important question: Do directors know what they’re in for when they consent to a directorship in a listed issuer?

In our study, close to two thirds of NEDs (62%) are going “solo”, i.e. serving on only one PLC board, whilst a fifth (20%) sit on two PLCs, illustrated as follows:

![Circle diagram showing distribution of NEDs by number of directorships]

**PLC Directorships**

With the revised Listing Requirements of Bursa Malaysia limiting listed issuer directorships to five, the 20 NEDs above (which is about 1% of our study) whom we identified as having more than five directorships will need to relinquish their seats. It will be interesting to note what effect this will have on these NEDs – will they be expecting increased remuneration from the companies they choose to remain as director with, to compensate for the loss of seats on the other PLCs?

In the eyes of the law, all directors, executive or otherwise, are jointly and severally responsible and accountable for actions taken or omitted. This reality was amplified clearly in the legal case involving the Centro Properties Group (see page 13).
The Centro case highlights the urgency in which the NED needs to move away from the somewhat ‘traditional’ model of simply turning up for meetings, taking a back seat, contributing a few token points and collecting directors’ fees.

In other words, the NED may be playing with fire unless he brings himself up to the standards required of a director. To do this, he must remain contemporary by continuously keeping tab with relevant developments, engaging with fellow directors and attending formal training on a regular basis to be apprised of regulatory changes affecting him and the company. This is why one of the recommendations in MCCG 2012 specifically addresses training for directors (Recommendation 4.2, MCCG 2012) and emphasises on the continuous nature of refreshing the directors’ training needs.
The landmark Centro case

In a now famous case brought by the Australian Securities and Investments Commission against property giant Centro Properties Group, the judge found the directors of the company had breached their duty of care and diligence.

The saga began in 2007 when the directors approved the group’s financial statements which incorrectly classified billions of dollars of short term debt (i.e. payable within 12 months) as non-current liabilities. The financial statements also did not disclose that the group had guaranteed, after the financial year end, USD1.75 billion of debts owed by an associated company.

When news of this discrepancy became public knowledge and the company acknowledged the error, its share price plunged from over AUD10 to less than 5 Australian cents.

In their defence, the directors claimed that they had done “everything that could be reasonably expected” of a director. This included making “appropriate” enquiries from management and the external auditor on whether the financial statements complied with relevant accounting standards.

Nonetheless, the judge found that whilst the directors were entitled to delegate the preparation of financial statements, they retained the duty to exercise a “diligent and intelligent” interest in the information contained therein, and would need to:

- read and understand;
- apply the knowledge that they should have possessed (or alternatively acquire the knowledge required);
- make the appropriate enquiries; and
- have any errors corrected

Note: The judge imposed varying penalties on the directors at the conclusion of the trial in June 2011. Class action lawsuits were also brought against the directors; in May 2012, the lawsuits were settled out of court for an amount of AUD200 million, which was paid by the company, the external auditors and the company’s insurer.
SO WHAT CAN THE NED BRING TO THE TABLE?

Our study indicates that 92% of NEDs have a first degree, with a small number thereof having gone on to secure a masters degree (and some further on to a doctorate). Although education isn’t the only indicator of competence, the study indicates that the vast majority of Malaysian NEDs do possess an adequate level of qualification that can enable them to serve effectively.

Perhaps it isn’t surprising that from the group with at least one degree, the majority (58%) are accountants, economists, bankers or lawyers, given that traditionally, executive directors are the ones with the technical (i.e. engineering) qualifications whilst the typical NED has a non-technical background. Certainly these NEDs can be complementary to the executive directors by providing advice and insights from a finance or legal perspective and the expectation is that they contribute their fair share during board and committee deliberations, particularly for the audit committee.

The board of a public-listed company typically has three board committees, namely:
- audit committee (sometimes called audit and risk management committee);
- nominating committee; and
- remuneration committee.

Spreading the work
In addition to the audit, nominating and remuneration committees, boards of larger public-listed companies may form other committees to spread the work amongst the directors. Examples of committees we’ve seen are:
- Executive Committee;
- Employee Share Option Scheme Committee;
- Risk Management Committee;
- Tender Committee;
- Corporate Governance Committee;
- Investment Committee; and
- Sustainability (or Corporate Social Responsibility) Committee.

One large company even has a Litigation Committee set up specifically to pursue legal cases against the company’s former employees.
Financial Institutions are required by Bank Negara Malaysia to have a board risk management committee.

(Note: The audit and nominating committees are mandatory under Bursa Malaysia’s Listing Requirements, whilst all three committees are recommended by MCCG 2012).

Our study shows that 21% of NEDs are involved in a board committee, with slightly more than half (55%) serving on two or more committees.

Committee Membership

As Bursa Malaysia allows only non-executive directors (with majority independent) to sit on the audit and nominating committees, it would be unsurprising for more NEDs to be increasingly occupied with committee work. Perhaps the percentage that we see of NEDs with no committee responsibility (24%) will likely fall significantly by the next refresh of this study.

Moving on to the audit committee (AC) level, the study finds that only half (47%) of AC chairmen have an accounting background. Is this statistics important? Bursa Malaysia requires at least one member of the AC to be a member of a specified accounting professional body amongst other criteria but no mention is made as to the AC chairman’s professional qualification, apart from the need to be independent.
Background of AC Chairmen

Given the increasing complexity of financial reporting standards and greater levels of disclosure required by the stock exchange, perhaps boards should ponder whether the audit committee would be more effective if the chairman is equipped with a higher level of financial literacy.

Whether the NED is at a committee meeting or at the full board meeting, he is expected to carry and project himself in a manner that befits his position as a director. In summary, an NED is expected to:

- contribute to the development of corporate strategy;
- monitor the performance of management;
- satisfy himself that financial information is accurate and that risk management and internal control systems are robust and defensible; and
- determine the remuneration of executive directors and be involved in succession planning – this includes appointing and, if necessary, removing senior management.

(Sir Derek Higgs, Review of the role and effectiveness of non-executive directors, January 2003)
5 WHAT IS THE TRUE MARKET VALUE OF THE NED IN MALAYSIA?

Our study indicates an average remuneration of RM122,000 per annum for the NED within the top 300 market-capitalised companies, with further segmentation of the top 300 into three “layers” as follows:

<table>
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<tr>
<th>NED Remuneration Per Annum</th>
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<tr>
<td>Average for top 300</td>
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<tr>
<td>No. 1 to 100 ranked PLCs</td>
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<tr>
<td>No. 101 to 200 ranked PLCs</td>
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<tr>
<td>No. 201 to 300 ranked PLCs</td>
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(Note: In all our calculations, we have only considered ‘genuine’ NEDs – see sidebar)

Or looking at it from another angle, the remuneration can be segmented into an overall “top line” number; another with the Government-linked Companies (GLCs) being omitted, and a further outcome with both GLCs and financial institutions excluded.

Top 300 Market Capitalised Companies

Refer to Appendix 2 for a comparison of the above three-layered remuneration against the results of our 2009 study.

The NED remuneration of RM122,000 per annum represents a startling increase of 37% over the results of our 2009 study (RM89,000 per annum). The increase is moderated to 27% if we were to exclude the effects of inflation. Nevertheless a jump of 27% is still large over a span of four years (the inflation rates are based on Consumer Price Index as reported by the Department of Statistics from 2009 to 2012).

The ‘de-facto executive director’

There are instances where we have classified certain NEDs as “de-facto Executive Directors” even though on paper they are NEDs.

Why do we do this? We believe excluding such directors gives a more realistic indication of the market rate for the true NED in Malaysia.

We usually exclude an NED if one or more of the following indicators are present:

- he is the founder or controlling shareholder who is now designated as an NED;
- he is a close relative of the founder, managing director or controlling shareholder;
- he is an executive director at the subsidiary level where the subsidiary is a major contributor to the group’s results; and/or
- his remuneration is significantly higher than the other NEDs on the board. In some cases, this could be in multiples of the amount paid to the other NEDs.
A side-by-side comparison with the 2009 averages indicate the largest increase in the 201 to 300 ranked companies, with remuneration doubling from RM32,000 to RM65,000 per annum.

NED Remuneration Per Annum, 2013 vs. 2009

| No. 1 to 100 ranked PLCs | 2009; 63,000 | 2013; 98,000 |
| No. 101 to 200 ranked PLCs | 2009; 32,000 | 2013; 65,000 |
| No. 201 to 300 ranked PLCs | 2009; 89,000 | 2013; 122,000 |

Average for top 300

2009: 89,000
2013: 122,000

2009: 160,000
2013: 182,000

(Refer to Appendix 2 for a tabular form of the above information)

Readers of our first study in 2009 will be well aware by now that the size or market capitalisation of the company doesn’t necessarily correlate with the remuneration received by the NED, as clearly illustrated by the scatter graph below:

Average NED Remuneration for the 300 Largest Market Capitalised Companies on Bursa Malaysia
In terms of industry, it is the financial services sector that is the clear leader of the pack (RM239,000 per annum per NED). This leading position of the financial services sector, which is similar to our 2009 study, isn’t surprising given the multitude of legislations regulating that sector. It is also accepted that directors of financial institutions spend more time relative to their peers in other industries, and this can be evidenced, for example, by the number of board meetings held for the year (an average of 9 meetings per annum for financial services companies, versus 6 across the top 300 companies).

(Refer to Appendix 2 for a comparison of the above sectorial remuneration against the results of our 2009 study)

Finally, there is the added risk factor as not only shareholders’ funds are involved, a proportion of the general public in respect of deposits placed would be affected should anything untoward happen to these financial institutions.

In addition, the number of board meetings held in a year, by companies in each sector, when averaged, closely mimics the remuneration received by the NED in that market sector.

**Red Bar: Number of Board Meetings in a Year**

Not quite a cinch

Although this study may appear to be a straight-forward exercise in data extraction, not everything is as it seems, for example:

- the level of remuneration disclosure by individual directors remains poor. Of the top 300 companies, only 46 (15%) disclose individual remuneration. This is, however, a minor improvement over the percentage recorded in our 2009 study (12%);

- companies contend that disclosure by totals and in bands of RM50,000 is sufficient and many cite privacy concerns as a main reason for not disclosing individually. Until such a time when individual disclosure is legislated in Malaysia, this statistics is not expected to improve;

- it was quite easy to trip over errors in the companies’ annual reports, for example:
  - numbers in the Corporate Governance Statement do not match those in the Notes to the Financial Statements;
  - the band of RM50,000 has ‘accidentally’ become a band of RM500,000 or sometimes over RM1 million;
  - no upper limit is specified (e.g. the director is described as earning ‘more than RMx’); and
  - directors of subsidiaries only (i.e. not at the holding company level) are lumped into the remuneration numbers and it is impossible to filter out these directors.

Finally, a high level of judgement is required to sniff out the ‘de-facto executive director’ and exclude him from our study, lest his numbers result in an inflated NED remuneration.
The following table shows the top 30 payers from this study, and to make things more interesting we include a comparison with the top 30 from the 2009 study.

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<td></td>
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<td></td>
<td>Total NED Remuneration¹</td>
<td>Number of NEDs²</td>
<td>Remuneration per NED per annum</td>
<td>Remuneration per NED per annum</td>
<td>Position in 2009</td>
<td></td>
<td></td>
</tr>
<tr>
<td>1</td>
<td>Public Bank Berhad (3)#</td>
<td>Finance</td>
<td></td>
<td>3,554</td>
<td>5.3</td>
<td>671</td>
<td>463</td>
<td>1</td>
<td></td>
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<tr>
<td>2</td>
<td>Malayan Banking Berhad (1)</td>
<td>Finance</td>
<td></td>
<td>7,024</td>
<td>10.8</td>
<td>650</td>
<td>345</td>
<td>6</td>
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<tr>
<td>3</td>
<td>IHH Healthcare Berhad (13)</td>
<td>Trading/Services</td>
<td></td>
<td>3,425</td>
<td>5.8</td>
<td>591</td>
<td>^</td>
<td>^</td>
<td></td>
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</tr>
<tr>
<td>4</td>
<td>Sime Darby Berhad (4)</td>
<td>Trading/Services</td>
<td></td>
<td>5,967</td>
<td>11.2</td>
<td>533</td>
<td>353</td>
<td>5</td>
<td></td>
<td></td>
</tr>
<tr>
<td>5</td>
<td>MMC Corporation Berhad (38)</td>
<td>Trading/Services</td>
<td></td>
<td>2,947</td>
<td>6.0</td>
<td>491</td>
<td>172</td>
<td>24</td>
<td></td>
<td></td>
</tr>
<tr>
<td>6</td>
<td>CIMB Group Holdings Berhad (2)#</td>
<td>Finance</td>
<td></td>
<td>3,543</td>
<td>7.9</td>
<td>448</td>
<td>450</td>
<td>2</td>
<td></td>
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<tr>
<td>7</td>
<td>Axiata Group Berhad (5)</td>
<td>Trading/Services</td>
<td></td>
<td>2,770</td>
<td>6.5</td>
<td>426</td>
<td>383</td>
<td>4</td>
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<tr>
<td>8</td>
<td>MNRB Holdings Berhad (178)</td>
<td>Finance</td>
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<td>2,570</td>
<td>7.0</td>
<td>367</td>
<td>262</td>
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<tr>
<td>9</td>
<td>Allianz Malaysia Berhad (118)</td>
<td>Finance</td>
<td></td>
<td>1,505</td>
<td>4.1</td>
<td>367</td>
<td>167</td>
<td>28</td>
<td></td>
<td></td>
</tr>
<tr>
<td>10</td>
<td>Bumi Armada Berhad (33)</td>
<td>Trading/Services</td>
<td></td>
<td>2,666</td>
<td>7.5</td>
<td>355</td>
<td>^</td>
<td>^</td>
<td></td>
<td></td>
</tr>
<tr>
<td>11</td>
<td>SapuraKencana Petroleum Berhad (16)</td>
<td>Trading/Services</td>
<td></td>
<td>2,501</td>
<td>7.4</td>
<td>338</td>
<td>^</td>
<td>^</td>
<td></td>
<td></td>
</tr>
<tr>
<td>12</td>
<td>TDM Berhad (137)</td>
<td>Plantation</td>
<td></td>
<td>2,356</td>
<td>7.0</td>
<td>337</td>
<td>234</td>
<td>13</td>
<td></td>
<td></td>
</tr>
<tr>
<td>13</td>
<td>RHB Capital Berhad (21)</td>
<td>Finance</td>
<td></td>
<td>1,921</td>
<td>5.8</td>
<td>331</td>
<td>293</td>
<td>9</td>
<td></td>
<td></td>
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<tr>
<td>14</td>
<td>S P Setia Berhad (37)#</td>
<td>Property</td>
<td></td>
<td>2,238</td>
<td>7.0</td>
<td>320</td>
<td>223</td>
<td>15</td>
<td></td>
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<tr>
<td>15</td>
<td>Maxis Berhad (7)</td>
<td>Trading/Services</td>
<td></td>
<td>2,820</td>
<td>9.0</td>
<td>313</td>
<td>^</td>
<td>^</td>
<td></td>
<td></td>
</tr>
<tr>
<td>16</td>
<td>LPI Capital Berhad (74)#</td>
<td>Finance</td>
<td></td>
<td>1,561</td>
<td>5.0</td>
<td>312</td>
<td>169</td>
<td>26</td>
<td></td>
<td></td>
</tr>
<tr>
<td>17</td>
<td>Alliance Financial Group Berhad (39)#</td>
<td>Finance</td>
<td></td>
<td>2,393</td>
<td>7.9</td>
<td>303</td>
<td>249</td>
<td>12</td>
<td></td>
<td></td>
</tr>
<tr>
<td>18</td>
<td>DRB-Hicom Berhad (54)</td>
<td>Industrial Products</td>
<td></td>
<td>2,002</td>
<td>7.0</td>
<td>287</td>
<td>316</td>
<td>7</td>
<td></td>
<td></td>
</tr>
<tr>
<td>19</td>
<td>Astro Malaysia Holdings Berhad (28)#</td>
<td>Trading/Services</td>
<td></td>
<td>1,121</td>
<td>3.9</td>
<td>286</td>
<td>^</td>
<td>^</td>
<td></td>
<td></td>
</tr>
<tr>
<td>20</td>
<td>BIMB Holdings Berhad (66)</td>
<td>Finance</td>
<td></td>
<td>2,053</td>
<td>7.5</td>
<td>274</td>
<td>101</td>
<td>73</td>
<td></td>
<td></td>
</tr>
<tr>
<td>21</td>
<td>Telekom Malaysia Berhad (22)</td>
<td>Trading/Services</td>
<td></td>
<td>3,034</td>
<td>11.1</td>
<td>273</td>
<td>202</td>
<td>20</td>
<td></td>
<td></td>
</tr>
<tr>
<td>22</td>
<td>AirAsia Berhad (35)#</td>
<td>Trading/Services</td>
<td></td>
<td>1,706</td>
<td>6.3</td>
<td>271</td>
<td>^</td>
<td>^</td>
<td></td>
<td></td>
</tr>
<tr>
<td>23</td>
<td>Boustead Holdings Berhad (52)</td>
<td>Trading/Services</td>
<td></td>
<td>944</td>
<td>3.5</td>
<td>270</td>
<td>184</td>
<td>23</td>
<td></td>
<td></td>
</tr>
<tr>
<td>24</td>
<td>Felda Global Ventures Holdings Berhad (27)</td>
<td>Plantation</td>
<td></td>
<td>1,937</td>
<td>7.2</td>
<td>269</td>
<td>^</td>
<td>^</td>
<td></td>
<td></td>
</tr>
<tr>
<td>25</td>
<td>Media Prima Berhad (79)</td>
<td>Trading/Services</td>
<td></td>
<td>1,795</td>
<td>7.0</td>
<td>256</td>
<td>81</td>
<td>110</td>
<td></td>
<td></td>
</tr>
<tr>
<td>26</td>
<td>Affin Holdings (46)</td>
<td>Finance</td>
<td></td>
<td>2,211</td>
<td>8.7</td>
<td>254</td>
<td>213</td>
<td>17</td>
<td></td>
<td></td>
</tr>
<tr>
<td>27</td>
<td>Perisai Petroleum Teknologi Berhad (117)</td>
<td>Trading/Services</td>
<td></td>
<td>988</td>
<td>4.0</td>
<td>247</td>
<td>25</td>
<td>276</td>
<td></td>
<td></td>
</tr>
<tr>
<td>28</td>
<td>Kuala Lumpur Kepong Berhad (17)</td>
<td>Plantation</td>
<td></td>
<td>1,459</td>
<td>6.0</td>
<td>243</td>
<td>166</td>
<td>29</td>
<td></td>
<td></td>
</tr>
<tr>
<td>29</td>
<td>Tenaga Nasional Berhad (8)</td>
<td>Trading/Services</td>
<td></td>
<td>2,141</td>
<td>9.0</td>
<td>238</td>
<td>141</td>
<td>44</td>
<td></td>
<td></td>
</tr>
<tr>
<td>30</td>
<td>UMW Holdings Berhad (24)</td>
<td>Consumer Products</td>
<td></td>
<td>1,581</td>
<td>7.0</td>
<td>226</td>
<td>124</td>
<td>55</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Total | 74,733 | 209

Top 30 weighted average (RM’000) | 357 (year 2013) | 253 (year 2009)

* Ranking according to market capitalisation on Bursa Malaysia Securities Berhad, as at 30 June 2013.
1 These amounts and the number of NEDs have been adjusted by excluding the ‘de-facto executive director’, if deemed necessary.
2 An NED who serves on the board for less than the full financial year is pro-rated accordingly. An NED who served as executive director at subsidiary level is also excluded.
^ The company was not listed during the period the first study was conducted.
# An adjustment has been made to account for the “de-facto ED”.

RM’000  RM’000  RM’000

A number of companies in our top 30 table shows startling increases over the four-year period, in some cases more than doubling compared to the broad increase of 37%. What drove these companies to reach the levels of remuneration seen here? Could it be that top tier NEDs are reaching the pay levels they expect, or could a dearth of truly capable NEDs have contributed to the rise?

A theme from the top 30, in both studies, is the dominance by Government-linked Companies (GLCs). Why is this so? Perhaps:

- GLCs are expected to recruit top talent, including non-executive directors, into their boards and management teams;
- GLCs being large, high-profile and public-interest entities inevitably carry a higher profile and, therefore risk, compared to a non-GLC company;
- a GLC is typically more complex by virtue of its size, geographical reach and/or diversity of businesses under its control;
- directors are limited to five listed issuer seats by the GLC Transformation Manual, as opposed to a limit of ten PLCs as per the Listing Requirements of Bursa Malaysia (this limit has since been revised downwards to five listed issuers in 2012); and
- quite plainly, in the “Green Book” (Enhancing Board Effectiveness, Putrajaya Committee on GLC High Performance, 2006), it is suggested that boards of Government-linked Companies regularly review the compensation of directors and align the remuneration to “at least around the 50th percentile” of an appropriate peer group.

Our study shows that, by and large NEDs are remunerated based on fees (57%). This is an approach also common in other economies, and the proportion paid out as fees is not too far off the results of our 2009 study (at 53%).

**Covering yourself**

Professional indemnity insurance for directors (also known as directors and officers insurance – D&O) has its origins in the United Kingdom; however the main market developed in the US up to the 1980s before the practice spread to other economies.

The take up appears to be still low. In a 2011 survey by the Australian Institute of Company Directors, only 45% of respondents believed they had D&O insurance in place.

Given the increasingly litigious society that we live in, it may be pertinent for the directors to consider insurance as an integral part of their remuneration package.

(Source: American International Group, Australian Institute of Company Directors)
The relatively “low” remuneration for the foreign-controlled PLCs can likely be attributed to a number of factors, amongst them, alignment with the holding company’s remuneration scheme or the PLC’s position in the wider group (although a public-listed company, the company and group are subsidiaries which execute the main business strategy developed at the holding company level. In this regard, the role of the local board in the strategy setting process is limited).
WHY SHOULD THERE BE AN UPWARD TRAJECTORY IN NED REMUNERATION?

In recent years and especially the post 2007/2008 global financial crisis, companies have tried to move remuneration from a short term focus and extend the timeline in which a remuneration package is fully vesting.

The global financial crisis, in particular, made boards realise that it was management, and not the board, who was effectively running the company and calling the shots. Boards frequently did not understand, in full, the risks that management was taking and often found itself reduced to the role of a rubber stamp when presented with strategic issues.

After a tumultuous last few years, directors are now re-discovering their place at the top of the company and, in particular, NEDs are expected to vigorously exercise their oversight role.

Apart from the increase in scrutiny of NEDs, the following developments are timely considerations for the board and may collectively drive an upward trajectory for NED remuneration:

- the nominating committee is mandated from 1 June 2013. Public-listed companies would now need to set up this committee (if they have not previously done so), comprising at least two NEDs with majority independent;
- the duties of the nominating committee include assessing and selecting directors to the board and managing the performance evaluation process for the directors. Such duties, if undertaken in the manner intended by the stock exchange, would require significant thought, input and effort by the committee members;
- Bursa Malaysia has reduced to five being the maximum number of directorships for a director in listed issuers from a previous limit of 10 PLCs. The intent of this amendment is to enable directors to devote the necessary time to their boards. It does, however, curtail the director’s ability to serve on more boards even if he has the capacity and capability to do so;
- Bursa Malaysia in January 2013 launched the “Statement on Risk Management and Internal Control – Guidelines for Directors of Listed Issuers”. The guidelines recommend the chief executive officer and the chief financial officer to provide an assurance to the Board that the listed issuer’s risk management and internal control systems, as a group, are operating adequately and effectively, in all material aspects, for the financial year under review. The board must also affirm that it has reviewed the adequacy and effectiveness of the same risk management and internal control systems; and
How much time is needed?

The Walker Report (officially, “A review of corporate governance in UK banks and other financial industry entities”, November 2009), a well-noted publication authored by Sir David Walker, suggests a time commitment of 25 days is typically required from an NED of a large bank or financial institution. Sir Walker however cautioned that this time commitment is expected to increase with the need for more work in board committees.

In recent years, increases in penalties have been legislated. For example, the Capital Markets and Services Act 2007 was amended in 2010 where the penalties for causing a wrongful loss has been increased dramatically, i.e. a custodial sentence of up to ten years and a fine of up to RM10 million for directors and officers, if convicted. The corollary is that directors will be looking for a greater level of compensation for the risk that they take on when assuming directorships.
Two strikes and you’re out

The now infamous ‘two strikes’ law was introduced in Australia in July 2011 via an amendment to the country’s Corporations Act.

Essentially, the amendment was intentioned to hold directors more accountable for their remuneration, and works in the following manner:

- the company’s remuneration report is tabled at the annual general meeting (AGM). If 25% or more of shareholders vote against the report, this is the ‘first strike’;
- if the same happens the following year, a ‘second strike’ is recorded and at the same AGM, shareholders will vote whether all the directors need to vacate office and stand for re-election; and
- if 50% or more vote for re-election, a follow-up meeting is held within 90 days in which all the directors (except for the managing director) must submit themselves for re-election.

The last two years since the introduction of this provision has seen some turbulent general meetings and the issue of directors’ remuneration has taken unprecedented attention.

Opinion has been split, however, amongst regulators, shareholder activists, fund managers and corporate directors. Whilst some quarters enthuse about the positive effect the rule has had on directors’ pay, others wail about the abuse by shareholders to target boards for reasons totally unrelated to pay.

During the 2011 AGM season, more than 100 ASX companies, or around 5% of the total population of listed companies, received a ‘first strike’.

(source: Henry Davis York, corporate lawyers, Australia)
Save the most controversial topic for last, should NEDs be compensated in line with the company’s (group’s) performance and results?

Bursa Malaysia clearly states that NEDs are to be paid by a fixed sum, and forbids remuneration by commission or a percentage of revenue.

In overseas jurisdictions, the UK Corporate Governance Code, for example, advises against share options or other performance-based remuneration. If share options are to be granted, the code recommends that shareholder approval is sought and on top of that, the exercise of those options is held back until at least one year after the NED leaves the board.

The Sarbanes-Oxley Act of the US, meanwhile, contains provisions against the payment of profit-related commissions to independent directors.

The intent of the above-mentioned provisions is obvious: The argument is made against performance-based remuneration because this could impair the NED’s objectivity and independence, particularly when asked to endorse risky business decisions that may have a vast upside potential.

On the other hand, the most compelling reason for performance-based remuneration is since all the directors are supposed to work towards the best interest of the company, why deny a large portion of the board its due reward? Conversely, if the company suffers a downturn in its fortunes, why should the NEDs continue to receive their remuneration at a fixed amount?

Thus, proponents of performance-based remuneration argue that current practices may not incentivise NEDs enough towards working for the success (and preventing failure) of the company.
A small number of NEDs in our study do receive share options. If a company desires to reward its NEDs in ways other than fees, it could consider paying through share options. This path is, however, fraught with pitfalls and it is vital that adequate safeguards are put in place by the company. Some examples of safeguards are as follows:

- a long term vesting period, including up to a certain period after the NED has left the board;
- the company should seek shareholders’ approval for the remuneration plan; and
- the company should be transparent about the intent of the remuneration plan, the level of remuneration and the process deployed in ascertaining the quantum of share options awarded to the NEDs.

Whilst we obviously are not advocating PLCs remunerating their NEDs based on performance (given also the prohibitions contained in the Listing Requirements), we think the time has come to have a debate on the merits of performance-based compensation for non-executive directors.

**Being invested in your company, literally**

Interestingly, the Association of British Insurers (ABI) advocates non-executive directors holding shares in their companies. It also suggests that NEDs may receive part of their remuneration in the form of shares, purchased at market price.
Every issue of the Audit Committee Insights newsletter has exclusive KPMG analysis.

Developed by our professionals, the newsletters leverage the thought leadership behind KPMG’s Audit Committee Institute (ACI). The newsletters provide access to ACI updates and unique insights that can help you understand the changing nature and emerging trends of the audit environment.

The Audit Committee’s Oversight Role on Financial Reporting 2013 – Are the numbers too good to be true?

Sheds light on the organizations’ and the Audit Committee’s role in the financial reporting process. This survey questions elicited the opinions of participants and analysed their answers to questions posed vis-à-vis better practices.

Global Boardroom Insights 2013

Audit committee chairs from global organisations in Brazil, Germany, the U.S. and UK offer perspectives on a range of issues, including lessons learned from the past several years; keys to maintaining strong audit committee/auditor communications; how the speed of technology change and an increasingly complex risk environment are impacting the audit committee and board agenda; and more.

Remuneration Committee: Time To Raise The Bar?

Is centred on the changing remuneration landscape of some developed economies, and provides much needed literature on this very current topic.

Directors Prism

This publication identifies a listing of 7 probing questions, compiled with a view to helping shape success for boards and directors.

2009 Non-Executive Directors: Profile, Practices & Pay

This ground-breaking publication aims to provide boards of PLCs with an understanding of a non-executive director’s profile, role and remuneration in Malaysia. Published in 2009, it is the precursor to this current study.
Appendix 1: METHODOLOGY AND ASSUMPTIONS

- This study is based on publicly available information of companies listed on the Main Market of Bursa. If necessary, further information was obtained from the websites of the relevant company.
- The analysis of remuneration received by NEDs is limited to the most recent annual report of each company.
- The top 300 companies on the Bursa Malaysia Main Market are ranked by market capitalisation as at 30 June 2013.
- The remuneration of NEDs is classified into three (3) main categories, namely:
  - fees (inclusive of allowances);
  - other non-fee remuneration; and
  - benefits-in-kind.
- If an NED has served for less than a year, his tenure of service is pro-rated accordingly.
- Where information was ambiguous or unavailable, we have not used the data or information in the study. Clarity of data was pivotal to the accuracy of our study.
- Where remuneration between the financial statements and the corporate governance statement differed, data that most accurately reflected remuneration received by non-executive directors of the holding company was used.
- For a number of foreign-controlled companies, certain Non-Executive Directors received their remuneration from the foreign holding company. These directors were excluded from the study in cases where their remuneration was not disclosed.
- We observed that remuneration of certain Non-Executive Directors was high relative to their peers within the same company. This could be due to any, or a combination of, the following factors:
  - founders who remain with the company as Non-Executive Directors are able to command significant levels of remuneration; or
  - NEDs who are family members of Executive Directors and they may receive remuneration that is comparatively higher than their fellow NEDs; or
  - there are Directors who are classified as Non-Executive Directors at the holding company level, but serve as chief executives, executive directors or executive advisors of the listed issuer’s principal subsidiary(ies), where the core activities/operations of the group reside in.

For reasons outlined above, these Directors are termed as “de-facto Executive Directors” and, accordingly, are excluded from our study.
Appendix 2:

COMPARISON OF HEADLINE NUMBERS IN THE 2013 STUDY VS. THE 2009 STUDY

Note: The remuneration and the number of NEDs have been adjusted by excluding the ‘de-facto executive director’, if deemed necessary. An NED who serves on the board for less than the full financial year is pro-rated accordingly.

Table 1: Headline remuneration

<table>
<thead>
<tr>
<th>Category</th>
<th>2013 study</th>
<th>2009 study</th>
<th>Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>Top 300 market-capitalised companies on Bursa Malaysia</td>
<td>RM122,000</td>
<td>RM89,000</td>
<td>+37%</td>
</tr>
<tr>
<td>Top 300 market-capitalised companies on Bursa Malaysia, with Government-linked Companies (GLCs) excluded</td>
<td>RM98,000</td>
<td>RM77,000</td>
<td>+27%</td>
</tr>
<tr>
<td>Top 300 market-capitalised companies on Bursa Malaysia, with Government-linked Companies (GLCs) and financial institutions excluded</td>
<td>RM90,000</td>
<td>RM72,000</td>
<td>+25%</td>
</tr>
</tbody>
</table>

Table 2: Remuneration for the top 100 companies, next 100 companies and final 100 companies

<table>
<thead>
<tr>
<th>Category</th>
<th>2013 study</th>
<th>2009 study</th>
<th>Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>No 1 to 100-ranked companies, by market capitalisation</td>
<td>RM182,000</td>
<td>RM160,000</td>
<td>+14%</td>
</tr>
<tr>
<td>No 101 to 200-ranked companies, by market capitalisation</td>
<td>RM98,000</td>
<td>RM63,000</td>
<td>+56%</td>
</tr>
<tr>
<td>No 201 to 300-ranked companies, by market capitalisation</td>
<td>RM65,000</td>
<td>RM32,000</td>
<td>+103%</td>
</tr>
</tbody>
</table>
### Table 3: Remuneration by sector
*(sorted by sector with the highest remuneration in the 2013 study, to the lowest)*

<table>
<thead>
<tr>
<th>Sector</th>
<th>2013 study</th>
<th>2009 study</th>
<th>Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>Finance</td>
<td>RM239,000</td>
<td>RM150,000</td>
<td>+59%</td>
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<tr>
<td>Trading/Services</td>
<td>RM148,000</td>
<td>RM83,000</td>
<td>+78%</td>
</tr>
<tr>
<td>Infrastructure Project Companies</td>
<td>RM110,000</td>
<td>RM80,000</td>
<td>+38%</td>
</tr>
<tr>
<td>Plantations</td>
<td>RM106,000</td>
<td>RM68,000</td>
<td>+56%</td>
</tr>
<tr>
<td>Construction</td>
<td>RM89,000</td>
<td>RM84,000</td>
<td>+6%</td>
</tr>
<tr>
<td>SPAC</td>
<td>RM87,000</td>
<td>N/A</td>
<td>N/A</td>
</tr>
<tr>
<td>Consumer Products</td>
<td>RM84,000</td>
<td>RM60,000</td>
<td>+40%</td>
</tr>
<tr>
<td>Industrial Products</td>
<td>RM84,000</td>
<td>RM70,000</td>
<td>+20%</td>
</tr>
<tr>
<td>Technology</td>
<td>RM83,000</td>
<td>RM62,000</td>
<td>+34%</td>
</tr>
<tr>
<td>Properties</td>
<td>RM78,000</td>
<td>RM63,000</td>
<td>+24%</td>
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<tr>
<td>Hotels</td>
<td>RM54,000</td>
<td>RM41,000</td>
<td>+32%</td>
</tr>
<tr>
<td>Closed-end Funds</td>
<td>RM40,000</td>
<td>RM20,000</td>
<td>+100%</td>
</tr>
</tbody>
</table>
about the author

Darren Lee Siet Loon
Darren is a Director in the Internal Audit, Risk and Compliance practice of KPMG in Malaysia. He advises clients on corporate governance, enterprise risk management and internal audit engagements. He also authored the 2009 publication issued by the Audit Committee Institute covering the profile, practices and pay of the Non-Executive Directors in Malaysia.

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