

STATEMENT ON RISK MANAGEMENT & INTERNAL CONTROL

BEING A WHOLY-OWNED SUBSIDIARY OF PERMODALAN NASIONAL BERHAD (PNB), PHNB BENEFITED FROM THE RESOURCES OF PNB BY VIRTUE OF THE SERVICE LEVEL AGREEMENT BETWEEN PHNB AND PNB FOR THE OUTSOURCING OF SUPERVISORY AND BACK OFFICE FUNCTIONS TO PNB WHICH INCLUDES INTERNAL AUDIT, COMPLIANCE AND RISK MANAGEMENT.

Recognising the significance of achieving good regulatory governance, management and operations, PHNB, through its parent company, PNB, affirms its full commitment to ensure a solid risk management and internal control system is put in place. The establishment of this system ultimately aids in creating, enhancing and protecting value; whilst adhering to our company's policies and achieving our goals and objectives within the constituted risk appetite.

The internal control system in PHNB covers Risk Management, Financial and Management Audit and Compliance. The system integrates effective processes with performance-focused risk management and internal control; including reviews on adequacy and effectiveness of the system at every level of the Management and across each Business Unit.

RISK MANAGEMENT

The Board of PHNB acknowledges that risk management is an integral part of PHNB's business model and an effective monitoring and review of significant risks on a continuous basis is essential in ensuring the integrity of PHNB's internal control framework. The Board has delegated the responsibility of overseeing risk management activities of PHNB to the Risk Management Committee of the Board of Directors of Permodalan Nasional Berhad (RMC).

The RMC is responsible for assisting the Board of PHNB by overseeing and approving the ongoing development and maintenance of PNB's Enterprise Risk Management Framework (ERM) and activities. The RMC is delegated with the responsibility to assess, identify, measure and monitor the overall risk exposure and ensuring a sufficient level of risk mitigation is in place.

RISK MANAGEMENT FUNCTION

Among the primary roles of the Risk Management Department (RMD) is to formulate, implement, monitor and continuously review risk management frameworks, policies, procedures, risk limits and risk management related internal controls. The framework provides a strong control environment through the implementation of appropriate systems and risk assessment processes to manage risks.

Scope of Work

The key elements of risk management can be summarised as follows:

- Risk Assessment Process: The overall process of risk identification, risk analysis and risk evaluation;
- Risk Monitoring and Review: The Risk Register and Key Risk Indicators (KRIs) are used as a tool to monitor and manage changes of its exposure over time.

The main key risks that might potentially affect the performance of PHNB are detailed under "Risk Management" of the Management Discussion and Analysis section. All identified risks are recorded in respective risk registers, together with the identification of existing and any future controls to mitigate such risks. All controls and action plans are continuously monitored to ensure their effectiveness in the current business environment and to safeguard PHNB against risks that could potentially affect the objectives and strategies of PHNB.

The independence of the risk management function and close alignment to the business ensures consistent and effective risk oversight via:

- Implementation of a holistic risk management process which provides a framework for building organisational resilience in ensuring critical business functions continue to operate during disruptions;
- Maintaining an incident management plan with high degree of readiness to safeguard against financial and physical disruptions; and
- Inculcating a proactive risk culture.

Activities in 2018

PHNB, in collaboration with the Risk Management Department of PNB, has reviewed and enhanced the system of recovery from potential threats by updating PHNB's Business Continuity Management (BCM) program.

- The BCM program included the review of Business Impact Analysis (BIA) and Departmental Business Continuity Plan (DBCP) for PHNB which was conducted via workshops held in February 2018 and April 2018.
- The BIA exercise requires PHNB to review critical business functions and business dependencies. This allows PHNB to determine appropriate business continuity strategies, which enables PHNB to resume its key business function within the predetermined time.

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INTERNAL AUDIT FUNCTION

By virtue of the Service Level Agreement between PHNB and PNB for the supervisory and back office functions to PNB, the internal audit function is outsourced to the Financial and Management Audit Department ("FMAD") of PNB. FMAD's primary responsibilities are to provide independent, objective assurance and consulting services designed to add-value and improve the operations of PNB Group, including PHNB, by ensuring that risk management, internal controls and established procedures are adhered to. This is achieved by carrying out financial, operational and information systems audits on core departments of PNB Group. These audit activities will provide the Board of Directors of PNB and PHNB the reasonable assurance with regard to the adequacy and effectiveness of risk management, internal controls and corporate governance.

Scope of work

FMAD develops a risk-based audit plan for the year encompassing assurance and consulting services, which is then reviewed and approved by the Audit Committee of the PNB Board of Directors. The annual audit plan, which also covers PHNB, is strategically aligned with PNB's business strategies and objectives.

Bursa Malaysia Main Market Listing Requirements requires the management company of a REIT to establish its own audit committee by 31 December 2018. On 27 November 2018, the Audit Committee of the Board of PHNB was established. In view of this, FMAD will also be reporting to the Audit Committee of PHNB.

During the year, FMAD communicates the result of the planned audits, follow-up audits to the Audit Committee of PNB and is now reporting to the Audit Committee of PHNB beginning 2019.

The scope of the audit work can be summarised as follows:

- Assets are safeguarded;
- Risks are identified and managed;
- The reliability and integrity of financial and operating information, and the means used to identify, measure, clarify and report such information are clearly determined;
- The systems established comply with policies, plans, procedures and regulations that have significant impact on operations and reports;
- The efficiency of resources employed in the relevant areas; and
- The results of operations or programmes are consistent with established objectives or goals and whether these operations or programmes are carried out as planned.

Activities in 2018

To ensure compliance with relevant policies, procedures, laws and regulations, FMAD had carried out audit activities on PHNB during the financial year. Among the areas covered by FMAD are PHNB's financial performance, budget review, cash and bank accounts, accounts payable, accounts receivable and also IT management.

In relation to operations, FMAD reviewed PHNB's Asset Management activities particularly on the Property Managers' performance, rental collection, occupancy rate, tenancy and agreements, building safety and also licensing permits.

FMAD also conducts regular follow-up audits on the status of the management's action plans to rectify matters highlighted in the audit report. These follow-up audits are to ensure that corrective actions are taken to resolve the identified issues.

CORPORATE COMPLIANCE AND POLICY STATEMENT

In safeguarding the interest of more than 13 million unit holders, it is paramount that PNB demonstrates the highest standards of governance and compliance with the requirements of the law and regulatory authorities. In line with PNB's vision to be a Distinctive World Class Investment House, compliance with high ethical standards as well as legal and regulatory obligations is fundamental to the preservation of our reputation for integrity.

A systematic and clearly defined approach therefore needs to be established and implemented to ensure compliance with all relevant laws, regulations and guidelines, internal policies and procedures and ethical standards.

Compliance governance structure

A Compliance Officer assumes the key responsibility to establish, implement, operate and monitor the Compliance Programme for the PNB Group, including PHNB. Meanwhile, the Compliance Committee of the Board of PNB supervises the Compliance Officer and oversees the implementation and operation of the Compliance Programme by the Compliance Department.

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CORPORATE COMPLIANCE AND POLICY STATEMENT (CONTD.)

Overview of compliance programme

A Compliance Programme, including for PHNB, has been established and implemented based on the fundamental elements described in the Guidelines on Compliance Function for Fund Management Companies issued by the Securities Commission of Malaysia. The Compliance Programme is a key component of the commitment to achieve the highest standards of corporate conduct. It is reasonably designed to foster compliance with applicable laws and regulations, the Capital Markets and Services Act 2007 and other requirements relevant to the business. As the Compliance Programme is dynamic, it is regularly reviewed and enhanced to meet the evolving compliance standards. The fundamental elements of the Compliance Programme are described in greater detail as follows:

1. Compliance Manual

The Compliance Manual is constructed with the intention of providing guidance for staff members, across all roles and responsibilities, to help achieve and maintain compliance with all applicable laws and regulations in performing their daily operations. The Manual also establishes the expectation that management, employees, and agents of PNB must act in accordance with the law, as well as all applicable company policies, procedures and guidelines.

2. Education and Training

PNB and its group of companies are committed to communicating the standards, policies, procedures and guidelines to all directors and employees. As part of the efforts in inculcating a compliance culture, provision of the education and training to new and existing employees on a variety of compliance-related topics are held. Training programmes are reviewed and updated periodically, and additional areas of training are also added from time to time.

3. Liaising with the Regulatory Authorities

In dealing with the regulatory authorities, the Compliance Department is committed in ensuring high values and ethical standards are adopted by PNB group of companies and its employees in discharging their duties. It is our responsibility and commitment to deliver any required reports by the regulatory authorities in a timely and effective manner.

4. Compliance Review and Advice

In ensuring compliance with securities laws, regulations and relevant guidelines, as well as early detection and prevention of any breaches, we perform a compliance review and monitoring on business units within the PNB Group using a risk-based approach and, where necessary, advise on particular areas for improvement. The compliance review conducted is also to meet the need to provide assurance and comfort to the stakeholders on PNB's compliance status to the applicable laws, rules and regulations.

5. Supervision of Anti-Money Laundering and Counter-Terrorist Financing Matters

In compliance with the Anti-Money Laundering, Anti-Terrorism Financing and Proceeds of Unlawful Activities Act 2001, PNB has established its Anti-Money Laundering and Counter-Terrorism Financing (AMLA) policy and procedures which had been implemented throughout the Group. We also conducted Know Your Customers (KYC) screening on the tenants and other relevant stakeholders of PHNB to ensure compliance to AMLA and other regulatory requirements.

None of the weaknesses or issues identified during the review for the financial year has resulted in non-compliance with any relevant policies or procedures, listing requirements or recommended industry practices that would require disclosure in the Annual Report.

CONCLUSION

The Board is of the view that the system of risk management, internal control and compliance for the year under review and up to date of approval of this statement for inclusion in the annual report is in place, sound and provides a level of confidence on which the Board relies for assurance.

The Board has received reasonable assurance from the Chief Executive Officer and PNB Group Chief Financial Officer that the risk management and internal controls system, in all material aspects, are operating adequately and effectively.

This Statement on Risk Management and Internal Control is made in accordance with the resolution of the Board of Directors dated 29 January 2019.