RESEARCH CONTRIBUTION FROM UNIVERSITIES IN MALAYSIA

CORPORATE GOVERNANCE AND DIRECTORS' REMUNERATION IN MALAYSIAN PUBLIC LISTED COMPANIES

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Over the past decade, the issue of compensation for top executives has been the subject of empirical research due to agency problems that might be manifested as a result of separation of ownership and control. Research into how executives are rewarded caught wide public interest in the Western countries and now has also captured the attention of Malaysians. This is more apparent particularly after a series of financial crises.

The massive distortion in the economic system during the Asian financial crisis has alerted Malaysians of the effectiveness of Corporate Governance practices, accounting and auditing standards and the levels of compliance. There is an increasing call from shareholders and investors for greater transparency in directors' remuneration disclosure. More efforts had been put in to reinforce the law and accounting rules, regulation of disclosure, Corporate Governance process, internal and external auditing. Since then the dual reforms of Corporate Governance and accounting began.

To regain investors' confidence and secure further financial growth, the Malaysian Accounting Standard Board (MASB, thereafter), Bursa Malaysia and Securities Commission have been entrusted for the reformation in Malaysia. MASB introduced Financial Reporting Standards framework (FRS) for financial periods beginning on or after 1 January 2006 and it was further enhanced by the issuance of the Malaysian Financial Reporting Standards framework (MFRS, thereafter) for annual periods beginning on or after 1 January 2012. To draw attention to the possibility that the financial reports may have been affected by the existence of related parties and by transactions, FRS 124 was revised in 2006 which requires disclosures about employee benefits for key management personnel including directors. In 2012, the Malaysian Code on Corporate Governance (MCCG thereafter) was further revised to focus on clarifying the role of the board in providing leadership, improving board effectiveness through strengthening board composition and reinforcing board independence. At the same time, Bursa Malaysia through Bursa Malaysia Listing Requirements (Bursa LR, thereafter) sets out greater obligations for public listed companies (PLC, thereafter) in financial reporting, disclosure on Corporate Governance matters and continuing listing obligations.

In term of directors' remuneration, the Bursa LR requires companies to disclose in bands of RM50, 000 their directors' remuneration without disclosing the identity of recipients, while the MCCG recommends PLCs to disclose board remuneration policies and procedures in the annual report. These disclosures in the financial reports which were previously treated as private and confidential information have received much attention not only from investors and shareholders, but also from researchers.

Traditionally, the literature on directors' remuneration in Malaysia highlighted a troubling issue, that is, there is no link between company's performance and directors' remuneration. For instance, some companies on Bursa Malaysia, despite making losses, are paying their directors top dollars. According to the MCCG, the amount of directors' remuneration should be sufficient to attract and retain the directors needed to run a company successfully. Also to structure it in such a way linking rewards to corporate and individual performance. Generally, the criteria used to set directors' remuneration are the size of the company, its profit, sale growth and turnover. But the absence of any clear cut guideline has created room for manipulation by directors.

Agency theory suggests that directors' remuneration need to be correlated with the total return to shareholders. Evidence have shown that directors should be rewarded based on company's performance. Without good Corporate Governance in a company, directors are paid excessively at the cost of shareholders.

Locally, studies were conducted to examine the relationship between directors' remuneration and the board characteristics. They include board size, board independence and CEO-duality and managerial ownership. The findings of this study support the point that shareholders' interests are best served when the board size and firm size is small and the ownership is concentrated. This also implies that directors' remuneration are better managed in companies that are relatively small and held by the same group of people.

It is also found that the level of directors' remuneration is not related to board independence, CEO-duality, managerial ownership and independent non-executive directors' interest. Instead, the major determinants of directors' remuneration are firm size, leverage and performance. The results of the study revealed that directors' remuneration for Malaysian firms are based on economic factors. As such, it is evident that Malaysian companies are moving towards linking remunerations to performance which is consistent with the trend of the world.

Having said that, more can be done in Corporate Governance so as to boost investors' confidence, especially in increasing disclosure and transparency. In the current state where the data disclosed to public is insufficient, there is a high possibility that some forms of compensation will go unnoticed, thus giving the impression of lower remuneration among Malaysian companies. Directors may use non-cash forms of compensation to avoid public scrutiny. Greater transparency will reduce the costs in obtaining information on remuneration and improve on directors' accountability. Disclosure is clearly an important tool to solve the agency problems on directors' remuneration and effectively lead companies to pay directors based on company performance.

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