

2005 Asian Roundtable on Corporate Governance

Bali, Indonesia, 8 and 9 September 2005

Synthesis Note

The 7th OECD / World Bank Asian Roundtable on Corporate Governance took place in Bali, Indonesia on 8 and 9 September 2005, hosted by the Indonesian Capital Market Supervisory Agency BAPEPAM. Principal agenda items included corporate governance of banks, a stock take of progress in policy reforms since the publication of the Asian White Paper in 2003, the role of the board in implementing the OECD Principles of Corporate Governance and corporate governance of state-owned enterprises. In relation to the last topic *OECD Guidelines on Corporate Governance of State-owned Enterprises* were presented, just four months after their adoption by the OECD Council on 28 April 2005. The meeting was opened by a representative of **Dr. Jusuf Anwar**, the Indonesian Minister of Finance.

Sessions 1 and 2 - Corporate governance of banks

The first session was devoted to recent developments in the regulatory framework on corporate governance of banks discussed from the perspective of the Basel Committee by **Mr. Jason George** of the Bank for International Settlements (BIS). This presentation was followed by a presentation on corporate governance of banks in Asia by **Professor Joseph Fan** of the Centre for Institutions and Governance, Chinese University of Hong Kong. Mr. George's presentation started with a brief introduction on the "Core Principles for Effective Banking Supervision", the Basel Committee's fundamental and important guidance on banking supervision, which also includes several issues related to corporate governance of banks. He then elaborated on the draft guidelines titled "Enhancing Corporate Governance on Banking Supervision" which was initially publicized in 1999 by the Basel Committee and is now under revision. The draft covers a wide range of sound corporate governance principles for banks including those related to the role of bank board and senior management. Professor Fan's presentation on corporate governance of Asian banks focused on issues of, amongst others, family owned banks and state owned banks. He emphasised that the corporate governance structure of banks in Asia is basically shaped by the banks' business strategy, ownership type, and more fundamentally the public governance and government regulations.

After the two introductory presentations on corporate governance of banks, the Asian Roundtable on Corporate Governance's Task Force on Corporate Governance of Banks presented the draft Policy Brief on Corporate Governance of Banks in Asia. **Mr. Motoyuki Yufu** of the OECD, secretary to the Task Force, presented the headlines of the draft Policy Brief. The subsequent floor discussion was lead by **Dr. Jesus Estanislao**, Chairman of the Task Force, in close consultation with each of **Mr. Anis Baridwan** of BAPEPAM, **Ms. Ann Marie Kohlligian** of the Federal Reserve Bank of San Francisco, **Mr. Maulana Ibrahim** of the Bank Indonesia, all Task Force members present at the Roundtable, and **Mr. Peter Taylor** of the International Finance Corporation, who also participated in the work of the Task Force members.

Session 3 – A stock take of recent developments in corporate governance in Asia

The third session dealt with a stock take of corporate governance developments in Asia since the publication of the White Paper in 2003. In the first part of this session **Mr. Louis Bouchez** of the OECD presented the main findings of the "2005 Stock Taking of Corporate Governance Related Developments in Asian Roundtable Economies". In the 2003 White Paper the Roundtable economies had committed themselves to undertake a stock-take of developments within two years after publication of the White Paper. The main purpose of the draft report presented is that it should be used as reference source for Roundtable economies and the public to assess progress of implementation of 2003 White Paper Priorities. Furthermore it is intended to identify future topics for agenda Roundtable. As such the report is not

intended to rank or rate Roundtable economies. It is a report on progress in *policy* reforms regarding the six White Paper Priorities. The report is based on public information and responses to a Questionnaire completed (in the period May – August 2005) by policymakers, regulators, stock exchanges, investors, academics, practitioners and other stakeholders from the 13 Roundtable economies. The report shows that significant progress has been made in developing the corporate governance policy framework in the Roundtable economies and provides numerous examples thereof. Based on the draft report, preliminary observations for issues to be covered by the future Roundtable agenda include (i) administrative enforcement, (ii) civil enforcement, (iii) ownership structure, (iv) (fiduciary) duties of directors, (v) corporate governance of groups of companies, and (vi) related party transactions. These topics are in addition to the topics already covered by the two current Task Forces in place, i.e. Corporate Governance of Banks and Corporate Governance of State Owned Enterprises.

In the floor discussion on the draft stock take report several participants provided further insights and updates on the situation in their respective economies. Mrs. Komal Anand from India referred to the use of the Ministry of Company Affairs' website for public consultation on draft legislation and more importantly to the proposed substantive changes to the Company Law which will be sent to Parliament in November this year. Mr. Leok Soon Lee from Malaysia stressed the need to further focus on the role of independent directors in implementing good corporate governance practices. Mr. Edward Chow from Hong Kong gave the example of Hong Kong in achieving full adoption and implementation of IFRS and underlined the fact that full convergence is indeed achievable. Moreover he pointed out that the necessary information is all available (via the IASB website) and thus there is no need to 'invent the wheel'. Mrs. Jaweria Ather referred to the upcoming publication of the ROSC on Pakistan as well as the establishment of the Pakistan Institute of Corporate Governance which was supported by IFC. Mr. Peter Tisman from Hong Kong referred to the public sector code on corporate governance issued by the Hong Kong Institute of Certified Public Accountants. Dr. Xiaopu Zhang from China mentioned that the Chinese Ministry of Finance recently issued guidelines on the implementation of IFRS and moreover the CSRB has imposed a stronger supervisory regime to verify compliance by banks with relevant corporate governance legislation and regulation. Mrs. Selvarany Rasiah from Malaysia explained that in Malaysia all accounting standards will be in compliance with IASB as per 1 January 2006. Moreover she referred to the upcoming reforms of the Company Law which will have an impact on corporate governance of listed companies as well. Mrs. Sopawadee Lertmanaschai from Thailand mentioned that IFRS will be implemented in Thailand by 2006 and furthermore she referred to the upcoming publication of the ROSC on Thailand. Mr. Asif Said from Pakistan referred to the issue by the Central Bank of new regulations on corporate governance of banks at the end of August 2005. Finally, Mr. Kanaka Puradireja from Indonesia explained that in Indonesia in 2004 the Association of Audit Committees has been founded in order to support the work of audit committees.

Subsequently, in the second part of session 3, **Mr. Jamie Allen**, Secretary General of the Asian Corporate Governance Association (ACGA), provided a preview into the upcoming "Corporate Governance Watch 2005" report, which is authored by the ACGA in co-operation with CLSA. CG Watch 2005 covers 10 markets, i.e. China, Hong Kong, India, Indonesia, Korea, Malaysia, Philippines, Singapore, Taiwan and Thailand. More than 400 companies have been investigated; including the top 30-50 companies covered by CLSA for its institutional clients in each of the 10 markets. ACGA works with CLSA on the country rankings as follows: (i) develop scoring methodology and template of questions (which CLSA comments on), (ii) work closely with CLSA research heads in each market to answer the template, and (iii) ensure consistency of approach across the 10 markets. CG Watch 2005 covers five question categories, i.e. (1) CG Rules and Regulations (19 questions), (2) Enforcement (public + private) (18 questions), (3) Political and Regulatory Environment (10 questions), (4) IGAAP (Accounting and Auditing) (13 questions), and (5) CG Culture (18 questions). Mr. Allen also explained the methodology used in the survey. The survey highlights both areas of strength and problematic issues. Recommendations included are (i) review problematic rules and procedures with market participants (e.g., pre-emption rights, voting systems, shareholder meetings); ask the market what it thinks is important; (ii) if mandatory rules are sound (e.g.,

audit committees), ensure they are: (a) implemented; and then (b) *properly* implemented; (iii) improve disclosure of enforcement track records; better enforcement = higher trust in the stock market; (iv) ensure all major laws and regulations are translated and easily accessible; and (v) ask companies and investors to rate the value of different best practices/CG rules, i.e. what works? what doesn't?

This session 3 was concluded by **Professor Kyung Suh Park** from the Asian Institute of Corporate Governance, Business School, Korea University, who presented the key conclusions of the "PECC Macro Corporate Governance Scorecard Project: Evaluation of Corporate Governance in East Asian Economies". This research, undertaken by Professors Stephen Yan-leung Cheung, City University of Hong Kong, and Hasung Jang, Korea University, aims to measure the progress of corporate governance reforms in some East Asian economies as disclosed through two surveys. This study examines this progress in two ways. The first is a stock-taking exercise to take note of on-going reforms in corporate governance rules and regulations. The second covers perceptions of the implementation and enforcement of corporate governance rules as seen by fund managers and analysts. Nine East Asian economies are included in this study, i.e. China, Hong Kong, Indonesia, Korea, Malaysia, the Philippines, Singapore, Taiwan, and Thailand. The research concludes that there is a deviation between the regulatory environment and market perception of corporate governance practices in these economies. Economies equipped with the 'best' rules and regulations are perceived to be the 'worst' in terms of practice by investors. The research paper states that there is no significant difference in the rules and regulations among these economies, but that there is a significant difference in term of market perception of their corporate governance practices.

In reaction to the presentations by Mr. Allen and Professor Park during the floor discussion Mr. John Lim from Singapore mentioned that for corporate governance to improve a holistic approach is needed, to be promoted by a national body of stakeholders in charge of supervising and improving changes made in the policy framework. In addition there is a continuing need for dialogue between regulators and markets in order for private sector firms to better understand the benefits of good corporate governance; in particular also institutional investors should be engaged. Mr. Allen warned for a box ticking mentality to just formally play the "compliance game". It was also suggested by a participant to further assess the methodologies used in the different rating / scoring exercises. Mr. Mats Isaksson from the OECD suggested a method to test respondents who complete the questionnaires and templates used in rating, mostly being investors; first such respondents should be asked how they would rank the different corporate governance criteria and secondly what premium they would be willing to pay for compliance therewith. After respondents completed this exercise they should answer the question what in their opinion good corporate governance encompasses. By doing this test one may get an idea of what perception of corporate governance investors have and thus better value their responses to the first questions. Professor Mak from Singapore pointed out that in the Asian context it is in particular relevant to understand whose interests (i.e. which large shareholders' interests) the (independent) directors are representing. Finally Dr Estanislao from the Philippines concluded in emphasizing that indeed substantial progress has been made in establishing solid corporate governance policy framework in the Roundtable economies. He added that this is not a reason to be complacent but that it is time to focus on the future agenda. Two items which should be addressed include is the role of directors and enforcement by the regulators.

Session 4 – The Boardroom Guide to the OECD Principles of Corporate Governance

Session 4 focused on the role of the board in implementing the OECD Principles of Corporate Governance. **Mr. Peter Dey**, partner with Osler, Hoskin & Harcourt LLP, and member of the Advisory Group to the OECD that is drafting the "Boardroom Guide to the OECD principles of Corporate Governance", stressed in his presentation that the Guide will focus on an aspect of corporate governance generic to all jurisdictions which is: what takes place in or should take place in the boardroom. The Advisory Group has six members (Ira Millstein, Chair, Peter Dey and Dominique de la Garanderie, Vice-Chairs, Gerhard Cromme, Sir Adrian Cadbury and Toyoo Gyoten; Holly Gregory act as counsel) and aims to first publish a

draft of the Guide for public consultation and to finalise the document by mid-2006. Issues to be addressed by the Advisory group include (i) fiduciary duties, (ii) independent directors, and (iii) “tough” board issues. The latter may include the following topics: (1) what is the board’s job?, (2) developing and implementing a governance system, (3) effective board leadership, (4) the “tone at the top”, (5) overseeing management, (6) efficient use of limited governance resources, (7) managing information, (8) dissenting, (9) a “company-defining” decision, and (10) responding to problems. Mr. Dey invited suggestions as to other issues facing directors which the Advisory Group should address as well as further relevant experiences. The Advisory Group intends to combine these in a user friendly way so that they provide guidance to boards on the application of governance guidelines.

Sessions 5 and 6 – Corporate Governance of SOEs

In this session **Mr. Mats Isaksson** presented the OECD Guidelines on Corporate Governance of SOEs which were adopted by the OECD Council in April 2005. The Guidelines form a set of non-binding guidelines and best practices on corporate governance of SOEs. These Guidelines should be viewed as complementary to the OECD Principles of Corporate Governance on which they are based and with which they are fully compatible. The presentation covered the different chapters of the Guidelines. The rationale for developing the Guidelines can be summarized as follows: (i) the scale and scope of the state sector, (ii) the impact of SOEs on economic performance, (iii) the pressure for reform deriving from globalization and liberalization, (iv) specific governance challenges, (v) expected benefits from improvements of SOE governance, and (vi) the strong demand from non-OECD economies. Priorities underlined in the Guidelines include (i) to ensure a level-playing field with the private sector, (ii) to reinforce the ownership function within the state administration, (iii) to improve transparency of SOEs’ objectives and performance, (iv) to strengthen and empower SOE boards, and (v) to provide equitable treatment of minority shareholders.

After the introduction of the Guidelines, the headlines of draft background report prepared by the Asian Roundtable on Corporate Governance’s Task force on Corporate Governance of SOE’s was presented by **Mr. Louis Bouchez** of the OECD. The subsequent floor discussion was lead by **Mr. John Lim**, Chairman of the Task Force. The draft Background report addresses (chronologically) the following issues (i) development and disclosure of an ownership policy, (ii) streamlining of the SOEs’ legal status, (iii) separation of ownership from regulation and other state functions, (iv) organisation of the ownership function, (v) aggregate reporting, (vi) accountability to Parliament, (vii) disclosure of specific obligations, (viii) setting objectives and reporting on performance, (ix) auditing of SOEs, (x) nomination process and composition of SOE boards, (xi) mandate, responsibilities and functions of SOE boards, (xii) evaluation and remuneration of SOE board members, (xiii) treatment of non-controlling shareholders, (xiv) reporting on transactions with related entities, and (xv) relationships with other stakeholders. This session was finalised by a summary by Mr. John Lim of the (possible) policy areas which the Task Force will address in drafting a Policy Brief to be presented at next year Roundtable.

Session 7 – Related activities

In this session different activities and initiatives which (may) have an impact on corporate governance policy development in Asia and which may thus be relevant for the ARCG and its participants were presented and discussed. The first presentation by **Mr. Charnchai Charuvastr**, President Thai Institute of Directors, outlined the activities of **IDEA.Net**. In addition Mr. Charuvastr provided an outline of the joint (cross country) work on the Corporate Governance Scorecard. This exercise was first initiated by the Thailand Institute of Directors and based on those experiences similar initiatives have been developed by respective institutes of directors (IDEA.Net members) in the Philippines, Korea, Hong Kong, Indonesia and China.

Subsequently **Professor Kyung Suh Park**, Asian Institute of Corporate Governance, Business School Korea University, provided a summary of the meeting of the **Academic Network of Asian Corporate Governance Specialists**, which held its first meeting on 7 September 2005 in Bali. In that meeting four papers were presented and discussed (and will be posted on the OECD Asian Roundtable website). In addition participants discussed the future structure and work of the Academic Network. Amongst others it was suggested to involve the participating (junior) academics in a joint cross country research project. Furthermore the Academic Network should try to align possible research with the policy topics focused on by the Roundtable. Finally, the Academic Network will report back to the Roundtable in its annual meeting.

The final presentation by **Mr. Sumant Batra**, Senior Partner Kesar Dass B & Associates, Advocates & Solicitors, India, dealt with the Synthesis Report of the **OECD International Experts Meeting on Corporate Governance of Non Listed Companies**. This meeting was held in Istanbul on 19-20 April 2005, with as its main goals to: (i) discuss policy implications of the on-going debate on corporate governance of NLCs, (ii) shed light on relevance of OECD principles of corporate governance in countries where NLCs and family / founder-owned companies play pivotal economic and social role, and (iii) to analyse and discuss the corporate governance challenges and opportunities for NLCs in the search for external capital. Important policy issues which arose during the meeting include the corporate governance characteristics of NLCs, the driving forces for changing corporate governance practices in NLCs, and the role of a public policy framework in supporting good corporate governance of NLCs. The meeting contributed to better understanding of corporate governance problems and solutions of NLCs. However, many issues remain unresolved and further discussion and research is necessary. Discussions should continue at regional corporate governance Roundtables. It was furthermore agreed that: (i) there is no requirement for a separate (internationally agreed upon) set of corporate governance principles or guidelines. A code for NLCs in addition to the existing local codes and OECD Principles could easily overstretch regulators; (ii) internal mechanisms for improving corporate governance in NLCs should address improving transparency of decision making processes as well as training and education for managers and shareholders; (iii) more research is needed also about the circumstances in which legal and regulatory mechanisms provide a more efficient alternative to the generally preferred contractual arrangements; and (iv) that the International Finance Corporation's corporate governance methodology for family-owned or founder-owned unlisted companies may provide a useful tool that should be further discussed.

Session 8 - Summary and Next Steps of the Asian Roundtable work

During the closing session a short summary of the headlines of the Roundtable meeting was provided by the OECD Secretariat. It was underlined that the Task Force on Corporate Governance of Banks aims to finalise the Policy Brief before the end of the calendar year and that any further input from Roundtable participants should be submitted to the OECD by 30 September 2005. That same deadline applies to any further contributions to the draft stock take report discussed in session 3 which will also be finalised by the end of the year. Reference was also made to the upcoming public consultation later this year for the Boardroom Guide to the OECD Principles of Corporate Governance (as discussed in session 4).

Furthermore the two key areas for the Roundtable's agenda in the coming year were identified to be (i) corporate governance of SOEs, and (ii) enforcement of corporate governance legislation / regulation. While the first issue will be addressed by the Task Force on Corporate Governance of SOEs, the scope and format of how to address the second issue will need to be considered further. Apart from these two priority issues the topics identified in the stock take report were repeated as further crucial areas for policy reform, i.e. (i) administrative enforcement, (ii) civil enforcement, (iii) ownership structure, (iv) (fiduciary) duties of directors, (v) corporate governance of groups of companies, and (vi) related party transactions.

In the subsequent floor discussion Mr. Sumant Batra from India suggested to invite both Sri Lanka and Nepal for future Roundtable events, as well as to consider the topic of corporate governance of small and medium enterprises for the Roundtable's future agenda. Professor Lu Tong from China suggested to consider the format of the presentations, i.e. there should be a balanced mix of presenters from the academic world and policy makers such as regulators. Finally, Mr. Behdad Nowroozi of the World Bank suggested to reserve time for the presentation of country assessments (ROSCs) in the next Roundtable agenda, as well as to focus on corporate governance of non-banking financial institutions and / or the role of (convergence of) listing rules in promoting good corporate governance.