

# CORPORATE GOVERNANCE STATEMENT

LPI Capital Bhd ("LPI") Group recognises the importance of enhancing shareholders' value through continued profitability and fostering the highest standards of corporate governance. The Board of Directors ("Board") strongly believes that good corporate governance is vital in enhancing the long-term performance and continuous growth of LPI Group. Hence, a sound governance structure is fundamental to safeguard the interests of LPI Group's shareholders.

LPI Group's corporate governance structure has been developed and enhanced based on the principles and best practices prescribed in the Malaysian Code on Corporate Governance ("MCCG") issued by the Securities Commission and the Corporate Governance Guide ("CG Guide") issued by Bursa Malaysia Berhad. The commitment of the Board, Management and staff of LPI Group in enhancing shareholder value is affirmed by the numerous awards and recognition that LPI Group received every year since 2005, of which those received in 2009 include the following:

## 1) Malaysian Business - CIMA Enterprise Governance Awards 2009

- **Merit Award**

LPI had won the Merit Award of the Malaysian Business - CIMA Enterprise Governance Awards for the fifth consecutive year. In 2008, LPI was also a winner in Best Return to Shareholders of the same award.

## 2) KPMG Shareholder Value Award 2008

- **Sectoral Winner - Financial Services**
- **Winner - Financial Services**

LPI was conferred a winner of the KPMG Shareholder Value Award 2008 for the fifth consecutive year. LPI was also the Sectoral Winner under the Financial Services Category in 2005, 2006 and 2008.

## 3) Euromoney 2009 "Best Insurer in Malaysia" Award

LPI's wholly-owned subsidiary, Lonpac Insurance Bhd ("Lonpac") bagged all the five (5) categories of the Euromoney 2009 awards to emerge as the Euromoney 2009 Best Insurer in Malaysia. The five categories won are as follows:

Best Insurer for Innovation, Malaysia

Best Insurer for Price, Malaysia

Best Product Range, Malaysia

Best Insurer for Claims Resolution, Malaysia

Best Consultant for Insurance Risk Transfer, Malaysia

**EUROMONEY 2009 BEST INSURER IN MALAYSIA**

## 4) Malaysian Corporate Governance ("MCG") Index 2009

- **Most Timely Held Annual General Meeting Award**
- **Distinction Award**

LPI was conferred the Most Timely Held Annual General Meeting Award and Distinction Award of the MCG Index 2009 by the Minority Shareholder Watchdog Group ("MSWG"). In 2009, LPI was the first public listed company to hold its Annual General Meeting within 43 days after the financial year end.

## 5) Excellent Financial Strength Rating by A.M. Best

Lonpac is rated financial strength rating of A- (Excellent) and issuer credit rating (ICR) of "a-" by A.M. Best.

## BOARD OF DIRECTORS

The Board is fully committed to ensure that the highest standards of corporate governance are observed throughout the Group so that the affairs of the Group are conducted in a transparent and objective manner with full accountability and integrity to safeguard shareholders' investment and ultimately enhancing their value.

## I DIRECTORS

### • The Board

The Board is responsible for the overall governance of the Group by ensuring the strategic guidance and succession plan of the Group, the effective monitoring of

management goals, and accountability to the Group and shareholders as well as ensuring that the Group's internal controls, risk management and reporting procedures are well in place. The Board Members exercise due diligence and care in discharging their duties and responsibilities to ensure that high ethical standards are applied, through compliance with relevant rules and regulations, directives and guidelines in addition to adopting the best practices in the MCCG issued by the Securities Commission and CG Guide issued by Bursa Malaysia Berhad, and act in the best interest of the Group and shareholders.

The Board Members are attentive to applying high ethical standards, taking into account of the interests of all stakeholders, in their decision-making.

#### • **Optimum Board Balance**

The Board consists of seven (7) Members. One of the Board Members is an Executive Director and also the Chief Executive Officer while six (6) are Non-Executive Directors. Four (4) of the Non-Executive Directors fulfill the criteria of independence as defined in the Bursa Securities Listing Requirements. The size of the Board is appropriate for the complexity and scale of operations of the LPI Group. The high proportion of Independent Non-Executive Directors provides for effective check and balance in the functioning of the Board.

The Independent Non-Executive Directors do not engage in the day-to-day management of the Group and do not participate in any business dealings and are not involved in any other relationship with the Group. This is to facilitate the Independent Non-Executive Directors to discharge their duties and responsibilities effectively and to avoid any conflict of interest situations.

There is a clear division of roles and responsibility between the Chairman/ Co-Chairman and the Chief Executive Officer/ Executive Director. The terms of reference of the Non-Executive Chairman and the Independent Non-Executive Co-Chairman are distinct and separate from the duties and responsibilities of the Chief Executive Officer/ Executive Director to ensure a balance of power and authority in an effective Board.

Tan Sri Dato' Sri Dr. Teh Hong Piow, the Founder and Chairman of LPI and Public Bank, has been acclaimed as a Banking Grandmaster. He is also an exceptionally

outstanding and accomplished leader and businessman. Since embarking on his financial odyssey 60 years ago, he has carved out an eminent career in the financial industry. His success has led LPI Group's wholly-owned subsidiary, Lonpac to be recognised as the Best Insurer in Malaysia for 2009 by Euromoney. Tan Sri Dato' Sri Dr. Teh Hong Piow has been conferred with many prestigious awards in recognition of his significant contributions to the banking and finance industries, and for his socioeconomic development initiatives.

The Independent Non-Executive Co-Chairman, Tan Sri Dato' Thong Yaw Hong, is well regarded and highly prominent in both the public and private sectors. He had held various distinguished and senior positions while serving the Government for 32 years. Upon his retirement from public service, he joined the private sector and was appointed as Chairman/ Director of several large public listed corporations. He is a Member of the National Economic Council, established by the Government to address the adverse effects of the global financial slowdown on the economy. He is also a Senior Member of the Working Group of the Executive Committee for the National Economic Council engaged in the formulation and implementation as well as monitoring of the Economic Stabilisation Plan (ESP) of the Government.

The other three (3) Independent Non-Executive Directors are professionals in their own right with wide-ranging experiences, skills and expertise in various fields.

The Directors of LPI Group are persons of high calibre and integrity, and they possess the necessary qualifications, experience and qualities that enable them to perform their duties effectively.

The profiles of the Members of the Board are presented on pages 50 to 55.

#### • **Directors' Code of Ethics**

The Directors continue to adhere to the Code of Ethics for Company Directors issued by the Companies Commission of Malaysia. The code is based on principles in relation to sincerity, integrity, responsibility and corporate social responsibility and is formulated to enhance the standard of corporate governance and corporate behaviour.

### • Duties and Responsibilities of the Board

The core responsibilities of the Board include reviewing and approving the Group's business strategies and plans, significant policies, and monitoring the Management's performance in implementing them.

In carrying out their duties and responsibilities, the Board exercises great care to ensure that high ethical standards are upheld, and that the interests of stakeholders are not compromised. The Board Members are constantly mindful that the interests of the Group's stakeholders are always being protected.

The four (4) Independent Non-Executive Directors, by virtue of their roles and responsibilities, in effect represent the minority shareholders' interests in LPI Group. The Independent Non-Executive Directors engage proactively with the Management and with both the external and internal auditors. This is particularly so in the case of Tan Sri Dato' Thong Yaw Hong who is the Chairman of the Audit Committee and Risk Management Committee and Dato' Haji Abdul Aziz who is the Co-Chairman of the Audit Committee.

The Independent Non-Executive Co-Chairman, Tan Sri Dato' Thong Yaw Hong, is the designated Senior Independent Non-Executive Director to whom concerns relating to the Group may be conveyed by the shareholders and other stakeholders.

The Board's principal functions include the following responsibilities:

- Approves the Group's annual business plans, and the medium-term and long-term strategic plans;
- Oversees the Group's business operations and financial performance against the approved business plans;
- Ensures that the operating infrastructure, systems of control, systems for risk management, financial and operational controls, are in place and properly implemented; and
- Undertakes various functions and responsibilities as specified in guidelines and directives issued by the regulatory authorities from time to time.

The Directors are at liberty to obtain advice from independent professionals if deemed necessary for the proper discharge of their duties at the expense of the Company.

### • Board Meetings and Supply of Information to the Board

Board meetings for each financial year are scheduled in advance before the end of the each financial year so as to enable the Directors to plan accordingly and fit the year's Board meetings into their respective schedules.

Board meetings are usually conducted on a quarterly basis. Board meetings are convened immediately upon the finalisation of the LPI Group's quarterly and annual results to review and approve the results for submission to Bursa Securities. Additional Board meetings are also held when warranted by situations such as to deliberate urgent corporate proposals or matters that require the expeditious direction of the Board.

Board meetings are conducted in accordance to a structured agenda. Board Members are provided with the structured agenda together with the relevant documents and information in a form and of a quality appropriate in advance of each Board meeting. This is to facilitate the Directors to peruse the Board papers and seek clarifications that may require from the Management or the Company Secretary well ahead of the meeting date. Urgent papers may be presented for tabling at the Board meetings under supplemental agenda.

The Board meetings are chaired by either Tan Sri Dato' Sri Dr. Teh Hong Piow (Chairman) or Tan Sri Dato' Thong Yaw Hong (Co-Chairman).

At the Board meetings, the Board reviews management reports on the business performance of the Company and its subsidiary, and reviews, inter-alia, the results compared to the preceding month and year-to-date, and also the comparison against the industry. As part of the integrated risk management initiatives, the Board peruses the decisions and salient issues deliberated by Board Committees and Management Committee through minutes of these committees. The Board Members also deliberate, and in the process, evaluate the feasibility of business propositions and corporate proposals as well

as any principal risks that would have significant impact on the Group's business and the measures to mitigate such risks.

The Chairman/ Co-Chairman of the Audit Committee would inform the Directors at Board Meetings, of any significant issues noted by the Audit Committee and which require the Board's attention and approval for implementation.

The papers of the Board meetings are presented in a concise and comprehensive format. Board meeting papers include progress reports on business operations, detailed information on business propositions and corporate proposals including the relevant supporting documents.

The Directors have a duty to make an immediate declaration to the Board if they have any interest in transactions to be entered into directly or indirectly with LPI Group. The interested Directors would serve notice to the Board and thereupon abstain themselves from deliberations and decisions of the Board on the transaction. In the event a corporate proposal is required to be approved by shareholders, the interested Directors will abstain from voting in respect of their shareholdings in LPI on the resolutions relating to the corporate proposal, and will further undertake to ensure that persons connected to them similarly abstain from voting on the resolutions.

Minutes of Board meeting are circulated to all Directors for their perusal prior to the confirmation of the minutes at the following Board meeting. The Directors may request for further clarification or raise comments on the minutes prior to the confirmation of the minutes as a correct record of proceedings of the Board.

The Board has direct access to the Senior Management and has full and unrestricted access to any information relating to the Group's operations in the discharge of their duties and may require to be provided with further details or clarifications on the Board meeting agenda items.

The Directors have ready and unrestricted access to the advice and services of the Company Secretary.

The Directors are regularly updated by the Company Secretary on the new statutory as well as regulatory requirements relating to Directors' duties and responsibilities or the discharge of their duties as Directors of the Company. The Company Secretary attends all Board meetings and ensures that accurate and adequate records of the proceedings of Board meetings and decisions made are properly kept.

The commitment and dedication of the Board of Directors in ensuring effective discharge of their duties and responsibilities are reflected by the high number of Board meetings held during the financial year ended 31 December 2009.

The Board met eleven (11) times during the financial year ended 31 December 2009. The dates of the Board meetings are as follows:

- 8 January 2009
- 22 January 2009
- 24 February 2009
- 8 April 2009
- 20 April 2009
- 6 July 2009
- 23 July 2009
- 8 October 2009
- 22 October 2009
- 26 November 2009
- 15 December 2009

Attendance by each Member of the Board during the financial year ended 31 December 2009 is as follows:

Director	Number of Board Meetings Attended/ Held	Percentage of Attendance
<b>i. Tan Sri Dato' Sri Dr. Teh Hong Piow</b>	9/11 *	82%
<b>ii. Tan Sri Dato' Thong Yaw Hong</b>	11/11	100%
<b>iii. Tee Choon Yeow</b>	11/11	100%
<b>iv. Tan Kok Guan</b>	11/11	100%
<b>v. Dato' Haji Abdul Aziz bin Omar</b>	11/11	100%
<b>vi. Dato' Yeoh Chin Kee</b>	11/11	100%
<b>vii. Quah Poh Keat</b>	11/11	100%

\* Did not attend 2 out of 11 Board Meetings held during the financial year ended 31 December 2009 as he was on medical leave.

### • Appointments to the Board

The proposed appointment of a new Member to the Board will be deliberated on by the full Board based upon a formal report, prepared by the Nominating Committee on the necessity for and qualification and experience of the proposed director. The Nominating Committee also carried out annual assessment of each Director's contribution to the Company and recommend for the re-appointment and re-election of Directors who are seeking for re-appointment and re-election at the Annual General Meeting. The appointment of Lonpac's Directors to the Board is subject to the prior approval from Bank Negara Malaysia ("BNM") pursuant to Section 70(1) of the Insurance Act, 1996. The Nominating Committee will review and assess the proposed re-appointment of Directors, and thereupon recommend to the Board for approval that an application be submitted to BNM.

The Nominating Committee comprises entirely Independent Non-Executive Directors; all the four (4) Independent Non-Executive Directors are Members of the Nominating Committee.

The terms of reference of the Nominating Committee is set out on page 72.

Upon its recent annual review, the Nominating Committee is satisfied that the size of the Group's Board is optimum and that there is appropriate mix of knowledge, skills, attributes and core competencies in the Board's composition. The Nominating Committee is satisfied that all the Board Members are suitably qualified to hold their positions as Directors of LPI Group in view of their respective academic and professional qualifications, experience and qualities. All the Directors have been assessed as meeting the "fit and proper" criteria established by BNM in the Prudential Framework of Corporate Governance for Insurers.

Upon its recent annual review, the Nominating Committee has also concluded that all the Directors have received training during the financial year ended 31 December 2009 that is relevant and would serve to enhance their effectiveness in the Board and the Audit Committee. The details of the Directors' Training and Education are set out on pages 69 to 70.

### • Re-Appointment and Re-Election of Directors

Pursuant to Section 129(2) of the Companies Act, 1965, Directors who are over the age of seventy (70) years shall retire at every Annual General Meeting and may offer themselves for re-appointment to hold office until the next Annual General Meeting.

In accordance with the Company's Memorandum and Articles of Association, one-third (1/3) of the Directors, or, if their number is not a multiple of three (3), the number nearest to one-third (1/3) with a minimum of one (1), shall retire from office at each Annual General Meeting and they may offer themselves for re-election. Directors who are appointed by the Board during the financial period before the Annual General Meeting are subject to re-election by the shareholders at the first opportunity after their appointments.

## II DIRECTORS' REMUNERATION

The Remuneration Committee reviews annually the performance of the Directors and submits recommendations to the Board on specific adjustments in remuneration and/ or reward payments that reflect their respective contributions for the year, and which are competitive and are consistent with the Group's corporate objectives, culture and strategy. The Remuneration Committee implements a formal and transparent procedure for the full Board to approve remuneration for the Executive Director based on corporate and individual performance. The remuneration of Non-Executive Directors, including Non-Executive Chairman/ Co-Chairman, which is based inter-alia, on the experience, skills and level of responsibilities of the Directors concerned.

Each individual Director abstains from the Board decision on his own remuneration package. Directors' fees are approved at the Annual General Meeting by the shareholders.

The Directors are paid annual fees, and are reimbursed meeting expenses of RM300 each for every Board meeting that they attend.

The Remuneration Committee comprises entirely Independent Non-Executive Directors; all the four (4) Independent Non-Executive Directors are Members of the Remuneration Committee.

The terms of reference of Remuneration Committee is set out on page 72.

Details of the Directors' remuneration (including benefits-in-kind) for each Director during the financial year 2009 are as follows:

	RM'000					
	Salaries	Fees	Bonuses	Other Remuneration	Benefits -in-kind	Total
<b>Executive Director</b>						
Tee Choon Yeow	600	101	450	126	39	1,316
<b>Non-Executive Directors</b>						
Tan Sri Dato' Sri Dr. Teh Hong Piow	-	325	-	-	23	348
Tan Sri Dato' Thong Yaw Hong	-	205	-	24	-	229
Dato' Haji Abdul Aziz bin Omar	-	140	-	24	-	164
Dato' Yeoh Chin Kee	-	140	-	24	-	164
Tan Kok Guan <sup>N1</sup>	426	101	266	83	34	910
Quah Poh Keat	-	140	-	24	-	164
	426	1,051	266	179	57	1,979
<b>Total</b>	<b>1,026</b>	<b>1,152</b>	<b>716</b>	<b>305</b>	<b>96</b>	<b>3,295</b>

N1 - Includes his remuneration as Chief Executive Officer at subsidiary.

### III DIRECTORS' TRAINING AND EDUCATION

The Directors have participated in conferences, seminars and training programmes to keep abreast with the development in the business environment, financial sector issues and challenges as well as with the new regulatory and statutory requirements.

Several Members of the Board are participating in the Financial Institutions Directors Education programme developed by BNM in collaboration with Perbadanan Insurans Deposit Malaysia and the International Centre for Leadership in Finance. The programme is aimed at promoting high impact boards in the financial institutions.

The training programmes and seminars attended by the Directors during the financial year ended 31 December 2009 are, inter-alia, on areas relating to corporate governance, risk management, role of an effective Board, banking, accounting, economics and insurance.

# CORPORATE GOVERNANCE

## STATEMENT (cont'd)

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Conferences, seminars and training programmes attended by the Directors during the financial year ended 31 December 2009 are as follows:

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### Corporate Governance

- Financial Institutions Directors Education ("FIDE") Programme : Talk by Jamie Allen on "The Global Financial Crisis – Implications for Corporate Governance in Asia"
  - FIDE Programme : Talk by Professor Mervyn King on "Governance Trends and Issues"
  - FIDE Programme : New Module Risk Management in Islamic Finance
  - Financial Industry Conference
    - Risk Management Practices in Financial Institutions – "What Went Wrong and Where Do We Go from Here"
    - Strengthening Institutional and Market Resilience – The Supervisory Agenda
    - Approaching Risks in Large and Complex Organisations
  - FIDE Programme : Lunch talk by Mr. David Webb on "Reforming Governance and Adding Value : An Investor's Struggle"
  - Investor Relations Workshop "International Best Practices for IR Communication"
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### Role of An Effective Board

- FIDE Programme : Module 1 – Role of the Board in Changing Financial, Legal, Regulatory and Business Environment
  - FIDE Programme : Module 2 – Practices and Processes that Promote/ Impede Effective Boardroom Deliberations
  - FIDE Programme : Module 3 – The Role of the Board in Enterprise-Wide Risk Management
  - FIDE Programme : Module 4 – The Board's Responsibility for Internal Controls, Financial Reporting and Capital Management
  - FIDE Programme : Module 5 – Building Board Teams, Compensation Issues and Role of the Board in Strategy and Stakeholder Relations
  - FIDE Programme : A Session with Mr. Jim Rogers on "How I See the World Today"
  - High Level Conference 2009
  - FIDE Programme : Talk by Professor James Sebenius on "3D-Negotiation : A Strategic Tool for Board and Senior Executives"
  - High Performance Directors' Conference
  - FIDE "Townhall Session with BNM"
  - FIDE Programme : Focus Group for Nomination Committee/ Remuneration Committee Programme
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### Banking

- In-House Training Programme : Current Development of Islamic Banking and Finance
  - The 13th Malaysian Banking Summit: "Riding Out the Global Financial Crisis – Banking Reforms and Revival"
  - Dialogue with Dato' Razif, Deputy Governor, BNM on "Islamic Banking – The Way Forward"
  - Seminar on "Masterclass for Islamic Bank's Board of Directors"
  - Anti-Money Laundering & Counter Financing of Terrorism (AML/ CFT) Trends & Typologies Seminar
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### Accounting & Economics

- Bank Negara Malaysia Annual Report 2008/ Financial Stability & Payment Systems Report 2008 Briefing
  - Financial Increasing Awareness Workshop
  - Tun Ismail Ali Chair : A Public Lecture on Comparison of the Financial Crises : Japan and Asia in 1997 – 1998 vs US 2008 – 2009
  - Bank Negara Malaysia Public Lecture on Continuing a Legacy in Monetary and Financial Economics
  - Forum on FRS 139 Financial Instruments : Recognition & Measurement entitled "The Challenges of Implementing FRS 139"
  - FRS Seminar by KPMG - FRS 4 on Insurance Contracts; FRS 7 on Financial Instruments Disclosure; FRS 139 on Recognition and measurements & Discussion on new model financial statements - Model Insurance Berhad
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### Insurance

- Services to the International Insurance Industry
  - MRC's Annual Insurance Claims Managers' Dialogue & 2008 Claims Monitor Programme
  - PIAM/GIAS/GIAB Joint Meeting
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## BOARD COMMITTEES

The Board has established several Board Committees whose compositions and terms of reference are in accordance with the best practices prescribed by the MCCG and BNM's Prudential Framework of Corporate Governance for Insurers.

The functions and terms of reference of the Board Committees as well as authority delegated by the Board to these Committees, are clearly defined by the Board.

The Board Committees are as follows:

- Audit Committee
- Nominating Committee
- Remuneration Committee
- Investment Committee
- Risk Management Committee
- Share Buy-Back Committee
- Employees' Share Option Scheme Committee

The composition of the Board Committees and the attendance of Members at Board Committees meetings are reflected as follows:

### Audit Committee

	Attendance at Meetings
Tan Sri Dato' Thong Yaw Hong – Chairman (Independent Non-Executive Director)	9/9
Dato' Haji Abdul Aziz bin Omar – Co-Chairman (Independent Non-Executive Director)	9/9
Dato' Yeoh Chin Kee (Independent Non-Executive Director)	9/9
Quah Poh Keat (Independent Non-Executive Director)	9/9

### Nominating Committee

	Attendance at Meetings
Tan Sri Dato' Thong Yaw Hong – Chairman (Independent Non-Executive Director)	4/4
Dato' Haji Abdul Aziz bin Omar (Independent Non-Executive Director)	4/4
Dato' Yeoh Chin Kee (Independent Non-Executive Director)	4/4
Quah Poh Keat (Independent Non-Executive Director)	4/4

### Remuneration Committee

	Attendance at Meetings
Tan Sri Dato' Thong Yaw Hong – Chairman (Independent Non-Executive Director)	1/1
Dato' Haji Abdul Aziz bin Omar (Independent Non-Executive Director)	1/1
Dato' Yeoh Chin Kee (Independent Non-Executive Director)	1/1
Quah Poh Keat (Independent Non-Executive Director)	1/1

### Investment Committee

	Attendance at Meetings
Tan Sri Dato' Sri Dr. Teh Hong Piow – Chairman (Non-Executive Director)	2/2
Tee Choon Yeow (Executive Director/ Chief Executive Officer)	2/2
Kong Thian Mee (Company Secretary)	2/2

# CORPORATE GOVERNANCE STATEMENT (cont'd)

## Risk Management Committee

	Attendance at Meetings
Tan Sri Dato' Thong Yaw Hong – Chairman (Independent Non-Executive Director)	3/3
Tee Choon Yeow (Executive Director/ Chief Executive Officer)	3/3
Dato' Haji Abdul Aziz bin Omar (Independent Non-Executive Director)	3/3
Dato' Yeoh Chin Kee (Independent Non-Executive Director)	3/3
Quah Poh Keat (Independent Non-Executive Director)	3/3

## Share Buy-Back Committee

	Attendance at Meetings
Tan Sri Dato' Sri Dr. Teh Hong Piow – Chairman (Non-Executive Director)	2/2
Tee Choon Yeow (Executive Director/ Chief Executive Officer)	2/2
Kong Thian Mee (Company Secretary)	2/2

## Employees' Share Option Scheme Committee

	Attendance at Meetings
Tan Sri Dato' Sri Dr. Teh Hong Piow – Chairman (Non-Executive Director)	N1
Tee Choon Yeow (Executive Director/ Chief Executive Officer)	N1
Dato' Yeoh Chin Kee (Independent Non-Executive Director)	N1

N1 – No meeting held as no Employees' Share Option Scheme in 2009.

The terms of reference and frequency of meetings for the Board Committees are as follows:

### i) Audit Committee

- The terms of reference of the Audit Committee are set out under the Audit Committee Report.

The Audit Committee meets not less than four (4) times a year.

### ii) Nominating Committee

- To propose nominees for appointment to the Board.
- To carry out annual assessment of each Director's contribution to the Company.
- To propose the removal of ineffective Directors.

The Nominating Committee meets as and when required.

### iii) Remuneration Committee

- To review and deliberate on the quantum of Directors' annual fees.

The Remuneration Committee meets as and when required.

### iv) Investment Committee

- To formulate policies, strategies and other matters relating to investment in shares and private debt securities.
- To review the Company's investment on shares and private debt securities and take necessary measures to improve its value, profitability and risk.

The Investment Committee meets as and when required.

### v) Risk Management Committee

- To review and recommend risk management strategies, policies and risk tolerance for the Board's approval.
- To review and assess the adequacy of risk management policies and framework for identifying, measuring, monitoring and controlling risks as well as the extent to which these risks are operating effectively.
- To ensure adequate infrastructure, resources and systems are in place for an effective risk management i.e. ensuring that the staff responsible for implementing risk management systems perform those duties independently of the Group's risk taking activities.

- To review the management's periodic reports on risk exposure, risk portfolio composition and risk management activities.
- To perform any other functions in relation to the risk management as may be agreed by the Risk Management Committee and the Board.

The Risk Management Committee meets every half yearly.

#### vi) Share Buy-Back Committee

- To ensure that the Share Buy-Back complies with the mandate given to the Share Buy-Back Committee by the Board to determine the purchase date, amount and price of LPI ordinary shares to be bought back.
- To ensure that the LPI ordinary shares bought back are retained as Treasury Shares unless otherwise determined by the Board.
- To ensure that LPI remains solvent after each Share Buy-Back in accordance with Section 67A of the Companies Act 1965, Part IIIA of the Companies Regulations 1966, and the Listing Requirements of Bursa Securities ("Solvency Declaration").
- To formulate plans and strategies to ensure that LPI's purchase of its own ordinary shares is carried out in the most efficient manner.

The Share Buy-Back Committee meets as and when required.

#### vii) Employees' Share Option Scheme ("ESOS") Committee

- To administer the ESOS in accordance with the ESOS Bye-laws.

The ESOS Committee meets as and when required.

### MANAGEMENT COMMITTEES

The Board has also established various Management Committees whose functions and terms of reference as well as authority are clearly defined and are set up to assist the Board in the running of the Group.

The Management Committees are as follows:

- Working Risk Management Committee
- Credit Control Committee

- Information Technology ("IT") Steering Committee
- Systems and Methods Committee
- Business Resumption Continuity Plan ("BRCP") Committee
- Corporate Social Responsibility ("CSR") Committee
- Occupational Safety and Health Committee

The terms of reference and frequency of meetings for the Management Committees are as follows:

#### i) Working Risk Management Committee

- To assist the Risk Management Committee ("RMC") on the management of operational, financial and general risks to achieve business objectives.
- To identify and communicate to the RMC on critical risks (present and potential) in terms of likelihood exposures and impact on the business and the management action plans to manage these risks on a continuing basis.
- To oversee the formal development of operational, financial and general risks management policies encompassing all business and activities and ensuring the development of procedures and manuals.
- To evaluate and assess the adequacy of controls to manage the overall operational, financial and general risks associated with the business activities inclusive of physical/ premises security.
- To review reports on significant fraudulent cases and lapses in operational, financial and general risks management processes.
- To ensure that there is adequate and prompt risk reporting in respect of operational, financial and general risks management.
- Monitor, assess and advise the credit risk portfolio composition.
- Review reports of the credit review process, assets quality and ensure that corrective actions are taken.
- Ensure compliance with regulatory requirements.
- To keep abreast with the latest developments, both domestic as well as international in the insurance industry and financial markets.

- To evaluate the adequacy of the capital available in the insurance and shareholders' equity to support the Total Capital Required as specified in the Risk-Based Capital Framework for Insurers issued by BNM.
- To develop an outsourcing risk management programme and policies for RMC's approval.
- To evaluate the materiality of all existing and prospective outsourcing, based on the framework approved by the Board.
- Implement approved outsourcing policies and procedures.
- Periodically review the outsourcing policies and procedures implemented to ensure their continued effectiveness in managing outsourcing risks.
- To communicate information pertaining to material outsourcing risks to the RMC in a timely manner.
- To oversee the Working Risk Management Committee – Singapore Branch.
- To perform any other functions in relation to the risk management as may be agreed by the RMC and the Board.

The Working Risk Management Committee meets quarterly.

### ii) Credit Control Committee

- To maximise the conversion of accounts receivable into cash flow and minimise bad debts written off whenever possible.
- To ensure timely collection of outstanding debts, identify problems (e.g. short payment, cancellation, unidentified items) and resolve it in a timely manner.

The Credit Control Committee meets monthly.

### iii) Information Technology ("IT") Steering Committee

- Ensure the establishment of effective computerisation plans for the Group in line with the overall corporate strategic plan and business objectives.
- Overall control of the implementation of the plans by monitoring and reviewing its performance and progress.
- Setting budgets within which computerisation objectives should be achieved and authorising any expenditure above pre-defined limits.

- To establish objectives, policies and strategies for computerisation in the Group.
- To develop long-term strategic plans for computerisation of the Group.
- To establish a detailed annual IT Plan.
- To establish standards for:
  - Hardware/ Software Acquisition;
  - Systems Development Lifecycle and Programme Change Operations; and
  - Computer Security.
- To consider software, hardware acquisitions and all items related to computerisation.
- To monitor and review progress of ongoing projects and the performance monitoring will be geared to the strategic plans, action plans and budgets.
- To review and approve new IT Project proposals.

The IT Steering Committee holds a minimum of six (6) meetings a year.

### iv) Systems and Methods Committee

- To provide online insurance services and an alternative communications channel to the agents, policyholders and prospective customers in a secured and user-friendly environment.
- To review and provide recommendations for streamlining of workflow and improving efficiency and increasing E-Enablement of processes and procedures that involves E-System enhancement resulting in reduced costs and improved efficiency.

The Systems and Methods Committee meets once in every 2 month.

### v) Business Resumption Continuity Plan ("BRCP") Committee

- To prepare a Business Resumption Continuity Plan to ensure that the Group suffers minimum interruption to its systems, processes or operations in the event of any disasters.

The BRCP Committee meets as and when required.

**vi) Corporate Social Responsibility (“CSR”) Committee**

- To carry out CSR activities in line with the CSR Vision.

The CSR Committee meets at least twice a year.

**vii) Occupational Safety and Health (“OSH”) Committee**

- To review the measures taken to ensure the safety and health of persons at the place of work.
- To investigate any matter at the place of work:
  - which a member of the OSH Committee or a person employed thereat considers is not safe or is a risk to health; and
  - which has been brought to the attention of the employer.
- Attempt to resolve any matter referred to in the above investigation, and if unable to do so, requests the management to undertake an inspection of the place of work for that purpose.

The OSH Committee meets quarterly.

## ACCOUNTABILITY AND AUDIT

### Financial Reporting

The Board recognises the responsibility for ensuring that accounting records are properly kept and that the financial statements are prepared in accordance with applicable approved accounting standards in Malaysia and the provisions of the Companies Act, 1965, the Insurance Act and Regulations 1996 and the directives from Bank Negara Malaysia.

Early announcements on the quarterly results and issuance of annual report to Bursa Securities reflect the Board’s commitment to provide timely, transparent and up-to-date assessments on the Group’s performance and prospects.

The Board assisted by the Audit Committee, oversees the financial reporting processes and the quality of the financial reporting by the LPI Group. The Audit Committee reviews and monitors the accuracy and integrity of the Group’s annual and quarterly financial statements. The Audit Committee also assists the Board in reviewing the appropriateness of the accounting policies applied by the Group as well as the changes to these policies.

The Statement of Responsibility by Directors in respect of the preparation of the annual audited financial statements of LPI and LPI Group is presented on page 165.

### Related Party Transactions

The Internal Audit Department reviewed the nature of related party transactions within the Group to ascertain any conflict of interest situations that would raise questions of management integrity. The results of this annual review is tabled at the Audit Committee’s meeting and thereafter reported to the Board.

Details of the related party transactions are disclosed in the Notes to the Financial Statements on pages 221 to 223 of this Annual Report.

### Internal Controls

The Board has overall responsibility for maintaining a system of internal controls that provide reasonable assurance for effective and efficient operations, compliance with laws and regulations, as well as adherence with internal procedures and guidelines.

The Group has established internal controls, which cover all levels of personnel, and business processes that ensure the Group’s operations are effective and efficient as well as the safeguarding of the Group’s assets and shareholders’ interest.

The size and complexity of the business operations involve the acceptance and management of operational risks, financial risks and general risks. The nature of these risks may give rise to the unanticipated or unavoidable losses. LPI Group’s systems of internal controls are designed to provide reasonable and not absolute assurance against the risk of material errors, frauds or losses occurring.

During the year, the Risk Management Committee ensures that the accountability for managing the significant risks identified is clearly assigned and that identified risks are being addressed on an ongoing basis.

The effectiveness of the system of internal controls of the Group is reviewed periodically by the Audit Committee. The review covers the financial operational and compliance controls as well as risk management functions. The Internal Audit Department monitors compliance with policies

and standards and the effectiveness of internal control structures across the LPI Group.

The Statement on Internal Control furnished on pages 97 to 100 of this Annual Report provides an overview of the state of internal controls within the Group.

### **Audit Committee**

The Group's financial reporting and internal control system is overseen by the Audit Committee, which comprises all the four (4) Independent Non-Executive Directors.

The composition, terms of reference and summary of the activities of the Audit Committee during the financial year are disclosed in the Audit Committee Report on pages 101 to 104 of this Annual Report. The activities of the Audit Committee are governed by a charter that is approved by the Board.

The Audit Committee meets quarterly. Additional meetings are held as and when required. During the financial year ended 31 December 2009, a total of nine (9) Audit Committee meetings were held.

The Audit Committee meeting is always held before the Board's meeting. This is to ensure that all critical issues highlighted can be brought to the attention of the Board on a timely basis. The minutes of the Audit Committee meetings are tabled to the Board for noting and for action by the Board where appropriate.

The Heads of Departments in Head Office are invited to attend the Audit Committee meetings when deemed necessary by the Audit Committee for the purpose of briefing the Audit Committee on the activities involving their areas of responsibilities.

### **Whistleblowing Policy**

The Board is committed to maintaining the highest possible standards of ethical and legal conduct within the Group. In line with this commitment and in order to enhance good governance and transparency a Whistleblowing Policy was adopted with the aim to provide an avenue for raising concerns related to possible improprieties in matters of financial reporting, compliance and other malpractices at the earliest opportunity, in an appropriate manner and without fear of retaliation.

The policy addresses the following areas:

- Policy statement
- Coverage statement
- Scope of policy
- Safeguards
- Disclosure procedures

The policy provides a transparent and confidential avenue for employees to raise issues that include:

- Financial malpractice or impropriety or fraud;
- Failure to comply with legal and regulatory obligations;
- Endangerment of individual health and safety or the environment;
- Criminal offences;
- Miscarriage of justice;
- Improper conduct or unethical behaviour; and
- Concealment of any or a combination of the above.

Confidentiality and anonymity is offered to employees who disclose their concerns in good faith and in doing so, had followed the appropriate disclosure procedures accordingly.

In view of the seriousness of an allegation can be, the policy sets a clear procedural guide for employees to follow in raising their concerns. This will ensure that issues could be addressed to the appropriate person and proper course of actions could be taken. Concerns that are expressed anonymously although less credible, will not be disregarded and will be acted on accordingly.

The policy also provides the contact details of the Audit Committee Chairman being the Senior Independent Director and the Group Company Secretary, should employees are in doubt of the Management's independence and objectivity on the concerns raised.

Each allegation will be dealt with fairly and equitably. Actions will be taken based on the nature of the allegation and may be resolved by agreed action. The Audit Committee Chairman or the Group Company Secretary may initiate the formation of an Investigation Committee consisting of persons from the Senior Management who are independent of the allegation, where deemed necessary.

The establishment of the Whistleblowing Policy within the Group is a clear signal to the public, stakeholders and regulators about the attitude i.e. “tone at the top” of the Board and Management towards fraud and illegal acts.

### Relationship with External Auditors

The Audit Committee meets with the Group’s external auditors at least twice a year to review the scope and adequacy of the audit process, the annual financial statements and their audit findings. The Audit Committee also meets additionally with the external auditors whenever it deems necessary.

The service provided by the external auditors include statutory audits and non-audit services. The terms of engagement for the services rendered by the external auditors are reviewed by the Audit Committee and approved by the Board. The Audit Committee also reviews the proposed fees for non-audit services and subsequently recommends to the Board for approval. In their review, the Audit Committee ensures that the independence and objectivity of the external auditors are not compromised.

The details of the statutory audit, audit-related and non-audit fees paid/ payable in 2009 to the external auditors are set out below:

RM'000	Group Total
<b>Fees paid/ payable to KPMG and its affiliates</b>	
• Audit	487
• Audit Related Service	
- Review of Statement on Internal Control	6
- Others	20
• Non-Audit Service*	51
<b>Total</b>	<b>564</b>

\* The non-audit service fees paid/ payable to the external auditors were for advice on taxation matters and for preparation, review and submission of tax returns. The provision of these services by the external auditors to the LPI Group were cost effective and efficient due to their knowledge and understanding of the operations of the Group, and did not compromise their independence and objectivity.

### Internal Audit

The Group has an established Internal Audit Department, which assists the Audit Committee in the discharge of its duties and responsibilities. Its role is to provide independent and objective reports on the organisation’s management, records, accounting policies and controls to the Board. The internal audits include evaluation of the processes by which significant risks are identified, assessed and managed. Such audits also ensure instituted controls are appropriate, effectively applied and achieve acceptable risk exposures consistent with the Group’s risk management policy.

The internal audit function is conducted in a manner that is consistent with and met the Standards for the Professional Practice of Internal Auditing and Code of Ethics of the Institute of Internal Auditors Malaysia.

The Head of Internal Audit reports directly to the Audit Committee and its findings and recommendations are communicated to the Board.

A Statement on Internal Audit Function is presented on page 107 of this Annual Report.

### EFFECTIVE COMMUNICATIONS WITH SHAREHOLDERS

Transparency and accountability to all stakeholders are the key elements of good corporate governance. The fundamental objectives of transparency and accountability are the communication of clear, relevant and comprehensive information that is timely and readily accessible by all stakeholders. In fulfilling its corporate governance obligations, the LPI Group maintains a high level of disclosure and extensive communication with its stakeholders by providing clear, comprehensive and timely information through a number of readily accessible channels. The provision of timely information is principally important to the shareholders and investors for informed investment decision making particularly in periods of financial turbulence and extreme volatility in the market place.

## CORPORATE GOVERNANCE STATEMENT (cont'd)

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LPI's Annual Report remains a key channel of communication with the Group's stakeholders. The contents of the annual report of LPI met the Bursa Securities Listing Requirements and other regulatory requirements of annual reports. The extensive information contents and disclosure requirements governing listed companies' quarterly Bursa Securities results announcements had also enhanced the transparency level of LPI Group generally.

The Group also provides an executive summary of its annual report, highlighting key financial and corporate information as well as the analysis of the balance sheet and income statement, in order to facilitate shareholders' easy access to such key information.

An important avenue for communication and dialogue with the shareholders is the Company's Annual General Meeting ("AGM"). All shareholders are encouraged to attend the Company's AGM and to participate in the proceedings. Shareholders are given both the opportunity and time to raise questions and seek clarification on the agenda items and on the performance of the Company and Group. The Chairman/ Co-Chairman and Chief Executive Officer are responsible for providing clarifications on issues raised by the shareholders at the Company's general meetings and they avail themselves to clarify matters or enquiries from shareholders. Shareholders' suggestions received during AGMs are reviewed and considered for implementation, wherever possible.

At the AGM, the Chairman of LPI presents a comprehensive review of the financial performance of the LPI Group and value created for shareholders. This review is supported by visual and graphical presentation of key points and financial figures. Printed copies of the financial performance review of the Group are also made available to the shareholders upon their request and to the media. The turnout of shareholders at LPI's AGM has always been good, a clear indication of the extensive engagement of shareholders. A total of 328 and 376 shareholders (and proxy holders) attended the AGMs held in 2008 and 2009 respectively.

LPI releases media statement of its quarterly and annual results announcements. The media statement is intended not only to promote the dissemination of the financial results of the LPI Group to a wide audience of investors and shareholders but also to keep the investing public and shareholders updated on the Group's business progress and development. In addition, the Group also provides press releases to the media on all significant corporate developments and business initiatives.

In order to maintain high level of transparency and to promote wider dissemination of corporate and financial disclosures, all information that is made public, such as LPI's Annual Report, the quarterly financial result announcement of the LPI Group and other corporate information are available on the Group's website, [www.lonpac.com](http://www.lonpac.com).

Prompt and timeliness in dissemination of information is important for shareholders and investors to make informed investment decisions. Outdated information although accurate and comprehensive, is less useful for such investment purposes. In this view, LPI Group places high priority to making available and disseminating information as early as possible. The release of periodic financial information such as LPI's Annual Report and the Group's quarterly financial results are generally earliest amongst large listed companies and are always well ahead of the deadlines specified in the Bursa Securities Listing Requirements, as reflected in the following tables:

### Release of Annual Report

	Date of Issue	No. of Days After End of Year	Deadline Imposed by Bursa Securities
Annual Report 2005	18 January 2006	18	30 June 2006
Annual Report 2006	10 January 2007	10	30 June 2007
Annual Report 2007	23 January 2008	23	30 June 2008
Annual Report 2008	21 January 2009	21	30 June 2009
Annual Report 2009	20 January 2010	20	30 June 2010

### Release of 2009 Quarterly Results

	Date of Issue	No. of Days After End of Quarter	Deadline Imposed by Bursa Securities
1st Quarter	8 April 2009	8	31 May 2009
2nd Quarter	6 July 2009	6	31 August 2009
3rd Quarter	8 October 2009	8	30 November 2009
4th Quarter	7 January 2010	7	28 February 2010

The Group consistently managed to achieve such early issuance of its annual reports and releases of the quarterly financial results despite of the regulatory requirements, which need to be complied with, including a significantly higher level of disclosure of financial information. The prompt and timely availability of information clearly enhances the value of such information to the shareholders and investors and reflects the high standard of transparency within the Group.

### INVESTOR RELATIONS

The LPI Group's investor relations activities serve as an important communication channel with the shareholders, investors and the investment community, both in Malaysia and internationally.

The Group's investor relations function are undertaken by the very senior level of Management personnel, reflecting the commitment of the Group to maintain strong investor relations as well as providing appropriate and substantive views and information on the Group to investors and equity research analysts.

### Investor Relations Activities in 2009

	Total
Meeting with analysts/ fund managers	16
Meeting with media/ media conference	11
Briefing by Minority Shareholder Watchdog Group	1

## CORPORATE GOVERNANCE STATEMENT (cont'd)

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Investor Relations activities such as meetings with fund managers and analysts, interviews by the media and press conference are attended by the following Directors to explain the Group's strategy, performance and major developments:

### Primary Contacts for Investor Relations Matters

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#### **Tee Choon Yeow**

Executive Director/  
Chief Executive Officer

#### Contact Details

Telephone number : (03) 2262 8688  
Email : cytee@lonpac.com

Mr. Tee was appointed to the Board of the Company on 29 October 1991. He is the Chief Executive Officer and Executive Director of LPI.

Mr. Tee holds a Bachelor's Degree in Commerce from the University of Canterbury, New Zealand. He is a Chartered Accountant of the Institute of Chartered Accountants, New Zealand and the Malaysian Institute of Accountants and a Fellow of Certified Practising Accountants of Australia.

He is also the Advisor of Lonpac Insurance Bhd, a wholly-owned subsidiary of LPI.

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#### **Tan Kok Guan**

Non-Executive Director

#### Contact Details

Telephone number: (03) 2262 8633  
Email : kgtan@lonpac.com

Mr. Tan was appointed to the Board of the Company on 29 October 1996. He is the Non-Executive Director of LPI.

Mr. Tan holds a Bachelor's Degree in Science (Hons.) from the University of London, United Kingdom and a Master of Business Administration from the University of Hawaii. He is also a Chartered Insurer and Associate Member of the Chartered Insurance Institute at London and an Associate of the Malaysian Insurance Institute at Kuala Lumpur.

He is also the Chief Executive Officer of Lonpac Insurance Bhd, a wholly-owned subsidiary of LPI.

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The efforts and resources allocated to the investor relations function reflect LPI Group's commitment to achieve a high standard of communication with, and a high level of transparency to its shareholders and the investment community.

Information on the Group's investor relations matters and the primary contacts are also available for the shareholders' and other stakeholders' view in our website at [www.lonpac.com](http://www.lonpac.com).

This Corporate Governance Statement is made in accordance with the resolution of the Board of Directors dated 7 January 2010.

### **Tan Sri Dato' Sri Dr. Teh Hong Piow**

Chairman

# RISK MANAGEMENT

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## OVERVIEW

The importance of risk management has been growing steadily over the years. In the financial services industry, risk management has become one of the critical factors in determining the success of an organisation especially when the industry is closely related to conditions of uncertainty. Risk management is a discipline designed to identify potential events that may affect an organisation in order to protect and minimise the risks. An effective risk management ensures the continuity of an organisation's operations.

Risk management is basically not simply about preparing for the worst but it is about realising the full potential. With a clear understanding of the risks that we encounter, we could maximise our performance and drive forward our competitive advantage. Risk management could also be geared to achieving an organisation's objectives through strategic decisions that flow through high-level goals, effective use of resources, reliability of reporting, and compliance with applicable laws and regulations.

Being in the financial services industry, LPI Capital Bhd ("LPI") Group is primarily in the risk business and is operating in a rapidly-changing business environment with diversified risks. The Board recognises the importance of effective risk management to achieve sustainable growth in profitability, strong asset quality and to continually optimise shareholders' value.

The Board, with the assistance of the management, implemented the risk management processes within the Group that set out the overall business strategies and the general risk management philosophy. The major areas of risk that the activities of the Group are exposed to are operational risks, financial risks and general risks. All identified risks are comprehensively dealt with and managed by established controls and monitoring measures supported by prudent risk management culture.

Effective risk management ensures that a good understanding of risk is backed up by the right appetite, capacity, and controls. The controls are constantly monitored and reviewed in line with the risk appetite and strategies of the Group, taking into account of changes in business market conditions, products and risk management best practices. Continuous efforts are undertaken to instil a culture of risk par excellence across all levels of staff through effective communication, training, clear policies, procedures and organisational structure, as well as clearly defined roles and responsibilities. The commitment in managing the risks within a rigorous risk management framework has built a solid foundation for delivery of effective risk management within the Group.

**OVERALL RISK MANAGEMENT FRAMEWORK**

The risk management infrastructure of LPI Group sets out clear accountability and responsibility for the risk management process which underlines the principal risk management and control responsibilities:



The risk management framework for LPI Group was established with emphasis on the insurance operations as the core business of the Group by its subsidiary company, namely Lonpac Insurance Bhd ("Lonpac").

The Board acknowledges their ultimate responsibilities for the management of risks within the Group. A Risk Management Committee ("RMC") was established by the Board with the responsibility to oversee the overall risks which includes inter-alia reviewing and approving risk management manual, reviewing risk exposure and portfolio composition, and ensuring that infrastructure, resources and systems are put in place for risk management activities. The RMC is supported by the Working Risk Management Committee ("WRMC") of Lonpac.

The WRMC, headed by the Chief Executive Officer was established with the responsibility to identify and communicate to the RMC on critical risks (present and potential) in terms of likelihood exposures and impact on the Group's business and the management action plans to manage these risks on a continuing basis.

A Working Risk Management Committee - Singapore Branch ("WRMCS") was also established with the responsibility to identify and communicate to the WRMC on critical risks (present and potential) in terms of likelihood exposures and impact on the business of Lonpac's Singapore branch and the management action plans to manage these risks on a continuing basis. The WRMCS reports to the WRMC at Head Office.

The independent risk management and control functions under the Internal Audit Department provides crucial support to the dedicated committees, WRMC and WRMCS are responsible for ensuring the risk policies are implemented and complied with.

The Business Units are responsible for identifying, mitigating and managing risks within their lines of business and ensure that their day to day business activities are carried out in accordance with the established risk policies, procedures and limits.

The role of the Audit Committee supported by the Internal Audit Department is to provide an independent assessment of the adequacy and reliability of the risk management processes and system of internal controls and compliance with risk policies, laws, internal and regulatory guidelines.

The risk management policies are subject to frequent reviews to ensure that they remain applicable and effective in managing the associated risks due to changes in the market and regulatory environments.

# RISK MANAGEMENT (cont'd)

## RISK MANAGEMENT PROCESS

The Group has established a structured approach within its risk management framework that comprises eight (8) phases that are categorised into four (4) distinct stages as listed below:

A Formal Approach			
<b>STAGE A</b>	<b>PHASE 1</b>	Planning and Control	<b>PHASE 2</b> Identify Core Business Process and Supporting Mission - Critical System
<b>STAGE B</b>	<b>PHASE 3</b>	Identify Risk	<b>PHASE 4</b> Perform Risk and Impact Assessment
<b>STAGE C</b>	<b>PHASE 5</b>	Develop the Control and Monitoring Measures	<b>PHASE 6</b> Document Risk Management Manual
<b>STAGE D</b>	<b>PHASE 7</b>	Develop and Initiate Training Programme	<b>PHASE 8</b> Maintenance of the Risk Management Manual

The key risk management processes for each phase are as follows:

### STAGE A

#### Phase 1 - Planning and Control

- Established WRMC and WRMCS which comprise representatives from various departments i.e. Underwriting, Claims, Business Development, Accounts & Finance, Information Technology, Human Resource, Compliance and Internal Audit.
- Define the Terms of Reference for the WRMC and WRMCS.
- Define roles and responsibilities for each WRMC and WRMCS members.
- The Group's risks are grouped into Operational, Financial and General perspectives and also focusing the planning effort on risks relating to critical core business processes.

#### Phase 2 - Identification of Core Business Process and Supporting Mission-Critical System

- Identified underwriting operations as the core business for the Group whilst the support mission-critical systems are Claims, Business Development, Accounts & Finance, Information Technology and Human Resource operations.

### STAGE B

#### Phase 3 - Identification of Risks

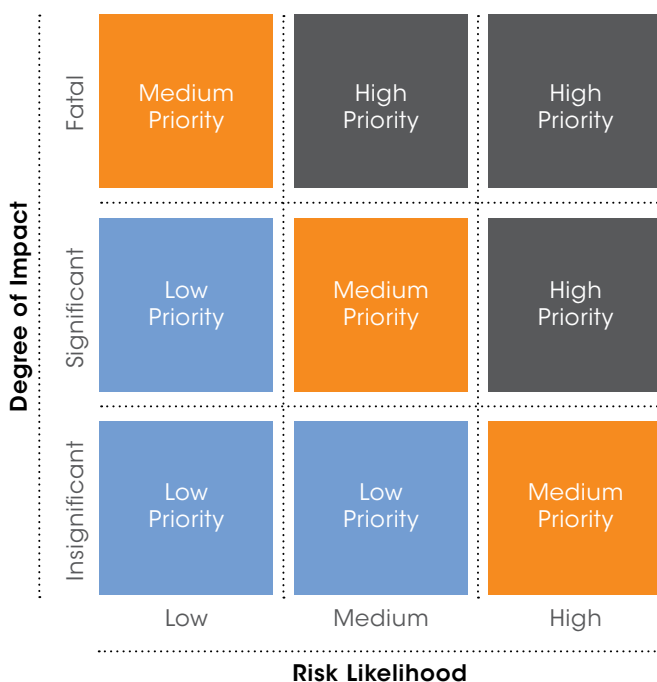
- Analyse possible threats (both internal and external) to the Group's business as a result of the occurrence of operational, financial and general risks.

**Phase 4 – Performing Risk and Impact Assessment**

- Assess each risk identified in Phase 3 to establish the degree of impact and risk likelihood of the particular risk into the following category:

Degree of Impact	Likelihood of Risk Degree
Fatal	High
Significant	Medium
Insignificant	Low

- Risk Mapping is used to determine the best way to focus resources in order to maximise the return and minimise risk through risk management as depicted below:



- High Priority = Major Focus
- Medium Priority = Peripheral Focus
- Low Priority = Minor Focus

- The objective of categorising the degree of impact as well as risk likelihood is to prioritise the protection of those components of the Group’s core business which would be most severely impacted by the identified risks.

**STAGE C**

**Phase 5 – Developing the Control and Monitoring Measures**

- Develop control and monitoring measures for each area of risk identified to counter the impact of the risks.

**Phase 6 – Documenting Risk Management Manual**

- Control and monitoring measures resulting from the analysis in Phases 3, 4 and 5 were translated into standard controls and operating procedures in the Risk Management Manual.

**STAGE D**

**Phase 7 – Developing and Initiating Training Programme**

- Develop and initiate training programme to address the following:
  - The Risk Management Structure and Terms of Reference
  - Specific Responsibilities of Various Teams
  - Risk and Impact Assessment
  - Control and Monitoring Measures

**Phase 8 – Maintenance of the Risk Management Manual**

- Review and update Risk Management Manual for ongoing changes in the risk profile.
- A yearly review on the Risk Management Manual will be conducted to ensure the completion of the risk profile and risk management.

AREAS OF RISK

The major areas of risk that the activities of the Group are exposed to are as follows:

### Support Divisions

- Underwriting
- Reinsurance
- Claims
- Accounts & Finance
- Human Resource
- Information Technology
- Customer Service
- Compliance

### Business Development Divisions

- Agency
- Financial Institution
- Broking
- NIPPONKOA
- Branches

### Operational Risks

Risks of operational disruption caused by failure of systems and facilities

- Business Development Risks
- Underwriting Risks
- Claims Risks
- Information Technology ("IT") Risks
- Internet Risks

### Financial Risks

Risks of financial disruption caused by credit risk, liquidity risk, investment risk and also volatility in interest rates and foreign currency as well as capital inadequacy

- Credit Risk
- Liquidity Risk
- Investment Risk
- Interest Rate Risk
- Foreign Currency Risk
- Capital Adequacy Ratio Risk

### General Risks

Risks related to human resources, physical operational and reputational risks

- Personnel Risk
- Physical Operational Risk
- Reputational Risk

## OPERATIONAL RISKS

### Business Development Risks

Business Development risks relate to *Social Risks* which affect the Group's image and reputation arising from lack of care, poor product knowledge and poor standard of services of personnel that undermine the public's trust and confidence in the organisation; *Economic Risks* which are influenced by loss of market share due to competition, de-tariff of Fire and

Motor insurances arising from market liberalisation, changes in reinsurance market due to mergers and acquisitions, and reinsurance support and facilities; and *Compliance Risk* where online business transactions and advertisement did not meet the requirements by the regulatory authorities.

## BUSINESS DEVELOPMENT RISK MANAGEMENT

### A. RISK IDENTIFICATION

Risks are identified by the Business Development staff based on their industry and technical knowledge. Identified risks are deliberated at Working Risk Management Committee meeting and addressed in the Risk Management Manual.

### B. RISK & IMPACT ASSESSMENT

An assessment is made to establish the degree of impact of the particular risk and the degree of impact is categorised into one of the following three levels:-

Fatal

Significant

Insignificant

An assessment will also be performed to determine the degree of risk likelihood of the particular risk which is categorised into one of the following three levels:-

High

Medium

Low

### D. RISK MONITORING

- Regular meetings to monitor and review complaints against staff, agents and brokers
- Regular meetings to monitor new developments in the international arenas on trade and services liberalisation and mergers and acquisitions of major reinsurers
- Business Development performs checking on online transaction and advertisement

### C. RISK CONTROL

- Provide regular comprehensive products and marketing/ customers services trainings to staff and agents to improve products knowledge and standard of service to clients
- Review of business portfolio and strategically plan to prepare for the liberalisation of the insurance industry by developing new niche products and services
- Communicate with agents on the specific online transactions or advertisement that require approval from the regulatory authorities

# RISK MANAGEMENT (cont'd)

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## Underwriting Risks

Underwriting risks relate to the following:

- accepting or holding covered risks declined in treaties or unacceptable to the Company or risks exceeding its retention or risks with backdated periods of insurance
- dealings with reinsurers with poor financial standing and poor reputation for claims settlement
- improper allocation and control of cover note books
- poorly drafted treaty contracts
- improper selection and appointment of reinsurance brokers
- improper facultative reinsurance placements

Underwriting risks also include processing risks, physical loss or damage risks, moral risks, human resource risks, breach of regulatory guidelines risks, new product development risks and money laundering and terrorist financing risks.

Processing risks arise as a result of disruption or failure of IT operational systems caused by system breakdown, lack or absence of system support and power failure; malicious damage to software and hardware; filing errors resulting in misplaced or lost documents; and erroneous data entries resulting in inaccurate documentation, duplication of documents and double entries.

Physical loss or damage risks relate to damages to documents, office equipments and office premises (including branch offices) resulting from perils such as fire, flood, explosion, collapse of building, denial of access, malicious damage, theft and impact damage.

Moral risks arise from fraud resulting in false data, unauthorised signatories in policies and cover notes and breach of confidentiality resulting in information given to competitors.

Human resource risks refer to termination, resignation and prolonged illness of key employees, integrity of employees in disclosure of confidential information to competitors and staff competency level.

Breach of regulatory guidelines risks relate to breaches of guidelines issued by regulatory bodies such as Bank Negara Malaysia ("BNM"), Persatuan Insurans Am Malaysia ("PIAM"), Monetary Authority of Singapore ("MAS") and General Insurance Association of Singapore ("GIAS") which may result in fines imposed to the organisation.

New product development risks arise from ignorance or incompetency of staff and inadequate market research upon launching of new products which may result in deterioration of claims ratio, affect the reputation of the Group and expose the risks of non-compliance with related regulations.

Money laundering and terrorist financing risks refer to the Group being used as a platform by the criminals and terrorists for their money laundering and terrorist financing activities.

## UNDERWRITING RISK MANAGEMENT

### A. RISK IDENTIFICATION

Risks are identified by the Underwriters based on their industry and technical knowledge. Identified risks are deliberated at Working Risk Management Committee meeting and addressed in the Risk Management Manual.

### B. RISK & IMPACT ASSESSMENT

An assessment is made to establish the degree of impact of the particular risk and the degree of impact is categorised into one of the following three levels:-

Fatal

Significant

Insignificant

An assessment will also be performed to determine the degree of risk likelihood of the particular risk which is categorised into one of the following three levels:-

High

Medium

Low

### D. RISK MONITORING

- Regular Internal Audit conducted and random checks by Department Heads on policies issued
- Procedures are carried out as per IT Manual
- Annual review of Business Resumption Continuity Plan ("BRCP") Manual by BRCP Committee
- Access to office is monitored by CCTV and Access Card
- Regular underwriting meetings are conducted with feedback from Department Heads on manpower and quality of staff
- Regular reviews are conducted by Compliance Officer to oversee the compliance issues
- Quarterly reporting of AML/ CFT initiatives to the Working Risk Management Committee

### C. RISK CONTROL

- Policies are issued within designated Authority Limits and in compliance with the Underwriting Manual
- Daily and weekly back-ups to minimise lost data. Default systems are implemented to prevent manual overrides
- Building is secured by CCTV cameras and sprinklers
- Personnel are given restricted access rights depend on the nature of their work and their level of authorisation
- Staff undergo series of trainings while agents are carefully selected to maintain level of competency
- Circulars/ Guidelines issued by regulators are immediately brought to attention of relevant personnels
- Conduct a comprehensive market research on the proposed new product
- Procedures on verification, maintenance/ retention of records and reporting suspicious transactions are set out in the Anti Money Laundering/ Counter Financing of Terrorism ("AML/ CFT") Manual

# RISK MANAGEMENT (cont'd)

## Claims Risks

Claims risks include delay of claims settlement; fraudulent claims; inaccuracy and inadequacy of claims reserves provision; lack of reinsurance support; premium does not commensurate with the risk; policies not renewed

when a claim materialises, increase in motor theft claims, non-compliance with Risk-Based Capital Framework and wrongful disclosure of material claims information.

## CLAIMS RISK MANAGEMENT

### A. RISK IDENTIFICATION

Risks are identified by the Claims staff based on their industry and technical knowledge. Identified risks are deliberated at Working Risk Management Committee meeting and addressed in the Risk Management Manual.

### B. RISK & IMPACT ASSESSMENT

An assessment is made to establish the degree of impact of the particular risk and the degree of impact is categorised into one of the following three levels:-

Fatal

Significant

Insignificant

An assessment will also be performed to determine the degree of risk likelihood of the particular risk which are categorised into one of the following three levels:-

High

Medium

Low

### D. RISK MONITORING

- Claims procedures and staff performance are reviewed regularly
- Spooling of statistics on claims experience
- Outstanding file reserves are reviewed on a quarterly basis
- Claims developments in the local and international insurance market are constantly reviewed
- Apply strict underwriting policy on vehicle models with high theft frequencies
- Close review and monitoring of claims management
- Implement password and access control

### C. RISK CONTROL

- Simplified procedures are in place and on-the-job training is provided
- In-depth investigation of suspicious claims
- IT system safeguards against inadequate provision during payment
- Liaison with the respective servicing staff upon discovery of inaccuracy
- Encourage motor policyholders to install anti-theft devices
- Emphasis accuracy, efficiency and competency on claims management
- Restricted access to certain categories of data

## IT Risks

IT risks include disruption to the operations of the Group, which arises from system breakdown, lack or absence of system support and security, legal or regulatory problems due to non-conformance or violation of laws, and adverse

business decision or improper implementation of decisions that affect capital outlay and incapable of meeting the organisation's needs.

# INFORMATION TECHNOLOGY RISK MANAGEMENT

## A. RISK IDENTIFICATION

Risks are identified by the IT staff based on their industry and technical knowledge. Identified risks are deliberated at Working Risk Management Committee meeting and addressed in the Risk Management Manual.

## B. RISK & IMPACT ASSESSMENT

An assessment is made to establish the degree of impact of the particular risk and the degree of impact is categorised into one of the following three levels:-

Fatal

Significant

Insignificant

An assessment will also be performed to determine the degree of risk likelihood of the particular risk which are categorised into one of the following three levels:-

High

Medium

Low

## D. RISK MONITORING

- Monitoring the performance of the production machine on a quarterly basis
- Log files are checked to ensure the anti-virus programmes are updated daily
- Activity log files are checked for any discrepancies and Intrusion Detection Systems are installed to monitor network traffic on a real time basis
- Staff are trained on the BRCP and testings are carried out every year
- An inventory monitoring software is installed in computers to check for any unauthorised software
- Meetings of the ITSC are held in every two (2) month in which progress of the ongoing projects are reviewed and monitored, and proposal of new projects/ purchases are deliberated

## C. RISK CONTROL

- Benchmark tests are carried out to ascertain the reliability and performance as according to the specifications given
- Anti-virus detection tools are installed to detect the presence of any known or potential computer viruses and remove/ isolate any emails containing the virus
- IT Security Policy is in place which establishes controls such as personnel controls, physical security, operating controls, system security and system development controls
- A Business Resumption Continuity Plan ("BRCP") is in place
- Email/ Internet Usage Policy is in place which establishes what is permissible when using Company's resources
- An IT Steering Committee ("ITSC") has been formed to ensure the establishment of effective computerisation plans for the Company in line with corporate objectives and business strategy

**Internet Risks**

Internet risks include key aspects of security such as data confidentiality, data integrity, authentication of users, non-repudiation of transactions and access control.

**INTERNET RISK MANAGEMENT**

**A. RISK IDENTIFICATION**

Risks are identified by the IT staff based on their industry and technical knowledge. Identified risks are deliberated at Working Risk Management Committee meeting and addressed in the Risk Management Manual.

**B. RISK & IMPACT ASSESSMENT**

An assessment is made to establish the degree of impact of the particular risk and the degree of impact is categorised into one of the following three levels:-

Fatal	Significant	Insignificant
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An assessment will also be performed to determine the degree of risk likelihood of the particular risk which are categorised into one of the following three levels:-

High	Medium	Low
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**D. RISK MONITORING**

- Periodic vulnerability testing is conducted
- Contingency plans and procedures have been developed to monitor the acceptable level of tolerance
- ITSC monitors the results of the systems review
- Adequacy of internal/ external expertise is reviewed to ensure sufficient technical support on the Internet insurance system

**C. RISK CONTROL**

- The host systems are not directly accessible by outsider or third party
- A full backup site has been developed to minimise the risk of total internet systems failure
- Systems are reviewed to ensure the performance expectations do not exceed the capabilities of the existing system
- Sufficient allocation of human resources and expertise has been planned to run and support the Internet insurance system

## FINANCIAL RISKS

### Credit Risk

Credit risk represents the loss that would be recognised if counterparties to insurance, reinsurance and investment transactions failed to perform as contracted.

### Liquidity Risk

Liquidity risk arises due to inability of the Group to meet its financial obligations as and when they fall due.

### Investment Risk

Investment risk arises from fluctuation in the market prices of equities. Investment credit risk refers to the ability of an issuer or counterparty to make timely payment of interest, principals and proceeds from realisation of investments. Investment concentration risk arises from over investing in certain asset classes or in securities issued by a single counterparty.

### Interest Rate Risk

Interest rate risk refers to changes in interest income as a result of fluctuation in interest rates in fixed deposits and other fixed interest securities.

### Foreign Currency Risk

Foreign currency risk refers to the risk which arises from fluctuation in the foreign exchange rates.

### Capital Adequacy Ratio Risk

The risk that the Company unable to meet its liabilities due to fluctuations in value of assets and liabilities based on the RBC Framework issued by BNM.

## FINANCIAL RISK MANAGEMENT

### A. RISK IDENTIFICATION

Risks are identified by the Accounts & Finance Department staff based on their industry and technical knowledge. Identified risks are deliberated at Working Risk Management Committee meeting and addressed in the Risk Management Manual.

### B. RISK & IMPACT ASSESSMENT

An assessment is made to establish the degree of impact of the particular risk and the degree of impact is categorised into one of the following three levels:-

Fatal

Significant

Insignificant

An assessment will also be performed to determine the degree of risk likelihood of the particular risk which are categorised into one of the following three levels:-

High

Medium

Low

### D. RISK MONITORING

- Monthly Credit Control Committee meeting is conducted
- Investments are closely monitored by the Investment Committee
- Placement of surplus into fixed deposits and the operational cash flow are monitored by the Accounts & Finance Department and approved by the Chief Executive Officer ("CEO")
- CAR is monitored by Accounts & Finance Department and is reported to the Working Risk Management Committee and the Board on a quarterly basis

### C. RISK CONTROL

- Credit Control Policies and Procedures are established and carried out by the Credit Control Committee
- Investment decisions are directed by the Investment Committee in line with the Group's business goals
- Mark-to-Market valuations of share investment are regularly reported to the Investment Committee
- Achieve Internal Capital Adequacy Ratio ("CAR") higher than the Supervisory target of 130%

# RISK MANAGEMENT (cont'd)

## GENERAL RISKS

### Personnel Risk

Personnel risk refers to the risk of losing key functional personnel which directly affects the ongoing business of the Group.

### Physical Operational Risk

Physical operational risk affects the continuity of the Group in conducting business in the event of disaster.

### Reputational Risk

Reputational risk affects the reputation of the Group when unauthorised statements of the Group were made to the public without the approval of the Executive Director/CEO.

## GENERAL RISK MANAGEMENT

### A. RISK IDENTIFICATION

Risks are identified by the Human Resource staff based on their industry and technical knowledge. Identified risks are deliberated at Working Risk Management Committee meeting and addressed in the Risk Management Manual.

### B. RISK & IMPACT ASSESSMENT

An assessment is made to establish the degree of impact of the particular risk and the degree of impact is categorised into one of the following three levels:-

Fatal

Significant

Insignificant

An assessment will also be performed to determine the degree of risk likelihood of the particular risk which are categorised into one of the following three levels:-

High

Medium

Low

### D. RISK MONITORING

- Well planned remuneration framework is in place to sufficiently attract and retain the key officers of caliber to manage the Company successfully
- BRCP manual is reviewed periodically
- The necessity to make public statements about or for the Group is reviewed by the CEO

### C. RISK CONTROL

- A succession plan for each key functional positions is well in place; in the event of cessation of employment, whether by choice or by accident
- Established BRCP is in place
- Only the CEO or his authorised representative are authorised to make public statements about or for the Group

## IMPLEMENTATION OF RISK BASED CAPITAL FRAMEWORK

Bank Negara Malaysia ("BNM") had issued a Risk-Based Capital Framework for Insurers ("RBC Framework") which is effective from 1 January 2009. The RBC Framework is the capital adequacy framework for all insurers licensed under the Insurance Act, 1996. Under the RBC Framework, each insurer is required to determine the adequacy of the capital available in the insurance and shareholders' funds to support the Total Capital Required ("TCR") which serves as the key indicator of the insurers' financial resilience.

### Capital Management Plan

Pursuant to the RBC Framework, the Board had approved and adopted a Capital Management Plan ("CMP") for the Group's wholly-owned subsidiary, Lonpac in line with the requirements set out in the RBC Framework with effect from 1 January 2009. The objective of the CMP is to optimise the efficient and effective use of resources in order to maximise the return on equity and provide an appropriate level of capital to protect our policyholders taking into account all possible events that can impact directly or indirectly on the operations and financial resilience of the Group whilst complying with rules and regulations issued by the relevant authorities.

The management of capital is guided by the CMP which is driven by the Group's business strategies and organisational requisites which take into account the business and regulatory environment in which the Group operates. In this respect, the Group sets capital targets for both Tier 1 and Tier 2 that is above the minimum regulatory requirements.

The management committee responsible for the oversight of the Group's capital management is the WRMC. All proposals on any deviation from capital targets or capital raising exercise must be addressed to and approved by the RMC prior to recommendation to the Board for approval and implementation.

### Stress Testing

The CMP also includes a Stress Policy which requires a stress test be conducted twice a year to systematically evaluate the extent by which the Group's capital could withstand market shocks and by which capital will be eroded by the principal risks identified due to exceptional but adverse plausible events and to determine the impact on the performance and financial conditions.

The stress tests will facilitate the formulation of appropriate business strategies and methodologies to counter-measure the adverse impact under such events and appropriate measures will be monitored and adopted to address the potential threats as well as to mitigate the effects and maintain an appropriate level of capital commensurate with the risk profile of the Group. The Stress Policy is in line with the Guideline on Stress Testing for Insurers issued by BNM. The stress tests results together with the counter-measures are tabled to the RMC for deliberation and recommendation to the Board for approval prior to the submission to BNM.

The Board and Management view stress testing as an effective risk management tool and have embedded stress testing as part of LPI Group's management culture. The Stress Test Policy incorporates challenging scenarios which have been appropriately defined and will be continuously developed as conditions evolve. In this view, participation of Board and Management is particularly critical in ensuring the robustness of these scenarios as well as in evaluating the stress testing results to gauge the impact on our business decisions.

The effectiveness of the risk management framework within the Group coupled with the CMP had enabled LPI Group to mitigate the impact arising from the spillover effects of the turbulence in the financial markets on the Group's operating performance.

# CODE OF ETHICS, INTEGRITY AND TRUST

The LPI Group via its wholly-owned subsidiary, Lonpac Insurance Bhd ("Lonpac"), operates in an industry where integrity and trust are of utmost importance. The trust and confidence that customers and the public have in Lonpac are vital to the continued growth and success of the Group. The Group actively strives with enthusiasm to conduct itself with integrity and trustworthiness to develop such trust and confidence in the Group. In addition, measures to safeguard the Group's integrity and credibility are undertaken to minimise the exposure to reputational risk arising from unethical or fraudulent conduct by the Group's employees.

The Group recognises that employees play an important role in building a trusted and reputable enterprise in the eyes of the public. The Group has taken, and continues to take proactive initiatives to ensure that employees have shared values and principles, and conduct themselves to the standards that are consistent with the expectations of the customers and the public.

The acceptable conduct expected of employees of the Group is formalised in the form of a clear and documented codes and policies. This is a critical part of building a culture of trust and integrity in employee conduct and behaviour. Included amongst such codes and policies are a Code of Ethics, an Anti-Fraud Policy and an Anti-Money Laundering and Counter Financing of Terrorism Policy.

## CODE OF ETHICS

Persatuan Insurans Am Malaysia ("PIAM") issues guidelines to promote proper standards of conduct and sound and prudent practices amongst general insurance companies. In today's insurance operations, it is essential that these ethical rules be codified and issued as written guidelines in order to promote and maintain a uniform ethical standard.

Lonpac had codified ethical rules that are vital in the Staff Disciplinary Handbook which emphasises on 5 key principles:

- Avoid conflict of interest;
- Avoid misuse of position for personal advantage/ benefit/ preferential treatment in any way;
- Avoid misuse of information for personal gains or for any purpose other than that intended by the Company;
- Observe integrity of records and transactions; and
- Observe confidentiality

## ANTI-FRAUD POLICY

Lonpac has a formalised Anti-Fraud Policy to prevent and detect fraud and fraudulent activities. The Anti-Fraud Policy outlines that employees are responsible in preventing and detecting defalcations, misappropriations and other irregularities. In addition, the Anti-Fraud Policy also sets out the fraud discovery reporting procedures and warns employees on the disciplinary actions against fraudulent acts.

Bank Negara Malaysia ("BNM") requires licensed insurers to report all cases on fraud and defalcation

and breaches of code of ethics and conduct. With effect from 1 November 2000, licensed insurers are required to submit such reports, if any via BNM's Fraud Information Database System ("FIDS").

## ANTI-MONEY LAUNDERING AND COUNTER FINANCING OF TERRORISM POLICY

The Board of Lonpac has approved the Anti-Money Laundering and Counter Financing of Terrorism ("AML/ CFT") Manual which is based on the Anti-Money Laundering and Anti-Terrorism Financing Act 2001, and the Guidelines on AML/ CFT, issued by BNM. The AML/ CFT Manual includes:

- Definition of Money Laundering and Financing of Terrorism
- AML/ CFT measures as follows:
  - Customer Acceptance Policy
  - Customer Due Diligence
  - Record Keeping
  - Ongoing Monitoring
  - Suspicious Transaction Reporting
- Examples of Suspicious Transactions

A communication system is in place to promptly update staff on procedural changes in fighting money laundering and terrorist financing. Part and parcel of this communication is training. Training is conducted for staff to promote the understanding of their fundamental responsibility in adhering to the procedures of verifying customers and reporting of suspicious transactions.

Lonpac remains concern and undertakes, so far as is reasonably possible and practicable, to safeguard itself from being involved with money launderers and terrorist financiers.

# STATEMENT ON INTERNAL CONTROL

The Board of Directors (“Board”) recognises the importance of a sound system of internal control to safeguard shareholders’ investment and the Group’s assets.

The Board’s Statement on Internal Control outlines the nature and scope of internal control of the Group during the year.

## BOARD RESPONSIBILITIES

The Board affirms its overall responsibility for the Group’s system of internal control. This includes reviewing the adequacy and integrity of financial, operational and compliance controls and risk management procedures. In view of the limitations that are inherent in any system of internal control, this system is designed to manage the Group’s risks within an acceptable risk profile, rather than eliminate the risk of failure to achieve the policies and business objectives of the Group. Accordingly, it can only provide reasonable but not absolute assurance against material misstatement of management and financial information and records or against financial losses or fraud.

Following the publication of the Statement on Internal Control: Guidance for Directors of Public Listed Companies (“Internal Control Guidance”), the Board has established an ongoing process for identifying, evaluating and managing significant risks faced by the Group. This ongoing process which includes updating the system of internal controls when there are changes in the business environment or regulatory guidelines, is reviewed by the Board and accords with the Internal Control Guidance. The Board is of the view that the system of internal controls in place for the year under review and up to

the date of approval of the annual report and financial statements is sound and sufficient to safeguard the shareholders’ investment, the interests of customers, regulators and employees, and the Group’s assets.

The Board is also assisted by the Management in the implementation of the Board’s policies and procedures on risk and control by identifying and assessing the risks faced, and in the design, operation and monitoring of the suitable internal controls to mitigate and control these risks.

## RISK MANAGEMENT FRAMEWORK

The Board fully supports the contents of the Internal Control Guidance and with the assistance of the Management, implemented the risk management processes within the Group.

The core business of the Group is underwriting general insurance business by its subsidiary company, namely Lonpac Insurance Bhd (“Lonpac”). Thus, the risk management framework for the Group was established with emphasis on the insurance operations.

The formalisation of the risk management framework was enhanced by the following initiatives:

- A Risk Management Committee (“RMC”) was established to drive the risk management processes in identifying principal business risks and ensures the implementation of appropriate systems to manage these risks. The RMC is supported by the Working Risk Management Committee (“WRMC”) of Lonpac.
- The WRMC, headed by the Chief Executive Officer of Lonpac was established with the responsibility to identify and communicate to the RMC on critical risks (present and potential) in terms of likelihood exposures and impact on the Group’s business and the management action plans to manage these risks on a continuing basis.
- A Working Risk Management Committee – Singapore Branch (“WRMCS”) was established with the responsibility to identify and communicate to the WRMC on critical risks (present and potential) in terms of likelihood exposures and impact on the business of Lonpac’s Singapore branch and the management action plans to manage these risks on a continuing basis. The WRMCS reports to the WRMC at Head Office.
- The consolidated risk profile of the Group and the risk management manual are in place.
- The details of the risk management processes are presented in the Risk Management on pages 81 to 95.

## STATEMENT ON INTERNAL CONTROL (cont'd)

### KEY INTERNAL CONTROL PROCESSES

The key processes that have been established in reviewing the adequacy and integrity of the system of internal controls include the following:

- The Internal Audit function is in place to enable the Audit Committee to discharge its functions effectively. The Internal Audit Department monitors compliance with policies and procedures and the effectiveness of the internal control systems and highlights significant findings in respect of any non-compliance. Audits are carried out on all Head Office departments and branches, the frequency of which is determined by the level of risk assessed, to provide an independent and objective report on operational and management activities of these Head Office departments and branches. The findings of the audits are tabled at the Audit Committee meetings for deliberation and the Audit Committee's expectation on the corrective measures will be communicated to the respective head of the departments and branches. The annual Internal Audit Plan is reviewed and approved by the Audit Committee. A Statement on Internal Audit Function is presented on page 107.
- The Audit Committee of the Group reviews any internal control issues identified by the Internal Audit Department, the external auditors, regulatory authorities and Management, and evaluate the adequacy and effectiveness of the risk management and internal control systems. The Audit Committee also reviews the internal audit functions and quality of internal audits. The minutes of the Audit Committee meetings are tabled to the Board on a periodic basis. Further details of the activities undertaken by the Audit Committee of the Group are set out in the Audit Committee Report on pages 103 and 104.
- The RMC was established by the Board in assisting the Board to oversee the overall risk management processes by identifying principal business risks and ensuring appropriate implementation of systems to manage these risks. The other committees set up to assist the RMC on managing areas of risks for the Group are the WRMC and WRMCS.
- A Risk Management manual was formulated to ascertain that the Group suffers no material interruption to its systems, processes or operations, or material damage to its assets upon the occurrence of any disastrous events. A separate Risk Management manual was also formulated for the Singapore branch. The Risk Management manuals are updated for ongoing changes in the risk profile. In addition, a yearly review on the Risk Management manuals is conducted to ensure the completion of the risk profile and risk management. The primary responsibility for maintaining the various portions of the plan will be assigned to the respective department heads.
- There is an organisational structure with formally defined lines of responsibility and delegation of authority to ensure proper identification of accountabilities and segregation of duties.
- Operating policies and procedures, which incorporate regulatory and internal requirements, are prescribed in the form of circulars to line management in all departments and updated on a timely basis.
- There are operational authority limits imposed on Executive Director and Management within the Group in respect of day-to-day operations, covering underwriting on accepting risks, claims settlement and fixed assets purchases.
- The treaty programme ensures that there is a proper spread of reinsurers with secure ratings of minimum A from accredited rating agencies. The securities of treaty reinsurers are reviewed on an annual basis by the Management and the Audit Committee.
- The Management submits annually a business plan and budget with six (6) year projections for approval by the Board. The Board reviews monthly management accounts, which are measured against budgets and the previous year's results to gauge performance. Any deficiencies are corrected and acted on a timely basis.
- Stress tests are performed semi-annually on Lonpac's financial position which commensurate with its risk profile and the business environment in line with Guideline on Stress Testing for Insurers issued by Bank Negara Malaysia ("BNM"). The stress tests are used as a risk management tool to identify potential threats to Lonpac's financial health due to exceptional but plausible adverse events. The results in the stress test report are deliberated at WRMC meeting and thereafter tabled at RMC meeting.

The RMC will then deliberate and recommend the Stress Test Report to the Board for approval for submission to BNM.

- On an annual basis, the Internal Audit Department reviews the stress test policy to provide a regular and independent assessment in ensuring the quality and effectiveness of the stress test policy as required under the Guideline on Stress Testing for Insurers. The internal audit report on the review of the stress test policy is presented at the Audit Committee meeting.
- The public releases of quarterly reports are made after being reviewed by the Audit Committee and the approval of the Board.
- Management meetings chaired by the Chief Executive Officer of Lonpac are conducted regularly to review financial performance, business development and deliberate on management and corporate issues.
- A Data Management and Management Information System ("MIS") Framework was formulated and approved by the Board in accordance with the Guidelines on Data Management and MIS Framework issued by BNM. The maintenance of adequate data quality is carried out at all times and internal controls, either in the systems or manually performed will be incorporated to further improve the data quality. All Head of Departments determine the materiality level for critical and non-critical data for data accuracy assessment purpose. The assessment of data accuracy is carried out on a half yearly basis and the assessment report will be submitted to the WRMC for review prior to tabling at the RMC and Board meetings.

- The Investment Committee is responsible for formulating policies, strategies as well as reviewing matters relating to the investment in shares and private debt securities.

- The IT Steering Committee is chaired by the Chief Executive Officer of Lonpac. The committee is responsible for establishing effective computerisation plans, authorising IT related expenditure above pre-defined limits and monitoring the progress of approved projects.

- Internal control requirements are embedded in computerised systems as well.

- The Systems and Methods Committee (previously known as Internet Committee) is chaired by the Chief Operating Officer of Lonpac. During the year, the committee changed its name to Systems and Methods Committee in view that its scope has been expanded to encompass the review of existing operational procedures involving E-Systems enhancement and the study of up-to-date information communication technology. The scope of the committee includes the following:

- Using technology to facilitate delivery of prompt efficient services and making it simple and easy for the customers/ prospects and intermediaries to transact business

- Simplifying workflow and enhancing user-friendliness resulting in costs savings

- Providing a secured environment in all E-Transactions

- Reviewing existing processes and operational procedures with a view to simplify and increase efficiency via E-Enablement

- Proposing new methods and processes via E-Enablement to improve efficiency and effectiveness

The terms of reference of the committee are as follows:

- To provide online insurance services and an alternative communications channel to the agents, policyholders and prospective customers in a secured and user-friendly environment

- To review and provide recommendations for streamlining of workflow and improving efficiency and increasing E-Enablement of processes and procedures that involves E-System enhancement resulting in reduced costs and improved efficiency

The committee also monitors the risk management of Internet insurance services and thereafter reports to the WRMC.

- The Business Development - Agency Division meetings are chaired by the Assistant General Manager - Business Development and are held to review the performance of Agency Division and deliberate on business development, marketing and sales issues.

- The Credit Control Committee is chaired by the Chief Executive Officer of Lonpac and represented by the Chief Operating Officer, Senior General Manager - Business Development, Head of the Business Development Divisions and Accounts & Finance Department. Monthly meeting is conducted with the objective of maximising the conversion of accounts receivable into cash flow and minimising bad debts written off.

## STATEMENT ON INTERNAL CONTROL (cont'd)

- The Business Resumption Continuity Plan ("BRCP") Committee is chaired by the Chief Executive Officer of Lonpac. The committee is responsible to prepare a BRCP to ensure that the Group suffers minimum interruption to its systems, processes or operations in the event of any disasters.
- A BRCP manual was formulated to ascertain that the Group suffers no material interruptions to its systems, processes or operations, or material damages to its assets upon the occurrence of any disastrous events. A separate BRCP manual was formulated for the Singapore branch. The BRCP is tested every year including testing for the Singapore branch. The BRCP testings are being observed by the Internal Audit Department to provide an independent evaluation of the testing preparation and to highlight any deficiencies noted during the testings. A written assessment report on the BRCP testing is prepared by the Internal Audit Department for Audit Committee's review. The results of the BRCP testings are submitted to BNM as required under the Guidelines on Business Continuity Management ("BCM").
- On an annual basis, the Internal Audit Department reviews the level of commitment to BCM and overall preparedness against Lonpac's BCM policies and regulatory requirements. Gaps identified will be documented in the audit report to the Audit Committee together with the action plans for further improvement by the respective business functions. An executive

summary of the audit report, which includes comments from the Audit Committee will be submitted to BNM as required under the Guidelines on BCM.

- Training and development programmes are conducted to enhance staff competencies and maintain a risk control conscious culture.
- Training for agents are conducted to enhance their competencies and technical knowledge for better risk management in developing the agency networking.
- Staff and agents are trained on Anti-Money Laundering and Counter Financing of Terrorism ("AML/ CFT") to promote understanding of their fundamental responsibility in adhering the procedures of verifying customers and reporting of suspicious transactions.
- There are proper guidelines within the Group for hiring and termination of staff, and annual performance appraisals in place to ensure that staff are competent in carrying out their responsibilities.

### REVIEW OF THE STATEMENT BY EXTERNAL AUDITORS

The external auditors have reviewed this Statement on Internal Control for inclusion in the annual report of the Group for the year ended 31 December 2009 and reported to the Board that nothing has come to their attention that causes them to believe that the statement is inconsistent with their understanding of the process the Board has adopted in the review of the adequacy and integrity of internal controls within the Group.

This Statement on Internal Control is made in accordance with the resolution of the Board of Directors dated 7 January 2010.

# AUDIT COMMITTEE REPORT

## MEMBERS OF THE AUDIT COMMITTEE

### CHAIRMAN

#### Independent Non-Executive Director

Tan Sri Dato' Thong Yaw Hong

PSM, SIMP, DSAP, DIMP, JMN, SMP, JBS, AMN, BA (Econs Hons), MPA (Harvard), AMP (Harvard), D.Econ (Hon)

### CO-CHAIRMAN

#### Independent Non-Executive Director

Dato' Haji Abdul Aziz bin Omar

DIMP, ACA (England & Wales), CA (M), FIBM (M'sia)

### MEMBERS

#### Independent Non-Executive Director

Dato' Yeoh Chin Kee

DIMP, FCPA (Aust.), F Fin (Aust)

#### Independent Non-Executive Director

Quah Poh Keat

FCCA (UK), CA (M), CPA (M), ACMA (UK), Fellow MIT (M'sia)

## 1. ATTENDANCE OF MEETINGS

The details of attendance of each member at the Audit Committee meetings held during 2009 are as follows:

Composition of Audit Committee	Number of Audit Committee Meetings	
	Held	Attended
<b>Tan Sri Dato' Thong Yaw Hong</b> Chairman/ Independent Non-Executive Director	9	9
<b>Dato' Haji Abdul Aziz bin Omar</b> Co-Chairman/ Independent Non-Executive Director	9	9
<b>Dato' Yeoh Chin Kee</b> Member/ Independent Non-Executive Director	9	9
<b>Quah Poh Keat</b> Member/ Independent Non-Executive Director	9	9

The dates of the Audit Committee meetings are as follows:

- 8 January 2009\*
- 10 February 2009
- 8 April 2009
- 6 July 2009
- 23 July 2009
- 27 August 2009
- 8 October 2009\*
- 22 October 2009
- 26 November 2009

\* Met with the external auditors without any executive Board members and management staff present.

## 2. COMPOSITION AND TERMS OF REFERENCE

### 2.1 Membership

The Board of Directors ("Board") shall elect an Audit Committee from amongst themselves (pursuant to a resolution of the Board) which fulfils the following requirements:

- i. the Audit Committee shall consist of at least three (3) directors;
- ii. all members of the Audit Committee should be non-executive directors and the majority of the Audit Committee must be independent directors; and
- iii. at least one (1) member of the Audit Committee:
  - (a) must be a member of the Malaysian Institute of Accountants ("MIA");
  - (b) if he/ she is not a member of the MIA, he/ she must have at least three (3) years' working experience and:
    - he/ she must have passed the examinations specified in Part I of the 1st Schedule of the Accountants Act 1967; or
    - he/ she must be a member of one of the associations of accountants specified in Part II of the 1st Schedule of the Accountants Act 1967; or
  - (c) fulfils such other requirements as prescribed or approved by Bursa Malaysia Securities Berhad ("Bursa Securities").

# AUDIT COMMITTEE REPORT (cont'd)

The Board shall ensure that effective orientation is given to the new Audit Committee members. A meeting should be held for the new Audit Committee members with the finance director and members of management who are responsible for the financial control system and internal audit.

The Board to ensure that there are adequate experienced directors on the Audit Committee.

## 2.2 Chairman/ Co-Chairman

The members of the Audit Committee shall elect a Chairman/ Co-Chairman from amongst themselves who shall be an independent director.

## 2.3 Meetings and Minutes

- The Audit Committee will hold not less than four (4) meetings a year, although additional meetings may be called at any time at the Audit Committee Chairman's/ Co-Chairman's discretion or if requested by any Audit Committee member, the management, the internal or external auditors.
- The Head of Internal Audit will attend the meetings. Representatives of the external auditors are to be in attendance at meetings where matters relating to the audit of the statutory accounts and/ or the external auditors are to be discussed.
- The Audit Committee members shall meet with the external auditors at least twice a year, without any executive Board members and management staff present.
- The Chief Executive Officer and/ or other appropriate officers may be invited to attend, except for those portions of the meetings where their presence may be considered inappropriate, as determined by the Chairman/ Co-Chairman.
- The quorum for each meeting shall be at least two thirds (2/3) of the members with independent directors forming the majority.
- The Company Secretary shall be the Secretary to the Audit Committee.
- Minutes of each meeting will be circulated to each member of the Audit Committee and the Audit Committee Chairman/ Co-Chairman shall report on each meeting to the Board.

## 2.4 Authority and Rights

The Audit Committee shall, at the Company's expense:

- i. have authority to investigate any matter within its terms of reference;
- ii. have the resources which are required to perform its duties;
- iii. have full and unrestricted access to any records, information, property and personnel of the Company;
- iv. have direct communication channels with the external and internal auditors;
- v. be able to obtain independent professional or other advice; and
- vi. be able to convene meetings with the external auditors, the internal auditors or both excluding the attendance of the other Board members and employees, where deemed necessary.

## 2.5 Duties and Responsibilities

The duties and responsibilities of the Audit Committee shall be:

### INTERNAL AUDIT

- To review and report the adequacy of the scope, functions, competency and resources of the internal audit function and that it has the necessary authority to carry out its works;
- To review the results of the Group's internal audit procedures and the adequacy of actions taken by the management based on the reports;
- Review any appraisal or assessment of the performance of the internal auditors and approve any appointment or termination of the senior internal audit staff.

### EXTERNAL AUDIT

- To review with the external auditors, the audit plan, scope of the audit and the areas of audits of the Company/ Group;
- To review with the external auditors, their evaluation of the system of internal controls and audit findings;

- To discuss problems and reservations arising from the audit, and any other matters the auditors may wish to discuss;
- To review the external auditors' management letter and management's response;
- To review the audit report with the external auditors;
- To review and report the assistance given by the Company's/ Group's Officers to the external auditors and the overall conduct of the audit;
- To review the competency, independency and suitability of the external auditors for recommendation to the Board for re-appointment and the audit fee thereof;
- To make appropriate recommendations to the Board on matters of resignation or dismissal of external auditors.

#### *FINANCIAL REPORTING*

- To review the annual audited financial statements of the Company/ Group and quarterly results of the Company/ Group, and thereafter submit them to the Board for approval, focusing particularly on:
  - True and fair view of the Company's/ Group's financial position and performance;
  - Changes in or implementation of new accounting policies and practices;
  - Significant adjustments arising from the audit;
  - The going concern assumption;
  - Significant and unusual events; and
  - Compliance with applicable approved accounting standards and other legal and regulatory requirements.
- To ensure prompt publication of annual audited financial statements.

#### *RISK MANAGEMENT*

- To review the adequacy and effectiveness of risk management and internal control systems instituted within the Group.

#### *RELATED PARTY TRANSACTIONS*

- To review any related party transactions that may arise within the Company/ Group.

#### *OTHER FUNCTIONS*

- To review and verify any allocation of shares option to eligible employees in accordance with the criteria set by the Employees' Share Option Scheme ("ESOS") Committee;
- To perform any other functions as may be agreed by the Audit Committee and the Board.

### 3. SUMMARY OF ACTIVITIES

During the year under review, the Audit Committee carried out the following activities:

#### **3.1 Financial Results**

- Reviewed the annual audited financial statements of the Company/ Group, semi-annual returns and quarterly results of the Group, and thereafter, submitted them to the Board for approval.
- Reviewed the Statement on Internal Control pursuant to Paragraph 15.26(b) of Bursa Securities' Listing Requirements for Board's approval.
- Reviewed the Press Release Statements and recommended to the Board for approval.

#### **3.2 Internal Audit**

- Reviewed the results of the Group's internal audit procedures and the adequacy of actions taken by the management based on the Internal Audit Reports. Where appropriate, the Audit Committee has directed the management to rectify and improve controls and operational workflow based on the internal audit's recommendations for improvements.
- Reviewed the Internal Audit Reports arising from the follow-up reviews following each audit.
- Reviewed and approved the Annual Report of the Audit Committee for insurance subsidiary in respect of the financial year ended 31 December 2008 for submission to Bank Negara Malaysia ("BNM"), pursuant to the Prudential Framework of Corporate Governance for Insurers.

# AUDIT COMMITTEE REPORT (cont'd)

- Reviewed the Internal Audit Reports on Compliance with BNM's Circular no. JPI: 7/2006 – Breach of Guidelines to Control Operating Costs of General Insurance Business.
- Reviewed the Compliance Checklist on the Corporate Governance Guide on matters pertaining to Audit Committee.
- Reviewed the Revised Audit Committee Charter pursuant to the Corporate Governance Guide and recommended to the Board for approval.
- Reviewed and approved the Revised Internal Audit Charter.
- Reviewed the quality and effectiveness of Lonpac's Stress Test Policy pursuant to the Guideline on Stress Testing for Insurers issued by BNM.
- Reviewed the Internal Audit Reports on the Observation of Business Continuity Plan/ Disaster Recovery Plan testings pursuant to the Guidelines on Business Continuity Management ("BCM") issued by BNM.
- Reviewed the level of commitment to BCM and the overall preparedness against Lonpac's BCM policies and regulatory requirements in accordance with the Guidelines on BCM.
- Discussed and approved the Internal Audit Plan 2010 for the Group.
- Noted the signed Service Level Agreement – Lonpac Insurance Bhd ("Lonpac") Singapore Branch on the outsourcing of Internal Audit services to LPI Capital Bhd ("LPI").
- Reviewed the adequacy of scope, functions, competency and resources of the internal audit function and evaluated the performance of the Internal Auditors.
- Reviewed and noted the Progress Reports of the Internal Audit Plan.

### 3.3 External Audit

- Reviewed the following of the external auditors:
  - their audit plan, audit strategy and scope of audits of the Company/ Group for the year;

- their evaluation on the system of internal controls of the Company/ Group;
- the results of the annual audit, management letter for insurance subsidiary including the management's response to the findings of the external auditors and also the auditors' report to the shareholders.
- Reviewed the competency, independency and suitability of the external auditors and recommended to the Board for re-appointment and the audit fee thereof and also approved the provision of non-audit services by the external auditors.
- Discussed the updated letters of engagement external auditors.
- Discussed the engagement letter from the external auditors on the review of Board's Statement on Internal Control.
- Noted the Review Report of the External Auditors to the Board on the Statement on Internal Control.
- Reviewed the draft Representation Letter to external auditors pursuant to the Guidelines on Audit Committees and Internal Audit Department.
- Met with the external auditors twice without any executive Board members and management staff present.

### 3.4 Related Party Transactions

- Reviewed the nature of related party transactions within LPI Group and recommended for Board's approval.

### 3.5 Other Matters

- Noted the appointment of a new Audit Committee member.
- Noted the Whistleblowing Policy adopted for LPI Group.

## 4. AUDIT COMMITTEE TRAINING AND EDUCATION

During the financial year ended 31 December 2009, the Audit Committee members have attended conferences, seminars and training programmes on the following areas:

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### **Corporate Governance**

- Financial Institutions Directors Education (“FIDE”) Programme :Talk by Jamie Allen on “The Global Financial Crisis – Implications for Corporate Governance in Asia”
  - FIDE Programme :Talk by Professor Mervyn King on “Governance Trends and Issues”
  - FIDE Programme : New Module Risk Management in Islamic Finance
  - Financial Industry Conference
    - Risk Management Practices in Financial Institutions – “What Went Wrong and Where Do We Go from Here”
    - Strengthening Institutional and Market Resilience – The Supervisory Agenda
    - Approaching Risks in Large and Complex Organisations
  - FIDE Programme : Lunch talk by Mr. David Webb on “Reforming Governance and Adding Value : An Investor’s Struggle”
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### **Role of An Effective Board**

- FIDE Programme : Module 1 – Role of the Board in Changing Financial, Legal, Regulatory and Business Environment
  - FIDE Programme : Module 2 – Practices and Processes that Promote/ Impede Effective Boardroom Deliberations
  - FIDE Programme : Module 3 – The Role of the Board in Enterprise-Wide Risk Management
  - FIDE Programme : Module 4 – The Board’s Responsibility for Internal Controls, Financial Reporting and Capital Management
  - FIDE Programme : Module 5 – Building Board Teams, Compensation Issues and Role of the Board in Strategy and Stakeholder Relations
  - FIDE Programme : A Session with Mr. Jim Rogers on “How I See the World Today”
  - FIDE Programme :Talk by Professor James Sebenius on “3D-Negotiation : A Strategic Tool for Board and Senior Executives”
  - High Performance Directors’ Conference
  - FIDE “Townhall Session with BNM”
  - FIDE Programme : Focus Group for Nomination Committee/ Remuneration Committee Programme
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### **Banking**

- In-House Training Programme : Current Development of Islamic Banking and Finance
  - The 13th Malaysian Banking Summit: “Riding Out the Global Financial Crisis – Banking Reforms and Revival”
  - Dialogue with Dato’ Razif, Deputy Governor, BNM on “Islamic Banking – The Way Forward”
  - Seminar on “Masterclass for Islamic Bank’s Board of Directors”
  - Anti-Money Laundering & Counter Financing of Terrorism (AML/ CFT) Trends & Typologies Seminar
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### **Accounting & Economics**

- Tun Ismail Ali Chair : A Public Lecture on Comparison of the Financial Crises : Japan and Asia in 1997 – 1998 vs US 2008 – 2009
  - Forum on FRS 139 Financial Instruments : Recognition & Measurement entitled “The Challenges of Implementing FRS 139”
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### 5. INTERNAL AUDIT FUNCTION

The Audit Committee is assisted by the Internal Audit Department ("IAD") in discharging its duties and responsibilities. The internal audit function is established to add value and improve the Group's operations by providing independent, objective assurance and consulting activities through its audit of the Group's key operations and also to ensure consistency in the control environment and the application of policies and procedures. The Head of IAD reports directly to the Audit Committee to maintain the objectivity of the internal audit function.

The IAD undertakes internal audit functions based on the audit plan that is reviewed and approved by the Audit Committee. The audit plan covers review of adequacy of operational controls, risk management, compliance with established procedures, laws and regulations, quality of assets, management efficiency, computer application system and telecommunications network, amongst others.

Further details of the activities of the Internal Audit Department are presented in the Statement on Internal Audit Function on page 107.

# STATEMENT ON INTERNAL AUDIT FUNCTION

The Internal Audit function is an integral part of the assurance framework and its primary mission is to provide assurance on the adequacy and effectiveness of the risk, control and governance framework of the Group. An Internal Audit Department ("IAD") was established to undertake the internal audit function within the Group to add value and improve the Group's operations by providing independent, objective assurance and consulting activities through its audit of the Group's key operations and also to ensure consistency in the control environment and the application of policies and procedures.

The Head of IAD reports directly to the Audit Committee to maintain the objectivity of the internal audit function. The position, objective, independence, authority, roles and responsibilities, resourcing, outsourcing and scope of audit work of the IAD are articulated in the Internal Audit Charter.

The IAD undertakes the internal audit function based on the annual audit plan that is reviewed and approved by the Audit Committee. The audit plan includes review of adequacy of operational controls, risk management, compliance with established procedures, laws and regulations, quality of assets, management efficiency, computer application system and telecommunications network. The Audit Committee also reviews the adequacy of the scope, functions, competency and resources of the internal audit function to ensure that it is adequately resourced with competent and proficient internal auditors.

A risk based audit approach is used to ensure that the higher risk activities in each auditable area are audited annually. These are designed to evaluate and enhance risk management, control and governance processes to assist management to achieve its corporate goals. The audits also help to ensure that appropriate instituted controls are in place, effectively applied and achieved acceptable risk exposures in accordance with the Group's risk management policy.

During the year, the IAD conducted various internal audit engagements in accordance with the annual audit plans that are consistent with the organisation's goals. The IAD evaluated the adequacy and effectiveness of key controls in responding to risks within the Group's governance, operations and information systems regarding the:

- Relevancy, reliability, integrity, accuracy, completeness and timeliness of financial and operational information;
- Adequacy of controls to safeguard the Group's assets;
- Adequacy and effectiveness of the system of internal controls;

- Compliance with policies, procedures, rules, guidelines directives, laws and regulations;
- Integrity of risks measurement, adequacy of control and reporting systems and compliance with approved risk management policies and procedures;
- Effectiveness of Information System ("IS") in supporting the business activities and adequacy of controls over IS management, systems development and programming, computer operations and security and data integrity;
- Quality and effectiveness of the stress test policy;
- Nature of the related party transactions and conflict of interests situation that could raise questions of management integrity; and
- Level of commitment to Business Continuity Management ("BCM") and overall preparedness against the Group's BCM policies and regulatory requirements, and adequacy and effectiveness of Business Continuity Plan and Disaster Recovery Plan testings.

The Internal Audit Reports prepared by the IAD arising from the audits are deliberated by the Audit Committee and recommendations are duly acted upon by the management. Follow-up reviews are conducted by the IAD to ensure that all matters arising from each audit are adequately addressed by the auditee/management.

IAD participates as consultative role prior to the implementation of new IT projects in evaluating the risk exposures and overseeing the controls issues to ensure that control procedures are in place to mitigate the risks identified.

All the internal audit activities were performed in-house.

The total cost incurred in managing the IAD in 2009 was RM1,402,000.

A summary of the internal audit cost is as follows:

Cost Category	RM '000	% of total cost
<b>Manpower</b>	1,347	96.08
<b>Training</b>	9	0.64
<b>Travelling (inclusive of accommodation)</b>	46	3.28
<b>Total</b>	1,402	100.00