



MALAYSIAN RATING CORPORATION BERHAD (364803-V)

# **POLICY ON CONFLICT OF INTEREST FOR ANALYSTS AND RATING COMMITTEE MEMBERS**

Version 2.0

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## **1. Introduction**

The purpose of the Policy on Conflict of Interest (the Policy) is to define the management of potential conflicts of interest on the part of analysts and rating committee members. Purposeful compliance with this policy will avoid both actual bias and appearance of bias and ensure that Conflict of Interest (COI) disclosures are made and disclosed in a manner that will allow users of Malaysian Rating Corporation Berhad's (MARC) credit ratings to make an informed decision about the existence and the impact of conflicts of interest.

The policy is designed to promote compliance with the COI provisions in the Securities Commission's (SC) Guidelines on the Registration of Credit Rating Agencies of 30 March 2011 and MARC's Code of Conduct.

## **2. Conflicts of Interest**

In the context of the rating process, a 'conflict of interest' exists where it appears that an analyst's performance of his/her duties and responsibilities as analyst or a Rating Committee (RC) member's professional judgement may be improperly influenced by competing responsibilities or interests. Under these guidelines, any real or perceived potential competing interests or compromising influences – financial, personal, or other situations that might raise the question of bias – have to be disclosed.

The consequences of acting with an undisclosed conflict of interest can be severe for both MARC and the individual. This can result in a breach of the SC Guidelines on the Registration of Credit Rating Agencies and regulatory sanctions. In addition, serious consequences could also result from a proven claim in contract or tort. At an individual level, this could result in disciplinary action.

## **3. Responsibilities of Analysts, Rating Committee Members and Portfolio Heads**

- 3.1 All analysts and RC members are responsible for:
- (i) being aware of their obligation to avoid, where possible, conflicts of interest and manage those conflicts of interest that cannot be avoided;
  - (ii) assessing potential conflicts of interest that could affect the rating process for both new and existing rating mandates; and
  - (iii) formally disclosing all conflicts of interest and reportable interests they may have according to the procedures set out in this Policy and/or pursuant to MARC's Code of Conduct. Reportable interests relating to parents, child or sibling of the analysts and RC members are to be disclosed on a 'best of knowledge' basis. The qualifier, however, shall not be extended to the spouses of the analysts and RC members.

- 3.2 Portfolio Heads supervising analytical team members are responsible for:
- (i) being aware of the risks of conflicts inherent in the work of staff they manage;
  - (ii) making staff aware of the policy and procedures for complying with it;
  - (iii) recording the receipt of disclosures of conflicts of interest reported to them by staff;
  - (iv) advising staff on appropriate ways to manage conflicts; and
  - (v) monitoring the work of staff and the risks they are exposed to.

#### **4. Identifying Conflicts of Interest**

##### 4.1. Definitions

###### Pertaining to the RC members:

“Immediate family” is defined to include an individual’s spouse, parents, children and siblings.

The term “family member” has the meaning ascribed to it in the SC’s Guidelines on the Registration of Credit Rating Agencies and includes (i) a spouse, (ii) parent, and (iii) child (including adopted or stepchild) or sibling of the individual or his/her spouse.

A “significant” financial interest refers to an equity interest that when aggregated for the RC member and his immediate family member(s) represents more than 5% ownership interest in the entity concerned.

A “non-significant but material” financial interest refers to an equity interest that when aggregated for the RC member and his immediate family member(s) represents 0.1% to 5% ownership interest in the entity concerned.

A “non-significant” financial interest refers to an equity interest that when aggregated for the RC member and his/her immediate family member(s) does not represent more than 0.1% ownership interest in the entity concerned.

###### Pertaining to related entity being rated:

A “related” entity is deemed to be related to another entity for the purposes of this policy if they meet any of the following criteria: one entity is the parent or subsidiary of the other and/or one entity owns directly or through one or more entities an **effective** 50% or greater interest in the capital or profits of the other.

#### 4.2. Conflicts of Interest at the Analyst Level

The following list provides some examples of the type of situations that may give rise to a COI. The list is not exhaustive. Situations, whether listed below or not, that have the appearance of, potential for, or involve actual conflicts of interest should be disclosed.

At the analyst level, conflicts of interest mainly arise when the individual has a personal interest in the outcome of the rating process as a result of:

- a) personal or family ownership of securities in an entity which is a related entity of the entity whose rating is being deliberated other than ownership interests held through diversified collective investment schemes;
- b) family member's business ties with an entity that has dealings with an entity which is closely linked with the rating under deliberation or whose rating is being deliberated;
- c) a family member's employment or membership on the board of directors of the entity whose rating is being deliberated or any other entity having an interest in the rated security;
- d) recent employment (within the last six months) with the entity whose rating is being deliberated;
- e) a business relationship with the rated entity that appears to be other than "arm's length"; and
- f) acceptance of any gift and/or other forms of benefit exceeding RM300 in value from the entity whose rating is being deliberated that could reasonably appear to influence his/her independence of judgement.

**An analyst should not participate in the RC proceedings where the analyst or any of his family members has interest in the entity being deliberated.**

#### 4.3. Conflicts of Interest at the Rating Committee Level

MARC recognises that conflicts of interest on the part of non-employees or external RC members are not always avoidable and it would be impractical to embrace a general policy which would prevent participation in RC proceedings by individuals having associations which may represent conflicts of interest. Where a potential COI has been identified and the RC meeting proceeds with the conflicted member's participation, the potential COI should be documented in a COI Register and minutes of meetings. A summary disclosure of the potential COI should then be made in the rating report concerned.

#### 4.4. Levels of Conflict of Interest

In addition to disclosing the COI, MARC recognises that it is beneficial to identify and categorise various levels of conflict at the RC level to determine the degree of significance of the conflict. This process ensures all conflicts of interest are not merely identified and disclosed but also allows 'major' potential conflicts of interest to be differentiated from 'minor' potential conflicts of interest so that they can be addressed in a rigorous and transparent manner.

##### Level 1 – major significance

A Level 1 COI may arise as a result of:

- a) personal or significant immediate family ownership of securities in an entity which is closely linked with the rating under deliberation or whose rating is being deliberated, other than ownership interests held through diversified collective investment schemes;
- b) a family member's employment or membership on the board of directors of the entity whose rating is being deliberated or its related entity;
- c) the individual's substantive involvement in the making, monitoring and realisation of investments held or dealt in on behalf of clients in securities of an entity whose rating is being deliberated or its related entity;
- d) current or recently concluded employment (within the last six months) at the entity whose rating is being deliberated, including current or prior involvement as a consultant or advisor; and
- e) current or recently concluded membership (within the last two years) on the board of directors of the entity whose rating is being deliberated.

Internal RC members with a Level 1 COI should not participate in the RC proceedings where the aforementioned associations exist, and shall leave the meeting when the rating concerned is being discussed.

Upon appropriate disclosure of the Level 1 COI by external RC members, it shall be the responsibility of the RC to determine whether such potential COI warrants i) exclusion from the deliberations, or ii) abstention from voting, or iii) exclusion from the committee proceedings, under all of the attendant circumstances.

The external member with a Level 1 conflict may be requested to remain in the meeting if his/her attendance is required to achieve the quorum for the rating committee meeting. The COI will be recorded appropriately in the minutes of the meeting and in a secure register.

In some cases, an individual who is a member of the board of directors of an entity which is a related entity with the rating under deliberation may not be regarded as having a Level 1 COI, e.g. securitisation financing transaction by a special purpose vehicle. For such cases, it will depend on the subject of the rating and shall be determined by the RC member who has no interest in the particular proceedings.

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Level 2 – medium significance

A Level 2 COI may arise as a result of:

- a) non-significant but material ownership of securities by the RC member and/or family members in an entity whose rating is being deliberated or its related entity;
- b) family member's business ties with an entity that has dealings with an entity which is closely linked with the rating under deliberation or whose rating is being deliberated;
- c) any interest arising solely by reason of affiliation through an advisor-client relationship with an institutional investment fund which has ownership of securities in the entity whose rating is being deliberated or its related entity;
- d) any interest arising solely by reason of ownership in an investment management services provider which has ownership of securities in the entity whose rating is being deliberated or its related entity;
- e) any interest arising solely by reason of ownership in a research firm or investment management entity that issues research and investment recommendations on an entity whose rating is being deliberated or its related entity;
- f) previous employment of more than two years ago at the entity whose rating is being deliberated; and
- g) previous membership of more than two years ago on the board of directors of the entity whose rating is being deliberated.

An internal RC member with a Level 2 COI does not have to leave the meeting when the rating concerned is being discussed but will not have voting rights.

Level 2 COI must be advised to the RC which will note and monitor the ongoing relevance of these conflicts. They will also be recorded appropriately in the minutes of meeting and in the COI Register. These conflicts will be monitored by the Compliance and Risk Management Department (CRM).

Level 3 – minor significance

Level 3 COI generally are not so significant that they could cast doubt on an RC member's ability to act impartially and give their unbiased consideration to the matter at hand. A Level 3 COI conflict must be advised to the RC. An example of a Level 3 COI is non-immediate personal or family ownership of a non-significant and non-material amount of securities in the entity whose rating is being deliberated or its related entity.

Where a member has more than one level of potential or actual conflicts of interest for the entity whose rating is being deliberated, the higher degree of significance shall be used to determine the level of the conflict.

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**5. Declaring Conflicts of Interest**

## 5.1. At the Analyst Level, individuals:

- 5.1.1. must complete a conflict of interest form, declaring any potential conflict of interest prior to undertaking a new issue rating assignment or a review of an existing rating;
- 5.1.2. bring to the attention of his supervisor any actual, potential or apparent conflicts of interest that may impact his ability to undertake the rating and monitoring process;
- 5.1.3. have a responsibility to inform his supervisor immediately to ensure that the conflict is removed, or managed to the satisfaction of the Designated Risk Officer of Ratings and the CRM where a change of circumstances results in an analyst having a declarable interest; and
- 5.1.4. must provide a quarterly 'Declaration of Conflict of Interest by Rating Analyst Who is Involved in the Rating Process' and update that information as and when required by CRM.

## 5.2. At the Rating Committee Level, individuals:

- 5.2.1. are required to assess whether he has an actual, reasonably perceived or potential COI arising from any current or previous personal, professional or financial relationship or association of any significance with an entity which is closely linked with the rating that will be deliberated or whose rating will be deliberated;
- 5.2.2. bring to the attention of the RC Secretary any actual, potential or apparent conflicts of interest that may impact his/her ability to participate in the rating deliberation concerned;
- 5.2.3. disclose the reportable interest at the RC meeting to determine the significance of the conflict and enable an adequately informed decision to be made by the RC on the extent to which that member may be involved in discussion or decisions of the rating concerned;
- 5.2.4. take all reasonable steps to prevent any identified potential COI from becoming an actual COI; and
- 5.2.5. provide updated information to the RC Secretary promptly if there is a significant change to his/her or their immediate family's interests as they become aware of those changes.

**6. Register of Interests**

The COI register is maintained by MARC's Compliance Officer under the CRM. This information will be reviewed half yearly by the CRM to ensure the information is accurate and complete. The information in the register is open to the public for inspection upon request, subject to the limitations of the Personal Data Protection Act 2010. Any individual who wishes to inspect an entry in the COI register must apply in writing to MARC's Compliance Officer, who must record who has been given access and inform the person(s) whose COI disclosure had been inspected.



## **7. Enforcement and Disciplinary Action**

Failure to disclose conflicts of interest in an appropriate and timely manner or failure to comply with procedures to resolve conflicts of interest as recommended by CRM Department may result in disciplinary action or sanctions. The Audit and Compliance Committee is charged with the responsibility to consider alleged violations of the disclosure requirements and other provisions of these guidelines, to investigate complaints of such violations, and to recommend appropriate sanctions.