Asian Business Dialogue on Corporate Governance 2003

Thinking Strategically about Governance

October 16, 2003
The Ritz-Carlton, Hong Kong

Conference Report

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Editors: Jamie Allen, Helen Wong

Organised by the Asian Corporate Governance Association

ACGA

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Speakers
Our sincere thanks also goes to our keynote speakers—Mr. Jin Liqun and Justice Jack B. Jacobs—and to all our moderators and speakers for giving so generously of their time and sharing their knowledge and insights.

Opening Keynote Speech

"Corporate Governance and Private Sector Development in Asia"

Jin Liqun
Vice President (Operations 1)
Asian Development Bank, Manila

Mr Jin argued that corporate governance can minimise the costs and tensions inherent in relationships between managers, shareholders and regulators, hence improving bottom-line value. He concluded by urging delegates to think of corporate governance as a "vitamin" (something you want to take) not a "medicine" (something you need to take).

Introduction

It is my honour to address the "Asian Business Dialogue on Corporate Governance 2003" on behalf of the Asian Development Bank (ADB). I am delighted to be here today to share and learn with you where we are in the development of corporate governance in Asia.

Between the mid-1960s and the mid-1990s, Asia—particularly East Asia—grew faster than any other region in the world. Contributing to this success were pro-growth public policies, declining income inequality, rapid growth of exports, high investment and saving rates, and superior accumulation of physical and human capital, among other factors.

Unfortunately, all this was not able to prevent the Asian financial crisis. In the post-crisis period, there was a lot of finger pointing at a host of problems in the crisis countries. It is certainly important to identify the root causes of the crisis, and it is gratifying to see that these countries are serious about getting things right. One of the priorities is to improve governance, both at the government and the corporate level. It is the right approach to fix the problems and ensure sustained, healthy development of this region.

The Chinese have an old admonition against complacency that goes: "Those who do not prepare for troubles far ahead will definitely find their hands full of problems soon." In other words, one should feel the worst when one feels the best.

The nature of Asian business is changing. The demands of Asian markets are increasing. The role of government vis-à-vis the private sector is evolving. In short, the status quo dictating the relationship among firms, investors, and government is being challenged. We must understand WHAT is corporate governance, WHY it is valuable, and HOW to implement it.

So today I would like to touch on two topics. First, I will briefly talk about the academic theories behind the need for corporate governance. Second, I want to share with you the results of some recent research that demonstrates the bottom-line value for good corporate governance. Throughout I will try to place an Asian-filter on these topics.

The theoretical rationale

First, the theories. There has long been academic rationale that explains the tense, costly, and necessary relationship among investors, managers, and regulators. In particular, "agency theory" and "asymmetric information theory" underpin the inherent costs involved in a capitalistic environment where investors provide the money, management controls its usage, and regulators keep watch over this relationship.

In agency theory, the cost of the relationship between investors and the managers is threefold. First, "divergence cost" arises from the fact that shareholders and managers have different goals and incentives. For shareholders, the goal is to maximise shareholder value. For managers, although it is their fiduciary duty to also maximise shareholder value, the goal for some may simply be to maximise their own compensation. This potential conflict of interest leads to the second cost, "monitoring cost", which shareholders bear in order to make sure that divergence cost is minimised. Finally, despite recent bad news, management is NOT the enemy. Shareholders know that management skills are necessary. And so the last cost in this relationship is "incentive cost", which is basically negotiating the right balance between compensation and performance.

The second theory behind the WHY of corporate governance is information asymmetry, or the fact that insiders (the founders and managers) generally know more about the company's value, potential and risks than outsiders (the shareholders and regulators). This gap in knowledge about the firm is a double-edged sword. On the one hand, that's exactly why shareholders entrust their money to managers, because managers know more about the business. On the other hand, this gap in knowledge can lead to three kinds of costs. First, "information cost" arises from poor (or fraudulent) disclosure of a firm's structure and performance by management. Consequently, this leads to higher risk perception by investors and higher funding costs for the firm. Other costs that can arise from information asymmetry are "mispricing cost", especially when firms go public, and "management cost", which occurs when managers interested in protecting their jobs employ anti-takeover provisions that are value-destroying. Finally, related to management cost is the practice of "self-dealing"—which is somewhat common in Asia—when firms engage in related-party transactions that could result in management selling goods or assets at below market prices to other firms owned by or related to management.

The bottom-line value

But so what? What does this mean to investors who want to see their stock rise in value? What does this mean to managers who seek lower costs and better performance for their firms? What does this mean to regulators who strive for strong and sustainable economies that provide fair opportunities for all? What's in it for them? Why should investors, managers and policymakers care about good corporate governance? To start, good corporate governance minimises the costs laid out in the theories we've just mentioned. And so the logic is that if these costs are reduced, the firm's bottom-line—its shareholder value—should increase. So does it?

Absolutely.

In the last two years, numerous studies clearly demonstrate that companies are more valuable when they are well governed. From McKinsey and CLSA to the S&P 500 and the World Bank, the data shows clear evidence that good governance is rewarded with a higher market valuation. Let me provide some examples.

From 2000 to 2002, the global consultancy McKinsey analysed almost 200 emerging market firms, scoring them along 15 metrics of corporate governance. What it found was that firms with higher scores enjoy a valuation premium of up to 30%. Interestingly, the force behind much of this premium came from institutional investors who are the leaders in recognising the bottom-line value of good corporate governance. Moreover, for companies improving from the worst to best in any of the 15 governance metrics, they enjoyed a 10% to 12% premium gain in their stock price. Finally, well-governed companies are found to be relatively more competitive. The McKinsey study showed that firms with higher corporate governance practices beat their respective local market indices by at least 20%.

In another detailed study conducted in 2001, S&P 500 joined with McKinsey to look at 90% of the firms in the S&P 500 index. These firms, with available data, showed a consistent relationship between corporate governance and performance. For example, well-governed firms consistently demonstrated (i) higher market-to-book ratios, (ii) higher return on capital employed, and (iii) lower stock volatility. And of particular relevance to us in Asia, when the same methodology was applied to 216 Asian companies, the researchers found an even "clearer correlation" for these premiums.

Another 2001 study done by CLSA, an equity research house specialising in Asia, arrived at similar conclusions. CLSA surveyed 495 companies in 25 emerging markets and found a 54% price-to-book premium for firms in the top quartile with regard to their corporate governance score. Interestingly, bottom quartile firms saw a reduction of 43% in their price-to-book ratio.

In short, corporate governance delivers real value. As more of these studies are conducted, as more findings are publicised, and as more investors are aware of the strong connection between value and corporate governance, the market will demand managers to comply. As a result, firms will become more efficient, investors will attain better share value, regulators will gain an ally in the market to monitor, enforce and enhance corporate governance regimes, and the general economy will benefit as a whole.

The opposite scenario is that the corporate weakness of one or two companies is likely to adversely affect market perceptions of other companies, and the loss of confidence may amplify excessively and have repercussions for the entire sector or even the entire economy. Thus the overall social costs could be devastating.

How to implement good corporate governance?

So far I have emphasised the rationale and incentives behind adopting good corporate governance. The logical next step is to tackle the implementation issues—the HOW question. Needless to say, the remaining few minutes won't do justice to such a vast topic. But let me try and share a few observations, specifically about the difference between "needing" and "wanting" good corporate governance.

The OECD begins its definition of corporate governance as "the system by which business corporations are directed and controlled". For some of us involved in public policy, especially here in Asia, the words "directed" and "controlled" oftentimes point toward a natural role for government. In the emerging markets of Asia, where market forces are not yet mature, the role of government is vital in establishing the rule of law, a level playing field, and even economic direction. So with corporate governance, governments also need to take the lead in drafting proper regulations, setting up monitoring and enforcement authorities, and guiding market participants towards adoption of such practices.

But at the risk of sounding controversial, let me also emphasise that the role of government, while necessary, is not sufficient to effectively implement good corporate governance in the market. Effective implementation requires the market to want it too. Yes, the role of government is crucial in setting up the system and guarding it around the edges. However, at the core of an efficient market—whether that efficiency is in production, pricing or proper governance—the participants must take charge. Investors, managers and other stakeholders must balance their relationships themselves. In the US, with the recent corporate governance scandals, we see the immense power of institutional investors—the CalPERS, Buffets and Templetons—to monitor and enforce good governance. We also see retail investors being more active through forming associations and initiating litigation. Yes, regulators like Eliot Spitzer are vital in keeping management on their toes. But at the end of the day, for every one officer in the SEC or Ministry of Finance, there are thousands of investors, both large and small, that constitute a wider resource base for gathering information, monitoring investments, and, if needed, blowing the whistle on violators.

The current challenge in Asia is to develop this strong investor base in tandem with the economic growth of our region. Let me give you some comparative numbers, using China and the US as a basis of comparison:

- In the US, institutional investors account for over 60% of US stock market capitalisation while in China it is less than 10%;

- In the US, retail investors account for almost 40% of market cap, while in China all of the "tradeable shares" available to small investors account for only 35% of market cap. Moreover, shareholder activism in the US, as measured by M&A transactions and shareholder lawsuits, is exponentially higher than in China;

- In the US, the government is almost non-existent as an investor in the stock market, while the Chinese government owns about 37% of market cap. This is an interesting point since on the one hand the Chinese government is technically the largest institutional investor in China and, therefore, should have a natural role in pushing for corporate governance. But on the other hand, many of the firms in which the government holds shares remain significantly owned by the government itself. Guarding against this potential conflict of interest is important to ensure market confidence.

Obviously, there can't be a cookie-cutter approach in implementing corporate governance in Asia.

ADB's role in promoting good corporate governance in Asia

At the Asian Development Bank, good corporate governance is an integral part of our core values. The ADB actively pursues and encourages good corporate governance in all aspects of our business endeavours within our Developing Member Countries. In all ADB loans and investments there is a strong element of good governance requirements. At the operational level, in our role as creditor and investor, we work closely with regulators, state-owned enterprises and particularly private businesses to emphasise and help implement good governance practices. We strongly prefer to invest only in companies that are committed to sound corporate governance as role models.

Our support for corporate governance began in the pre-Asian crisis era in 1994 when ADB formed a partnership with CalPERS to eventually establish a US$252m private equity fund for Asia through Lombard Asian Private Investment Company. In 2001, ADB continued its partnership with CalPERS and established the Thai Equity Fund with the International Finance Corporation. This year, ADB forged a relationship with Hermes Pensions Management of the UK, one of the largest pension fund managers in the world, resulting in a recent joint publication: "Corporate Governance Principles for Business Enterprises." This publication and other documents highlighting our commitment and work in this area can be accessed from our website.

Conclusion

In conclusion, I'd like to leave you with this thought:

In post-1997 Asia and post-Enron America, the focus on corporate governance has emphasised what I would call the "medicinal" requirements for the system. We have taken a very clinical approach to drafting the parts and pieces that define good corporate governance: composition of boards, roles of committees, disclosure and accounting guidelines, listing requirements, protection of minority shareholders, etc. And as these parts were designed, it was simply assumed that people would automatically accept this need, and acceptance would lead to implementation.

In this manner, corporate governance has been perceived as a medicine rather than a vitamin. What do I mean by this? Let me put it this way: you take medicines to cure a sickness, but you take vitamins to grow stronger. You take medicine because you need to, but you take vitamins because you want to. This difference in motivation may be semantic but I think it offers a crucial key in the effective implementation of good corporate governance practices, especially in the context of Asian emerging markets.

In other words, academics have outlined the reasons to convince us of what we should do, and regulators are drafting the laws to enforce what we need to do. But, in the end, it's the market that will provide the right incentives to motivate us toward what we want to do. And in the end, it's the doing that matters most.

Session 1: Asia Progress Report

Moderator:

Jinwon Park
Senior Foreign Legal Consultant, Shin & Kim, Seoul

Corporate governance in Korea is no longer the rubber-stamping exercise it once was, says Jinwon Park. But it will take some time for substance to replace form.

I would like to start, and hopefully break the ice of this session, by sharing my first experience as an independent director in Korea. It was 1997. As you recall that was Asian Crisis time. It hit very hard in my country, Korea. I was invited to sit on the board of one of the 30 largest business groups in Korea, (a chaebol). I accepted the job and voilà, the first directors' meeting took place. I didn't know what was to be discussed, but I went to the board meeting anyway. The board meeting took place in a huge room, almost half this size, containing only eight people. It was my first visit to the company, my first board meeting and there were seven people other than myself sitting at the board table. The chairman walked in very solemnly. Everyone stood up, but I did not. Then the chairman declared the meeting was in session. The president was working for the chairman, who, by the way, was also the owner.

The agenda was about a proposed spin-off of a subsidiary owned jointly by the group and a foreign investor. Then the CEO explained the reasons: why this spin-off was being proposed; in what fashion; the basic terms and conditions of the sell-off, and so on. After the proposal was read out the chairman said, "Does anyone have any questions or comments?" Everyone turned and looked at me, meaning you are the only guy who has anything to say. I was the only one who asked questions and discussed the issues and rationale; the pricing; how to use the proceeds of this spin-off, and so on. After 15 minutes of discussion the meeting ended. Everyone else was very quiet. Then the chairman said; "Now we need to sign this resolution". And the CEO called out and said, "Miss Choi, please bring the chops." In Korea, everyone uses chops instead of a personal signature to sign an important document. It turned out every director had a chop that was kept by the chairman's personal secretary, Miss Choi, and she walked in with a box full of them! Of course, I had brought my own chop, so I was the only one to pull it out and sign off the document. That was my second surprise. After the meeting was over the chairman invited me to take tea in his office. I went there and he said, "Mr Park, what did you think of the meeting? Didn't it go well?" So, I replied, "I think it went very well, Mr Chairman." And he said, "You know, this is the first actual board meeting we have had in the 37 years of our company history." That was the state of affairs of corporate governance in Korea in 1997!

Since that time a change has taken place in Korea, as well as in other nations, in corporate governance.

What is corporate governance? It is about dividing the power and authority among shareholders, the board of directors, and the executive body of a company. It also means the board is responsible for people outside the corporation, such as minority shareholders, regulators, consumers, employees, labour and so on. It is a power relationship defining the management and conduct of the corporation. Two principles: accountability of the board and executive body; and then to ensure that accountability is shared among all the relevant parties, that there is transparency and sharing of information in a very fair and accurate manner.

Korea has seen many changes in this regard. The laws have been changed. New regulations have been put in place requiring independent directors in large-scale or listed companies. A lot of things have been made easier. For example, derivative lawsuits have become easier to file and also class action is being considered as a more powerful enforcement tool to promote corporate governance.

But still there are many things to be done. I think the changes in laws, regulations, institutions are basically a matter of form. The question we have to think about today, from our first session to our last, will be whether there been a real and substantive change in corporate governance in Asia? Are these changes acceptable to investors? Are there true and important material changes empowering the board of directors itself, especially the independent directors? Majority shareholders have enough say, or leverage, in the conduct of a board and executive body, but what about minority shareholders? Has enforcement been strong enough to ensure that rules and regulations are meaningfully applied? We also have to think about whether there has been enough education and training to ensure a sufficient number of qualified independent directors when the larger corporations need to mobilise them.

Session 1 Speakers:

Ko-Yung Tung
Senior Partner, O'Melveny & Myers, New York

Ko-Yung Tung warns against Asia simplistically adopting standards of corporate governance from other parts of the world. "Emulation is good, but imitation has its dangers."

I have spent the last four years or so at the World Bank. I would like to use that perspective and experience to share with you some of the issues arising in the context of corporate governance in Asia. One of the main things that I did at the World Bank was to promote the rule of law. In my definition of the rule of law, corporate governance plays a very important part. As Mr Park said, the definition of corporate governance, the one used by the OECD, is the system by which business corporations are directed and controlled, and it obviously has many implications rather than just within the four corners of a corporation.

To talk about corporate governance in Asia is interesting because, seen from Washington and New York, it is either the brightest corner of the earth or the darkest. It is never in-between. We had all this publicity about the Asian miracle—remember Japan as number one, eclipsing the United States, and the tigers taking over the whole world? Everybody was supposed to be imitating the Confucian method of doing business.

Then we had the financial crisis in Asia and, of course, the region was put in the doghouse. It turned out to be a paper tiger, they said. Many people said that the failure of Asian economies had to do with a lack of one thing or another and, depending on whom you read, a lack of corporate governance was one of the reasons for their downfall. Well, I take a sort of middle ground. I'm a pretty grey fellow, so it's neither black nor white. We have done well in Asia, but we haven't done that well either.

The World Bank has basically two missions. One is economic development. That is, growth in the member countries. There are 184 countries and almost all Asian countries are members, except for North Korea. The other is poverty alleviation. There is no doubt in anybody's mind, I think, that economic growth is a key driver for poverty alleviation. That's the tide that will hopefully bring up the little boats and get many people out of poverty. The World Bank and the international community pledged in the year 2000 to a set of "millennium development goals". This plan has many ambitious goals, but the key point is to take approximately 3 billion people (that is half the world's population) who live under US$2 a day, and within that about 1.2 billion people who live under US$1 a day, and to halve that number by the year 2015. That is only 12 years from now. This is a big task and I think private enterprises have a significant role to play in achieving this goal. The way I see it is that there are two basic partners, the public sector and the private sector. So far there has been a dichotomy of analysis and prescriptions regarding governance and transparency. The public sector—that means governments, regulators, and supervisory agencies—has an enormous role, particularly in many countries of Asia. And, of course, the private sector does too.

Many people—this includes many of my former colleagues at the World Bank—take the Western definition of corporate governance as gospel. And there is a lot to be learned. But I have brought with me the New York Times of the day that I left, so it is a random choice. The front page of the business section had the following articles: one on Enron and its repercussions; one about the Tyco scandal where the CEO had an extravagant birthday party for his wife, I think in Corsica; a story on WorldCom; and another about the New York Stock Exchange, a watchdog not watching over itself. This was just an ordinary day in corporate America. One has to wonder whether or not something is wrong there too. And there has been a lot of attention on Sarbanes-Oxley, which is a by-product of the Enron implosion.

Now many jurisdictions in this area are looking at Sarbanes-Oxley, called SOX—not to be confused with the Red Socks!—and looking for guidance. I, frankly, think that SOX and its prescriptions are maybe too US-centric and not Asia-specific enough to adopt. Asia has two specific characteristics that are not dominant in the United States. One is ownership. In China, the majority of companies are controlled by the government. In other areas of Asia they are family controlled. Now, that means that the normal US dichotomy between the separation of ownership and management starts to have different dimensions. For example, in China, it may not be the mission of a state enterprise to maximise profitability. The state may have public interests, such as employment, environment, or other issues, which may not be consistent with maximisation of profit. Therefore, this will play out differently from the pure commercial enterprises envisaged by Sarbanes-Oxley.

Similarly in family-owned companies, there is often little difference between ownership and management—the family may control everything and there is a close identity between the two sides (which in US companies would be separated). Again, you have to think about how you deal with these issues.

Lastly, there is the role of so-called gatekeepers. John Coffee, a well-known law professor at Columbia University, recently wrote an article saying that the Enron situation was not a failure of corporate governance, it was a failure by the gatekeepers: auditors, accountants, stock analysts, bond rating agencies and, lastly, lawyers. In essence, the gatekeepers were asleep at the gate. In many parts of Asia, the role of these gatekeepers is very different. Their power is different, their capabilities are different, what they can do is different.

I just want to finish by saying a couple of things. Emulation is good, but imitation has its dangers. We must be careful about learning lessons from American examples, American prescriptions. We should be concentrating on principles rather than specific prescriptions. And we must always think about the role of the public sector, because it plays a much more important role in this region in corporate governance than does its counterpart in the mature corporate economies of the US and Great Britain.

Lalita Gupte
Joint Managing Director, ICICI Bank, Mumbai, India

Lalita Gupte recounts ICICI Bank's painful yet life-saving transformation from a single-product Indian development bank to a successful commercial bank following global best practices in corporate governance.

What I am going to talk about is not the general issue of corporate governance, because I think there are many more eminent speakers who can talk on that. I am going to speak about the issues that we, as a bank, faced in our transformation from a development bank—a single-product company—to the largest private-sector financial institution in India. It has been a struggle for six hard years. If I sound passionate about it, please excuse me, because I have been part of this journey.

Six years ago we were faced with a situation where we realised that problems were in front of us. If we remained a development bank, the writing was on the wall. We would not be in existence a decade later. No single-product bank would be able to survive a competitive and globalising market. We had to set ourselves a very clear path. The way we chose was to go against what the rest of the industry was doing and to say that we would not survive if we remained in the mode we were in.

It meant telling the world, telling the banking industry, telling everybody in India that the future, as we saw it, was not bright unless we changed. So we had to take a series of steps, which meant bringing in best governance practices at the board level before they became the industry hallmark. We were very scared about disclosing information and giving details that were not disclosed by anybody else in the system. A lot of people called us foolish because we were entrepreneurial, but I think all of them forgave us on one fact—that we were passionate about our organisation and passionate about not only surviving, but being the best in the system. We also knew that global competition was in front of us. India was opening up, inviting everybody from the financial system worldwide to come in, while the rest of the world was putting up garden walls and making it difficult for international banks to enter.

Yet we knew that international competition would eat us up in less than two years. In hindsight, it was probably the best thing we did. We brought in McKinsey, KPMG, and a lot of advisers. We told them, "Don't give us any reports. We just want you to guide us through and help us implement." What I am going to talk about in the next five minutes is our journey over the last six years.

When we set up audit and other governance committees, this was new. It was new, not just for us, but all over the world. We had taken a path to become a commercial bank. We already had a subsidiary that was a bank. It was clear that we had to merge at some point. Yet we had to be in line with government policy. So we brought in all the best practices. We were also clear that in the next few years we would have to diversify our portfolio to make it less risky. We would be going into retail finance, of which we knew nothing. Most people in the system thought we were mad! They said, "How can you, from being a corporate bank, become a retail bank?" We were only known as a development bank. Yet today we are number one or two among financial services brands in India.

The journey has been difficult. We had to learn first what the market wanted, what investors wanted. Then we had not just to do it, but to communicate it. We clearly had to communicate that there would be a transition period when non-performing assets would increase. We would have to restructure loans, disclose more information, and then there would be light at the end of the day. There were days when we asked was it all worth it? Was it worth being the first in the system to do all of this, take all the pain? And then, where was the light? But six years later, we realise that we are benchmarked differently. We were the first bank from India to be listed on the New York Stock Exchange, along with the parent and the subsidiary. We are one of the few who have pierced the sovereign ceiling. And while I disagree that India is not rated as investment grade, we are a notch higher.

The path has also been extremely difficult because when we first started we did a series of ADRs[1] and GDRs[2], and there were young 23-year-old analysts, who had been in business only two or three years, saying to us, who had been in business 25 years: "You don't know how to run your business. Why aren't you disclosing more about the steel companies? Why are the NPLs[3] so high in India? What makes you think you have the gumption to think you can go from being a development bank to a retail bank?" We had already said we wanted to be in the top three in the business. Any business we go into, we want to be in the first three. We want to be the best or we will get out. "What makes you think that you have the gumption to stand in front of us and tell us this, when you have no proven track record?" Fortunately, we were all so passionate that we said, "Let's make sure that we succeed."

It is easy to talk about this. It is difficult to do it. As we had no stake in our company, some people would say that since you do not own the company it will be easy, because you are not going to lose anything at the end of the day. Yes, but we all would have been without jobs. I think that was incentive enough.

We decided that governance went beyond legal and regulatory requirements. It meant a series of voluntary practices that aimed at a high level of business ethics, transparency and

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[1] American Depository Receipts
[2] Global Depository Receipts
[3] Non-performing loans

enhancing value for all stakeholders, including our employees. And that's what we did. We put in everything that was required in terms of board committees, whistleblower policies, subsidiary company data and disclosure of business risks. We clearly articulated our values and ensured that the board was eminent. And board committees were chaired by independent people of real substance.

The other thing we tried to do was impress this message upon on our clients. It was not sufficient just to adopt best practices ourselves. We had to deal with an India that was emerging, which felt it was better to hide things. I mean the whole of corporate India. Many companies felt they needed to hide things so that we as a bank wouldn't be tough on them. We were faced with a situation where, if all our customers disclosed their true performance, many of our accounts would become non-performing and we would take a hit on our bottom line. And this was during a period when we had to manage our own transition. As for our clients, we had to closely monitor what they were doing. We had to have discussions with them, while trying to restructure their assets. We found it was easier to talk to clients once we declared them non-performing. Until that point if we tried to tell them anything they would say, "But you are not disclosing that my account is non-performing. So you are not really meeting the standards of governance yourself."

We then had to go through the pain of taking a hit on our balance sheet. After that, we found it much easier to deal with our clients on an equal basis. Much easier to say, "Yes, we have to improve our own governance by declaring this as non-performing and, hey, you also need to do a series of actions." No matter what the laws said, or what regulations said, one had to instil in these companies that good governance was also good business. For Indian companies the writing was on the wall—unless they internationalised their operations and brought in best practices, they were not going to be able to meet international competition.

We took these decisions while business associations like the Bombay Club and other people said we wouldn't be competitive. But six years later, our customers are the guys who are the most competitive and are now creating the beginnings of Indian multinational companies, setting up manufacturing bases in Indonesia, China and the United States. Over a period, it became clear that unless you disclose, unless you bring in best practices, you will not survive, you will not do well and you will not enhance your value to shareholders. This is true whether it is a family or state-owned company. We have excellent examples of good families—there are a lot of young second-generation entrepreneurs who have been educated overseas, who have seen best practices—driving their companies towards best standards. Yet we also have many publicly listed companies who don't bring in high standards of governance.

We found too that in communicating with our employees and stakeholders we had to be equally honest and transparent about the task that lay in front of us, about the difficulties we faced as employers, and what we expected of our employees. We told them that there would be a lot of sacrifice—you probably won't get bonuses for two years. We also had to be clear in our dealings with government and impress upon officials that this was essential. What we did was make sure that our best practices became industry norms. We worked with the Securities and Exchange Board of India, the Company Law Board, and with several institutions to create what today are amongst the best practices in the banking sector. That has been an important part of our governance.

I think one of the things we have learned is that it is very easy to say—and take refuge behind saying—that the laws in the UK, the US and Singapore are very tough. But if you want to be an international bank, as we have set our path to be, you have to be regulatory compliant. You have to follow best practices, even if it means complying with ridiculous things like the prohibition of home loans to directors under the Sarbanes-Oxley Act. After all, we are the largest provider of home loans in India!

You know there is a period of transition. We went through a phase when the market price of our stock on the NYSE fell about 50% and it took perhaps three years to get back to a level above the issue price. But we realised that if we wanted to borrow from the international markets—and the same is true for all of Indian industry—we had to make sure that we actually qualified for the best standards.

I don't want to talk any more. The idea was not to lecture, but to share the pain of an institution that has gone through a series of transformations in the last five to six years. And we are going through another series of transformations as we try to achieve regulatory compliance in some eight overseas jurisdictions that we have chosen to set up offices in. Thank you very much.

Vincent Duhamel
Senior Principal and Chief Executive, State Street Global Advisors Asia, Hong Kong

Vincent Duhamel links the recent rise of corporate governance in Asia to fundamental capital-market and pension reforms. In a concise regional overview, he also questions Hong Kong's approach to corporate governance.

We manage close to a trillion US dollars for approximately 3,000 clients and have investments in about 8,000 companies, a fair number of them here in Asia. As an investor, we are about as close as you can get in terms of the tyre hitting the road.

Here in Asia, corporate governance issues face their own set of challenges. I would like to focus on the progress that has been made throughout the region, while offering some comments on reforms, in China in particular. As governments, multinational firms and domestic companies all grapple with the best approach to this set of issues, there is one thing we must all remember: Good corporate governance is good risk management.

Three trends

Good governance arises from and supports three significant global trends—two very important ones and one that has just appeared over the last six months. The first is capital market development. The second is pension reform. And the third is what I would call the "Kozlowski trend". The experience of Asia—especially China—in the 1990s has mirrored these trends, which have been nurtured by the simultaneous and parallel efforts of governments and business to create greater transparency on a variety of levels. I believe in the last five years Asian managers have become much more aware that improved corporate governance and operational transparency work in their favour. Adopting such an approach can fulfil investor expectations, improve confidence in both management and the corporations themselves and, in turn, increase the valuation of stocks. Improved stock prices, as many of us know, are particularly important to firms aiming to attract capital from international markets. And as this region globalises and plays in the international capital market, the cost of capital basically becomes cheaper. At the same time, Asian governments and regulators are putting pressure on companies to raise the quality of corporate governance and information disclosure focusing on the transparency of financial conditions, operations and management activities.

I was interested and amused to hear Lalita's comments about young research analysts. Yes, these are young research analysts that we send out. The fund managers tend to be a bit older and then, once you are past your due date as a fund manager, you become a business manager. Yes, we don't always know what we are talking about, but at least in the ICICI case management got involved with the fund managers. This is one area of progress that we are finally starting to see in Asia.

On the pension reform side, corporate board members, pension fund sponsors, trustees and fund managers have a fiduciary duty to uphold, and that duty has been increased over the last five or six years. Six years ago we never heard any trustees, or any clients among the 3,000 that we have, mentioning or having issues regarding corporate governance. It is now a major issue being discussed at every portfolio review that we have. So, while charged with adding value to our clients' wealth, each of us is bound by loyalty to protect their interests in the companies in which we invest.

This is particularly true and relevant for passive buy-and-hold (or index) managers, who do not have the flexibility to influence corporate management by simply selling their shares. In fact, given the magnitude of institutional investments—the equivalent in some countries of up to 90% of GDP, representing millions of investors, pensioners and savers—the potential influence and power that these investors can yield over the management of the corporations in which they own shares should be staggering.

Over the last few years there have been some positive changes in corporate governance in parts of Asia and I believe they are starting to make a difference. We are seeing substantive and real changes in corporate governance in Asia. Our major concern now is whether these changes will stay in place now that stock markets are becoming attractive again?

The third thing I would like to talk about quickly is the "Kozlowski trend". I am convinced that the picture we saw in the Wall Street Journal, the Financial Times, the National Inquirer, the New York Times, of Dennis Kozlowski going into court about two or three weeks ago will have a powerful effect on corporate leaders around the world. I think nobody in Asia, no chief executive officer, would want to see his face in the newspapers like this. Sarbanes-Oxley was a reaction of politicians to a situation. I think the pictures that we have seen of a number of executives going to court will be a catalyst for making sure that corporate governance gets implemented around the world.

Regional round-up

In **Korea** we have seen some interesting improvements and I have to say that corporate Korea has made some amazing progress over the last five or six years. The main one is dialogue with institutional investors. I believe the situation Mr Park addressed this morning about board meetings is probably still happening, but there are some good examples of companies that have tried to engage and improve their act. I am thinking here of Samsung Electronics, which three or four years ago was put in the doghouse of bad governance. I am thinking also of SK Telecom, whose board of directors recently decided not to support a bailout of an associated company. We do still have difficulties in Korea, such as in mobilising proxy votes, but that is often more of a logistical problem.

Taiwan: Transparency has improved in some sectors, especially the technology sector. Financials need to be worked on quite a lot. Transparency concerns also arise in the China operations of many companies, as it is never really very clear what they are doing. And the one-man show that you tend to have in Taiwan companies, because of family control, does not help corporate governance.

Singapore: Corporate governance has never been a major issue there, although transparency, especially of the government-linked companies, has improved tremendously and management has had to become much more accessible to us.

Malaysia has seen enormous improvement in terms of its code on corporate governance and listing requirements. We have even seen some people, such as directors, going to jail, which is always a good sign and sets an example for other companies.

Let me discuss something closer to home, Hong Kong. **Hong Kong** has probably been, I would say, one of the best environments for corporate governance in Asia. Five years ago I remember a CLSA conference that had a session on corporate governance, with Narayana Murthy of Infosys, a star corporate governance advocate, and myself presenting. Only about two people showed up, and I suspect one of them was in the wrong room! At that point in time, frankly, we were presenting more of a defensive mechanism, because we had just launched the Tracker Fund in Hong Kong, which made us the second, third or fourth largest shareholder in the 33 largest companies in Hong Kong. Nobody wanted to talk to us. Even if we tried to call the company they would say, "No, we don't want to talk to you guys. You are just a bunch of 30-year-old fund managers out of Boston, you don't know what you are talking about." The problem we had was that we represented the interests of hundreds of thousands of shareholders in Hong Kong and, frankly, my major concern was being put on the front page of the Apple Daily saying that the Hong Kong Tracker Fund was being stolen from by some of the tycoons here in Hong Kong. We thought at the time that the best road to take was to be proactive and clear about the things that we would not tolerate (one of them being stealing from minority shareholders).

This came as a surprise to a number of companies here and they are starting to engage. This shows that Hong Kong, despite having one of the most established rule-of-law systems in Asia, is still a little slow and complacent about adopting new standards of corporate governance. It is not an issue of being bad. It is that the standards have changed in Asia and around the world and Hong Kong companies need to address that quickly. A few corporate actions have been defeated at shareholder meetings where companies thought that the minority shareholders would just roll over, thank you very much, and head straight for the buffet. We didn't go for the buffet, but we did vote our shares and a number of management initiatives have been defeated. That has come as a surprise to several companies, and it will probably continue. Now we are seeing a bit more discipline and companies are starting to realise that, if they want to participate with global financial players, they will have to engage them. And they will have to do things in the best interests of all shareholders, not just controlling shareholders.

One area that is always quite surprising in Hong Kong is quarterly reporting. We still hear some big companies saying that it is too difficult. Not true. The timing of reporting still takes more than 60 or 70 days for some companies. I can't believe that Citibank, which has operations in a hundred countries, can produce its quarterly earnings in 16 days and yet a small company that produces plastic, or whatever, cannot produce its results in 60 days. This is clearly an unacceptable level for a market like Hong Kong.

Then they come up with the issue about the cost of quarterly reporting. Again not true. If the chairman of HSBC or the chairmen of any of the large conglomerates here does not know on a weekly basis their company's sales and margins, and what is happening within their companies, I would be very surprised. They could do quarterly reporting pretty quickly. They talk about being concerned about kidnapping. Well, this is the city that, after London, has probably more Rolls Royces than anywhere in the world! If I was concerned about kidnapping, I wouldn't be walking the streets or going around in a Rolls Royce in Central.

Now, about **China.** It is a country that basically has two major reforms happening at the same time—capital market reforms and pension fund reforms. Companies in China need to raise capital in the financial markets and the government needs to address a host of social economic challenges. Corporate governance is right in the middle of this. We believe that there have been some great improvements in China in terms of regulation. They have been talking the talk. Now it is a question of convincing global investors that they can walk the walk over the long term.

There have been improvements. I remember the first IPO[4] I participated in in Hong Kong was Tsingtao Brewery in 1993/94. In the first earnings that Tsingtao was to report, they came out and said, "Well, we don't want to report them, we don't like them. Let us work on them a little more." Tsingtao is now one of the best China companies listed in Hong Kong. You have companies—China Mobile, Petrochina—that are way up there on a par with best global practices. So we have seen some major improvements. There are still some things that need to be worked on. Investment protection laws need to be better established. State ownership needs to be reduced. Yes, it is true, Asia is still in a state of development. But again, if China wants to tap into international capital markets, it will have to change. And there is a need to fund other social economic challenges that exist out there, such as pension systems.

The pension system will change. You are going to have millions and millions of shareholders as opposed to having one major group of shareholders (that is, the government). Transparency of the markets needs to be improved. The quality of management needs to be worked on, and so too boards of directors. The China Securities Regulatory Commission (CSRC) has established a school for directors, which is a great improvement, and put in place some pretty strict guidelines for directors. I will stop, because I suspect that we will have more questions on this, but this is a quick overview, from an investor's perspective, of some of the markets here in Asia. Thank you.

[4] Initial public offering

QUESTIONS & ANSWERS

Questions and comments from delegates covered the following issues:

- Public governance vs rent-seeking and corruption
- Implementing corporate governance in a corrupt market
- The fiduciary duties of all directors, including government appointees, to shareholders
- Avoiding corruption by not asking for favours from officials
- Governments in Asia—not usually model shareholders
- Improved governance among banks and other financial institutions
- Quarterly reporting—how can it stop deliberate dishonesty?

QUESTION: My question is for Mr Ko-yung Tung. I am very curious about the role of public governance and corporate governance—the quality of the government and the governance of the government—because we observe in many Asian countries that corruption and rent-seeking activities are quite pervasive. Firms adapt to their environment. Some have to make a profit by dealing with government and keeping a low profile. Being opaque may be in the best interests of both the companies and even minority investors (in some markets). Realising that, it is not surprising to see, despite all the reform in the bigger system and improvement in transparency, that in reality if you live in a rent-seeking society you simply cannot afford to disclose too much. It may even be against the interests of the minority shareholders if that is the way the company makes a profit. So I wonder if you have any opinion, especially from a World Bank perspective?

KO-YUNG TUNG: Those are very good questions. First, I think that when a major shareholder is a government and has a representative on the board, it has unique issues to confront. I was thinking the other day that if I were appointed by my government to be on a board of a partially state-owned company, how would I vote? Am I really independent? Should I exercise my independent judgement or am I taking instructions from the authorities? If I want to represent the interests of the shareholder that appointed me, what are those interests? I may think that maximisation of profit may not be exactly what my shareholder, the government, wants. Its interest may be more to protect employment. It may be that I want to have more pollution control equipment installed rather than maximisation of profit. This raises a host of issues and I don't have an easy answer.

In terms of corruption and rent-seeking, obviously that is a bad thing. Having said that, I want to raise a couple of issues just to be somewhat controversial. I think Lalita said good corporate governance was good business, and Vincent said good governance was good risk management. The professor who asked the question raises another issue: sometimes, from a purely economic view, corrupting an official may be best for maximising profits for your shareholders. Being a good citizen may not be best for maximisation of shareholder value. Therefore when we talk about maximisation of shareholder value and the like, we ought to think about what are the other incentives? What are the other disincentives? The impact of seeing yourself on the front page of the Financial Times in handcuffs is a real disincentive. Again, we need rules, we need laws, and we need very strict enforcement.

JINWON PARK: I think that corruption and corporate governance in the public sector, or publicly-owned companies, is basically related to enforcement. The Kozlowski impact, as Vincent mentioned, can be one of the deterrents. But we also need to also think about alternatives to this deterrence measure. One is private lawsuits—enhancing or making it easy for shareholder actions in the form of derivative law suits and class actions. The other alternative would be criminal sanctions. In Korea, for example, the Financial Supervisory Commission has a wide range of measures to sanction, penalise in monetary terms, and prevent a body from engaging in future in the securities or banking industries. They have a variety of administrative sanctions, like taking away or suspending licences. Are administrative sanctions more effective than private actions such as class actions in having an impact on corporate governance? I think they should be. Korea has tried to ease derivative action rules and enhance the rights of minority shareholders by allowing inspection of records and making it easier to call for shareholder meetings. In a lot of senses, shareholder rights have been tremendously increased. But whether they are using it as an effective mechanism to protect their interests and values is not clear yet. In that sense the impact of the new legal regime has not been very effective yet, except for certain larger corporations such as SK Group, Samsung Corporation and a couple of banks (that were hit by huge derivative actions).

The other thing I would like to talk about is the family-owned company issue. There have been many studies suggesting that in the 1980s and early 1990s that the family-owned business might be desirable in the sense that it could engage in quick decision-making, easy risk-taking and so on. But we may be forgetting the basic fact that we are not talking here about 100%-owned family businesses. Recent statistics suggest that on average the top 30 Korean chaebols are only 7% owned by their "controlling" families. That means more than 90% of the investment has been made by non-controlling shareholders. That means that the families are using some high-leverage ownership structures to control 10-15 times their investment. That calls for more transparency and the proper protection of the other 90%.

QUESTION: I think the previous delegate raised a very important issue and I would like to direct this question to Lalita Gupte. When Lalita was trying to introduce best practices in her bank, it was not very transparent. Yet she did it and went through a painful transition. So I would not buy the notion that because the regulatory body, the government, is less than transparent we should somehow sit back and consider colluding with them. I would like Lalita to expand on how she implemented good governance in that kind of system?

LALITA GUPTE: I think we really had no choice. We were very clear that we wanted not just to survive but to be winners. In a way we had a board who, I think, gave us sufficient backing as management. We also had a set of international shareholders who said, "Yes, we might see a drop in your share value over a period." I think this is where you need long-term investors who believe in your story and who are willing to back management. Without that, I think it would have been impossible. But we had to be transparent right at the beginning and tell investors that they would see 'value through values'. You might see a drop in profitability, but fortunately that didn't happen except in one year. You have to keep communicating.

And, you know, I don't want to belittle those 23-year-old research analysts. They woke us up. They said, "You could have been in management for 20 years, but I call the shots. I decide whether I'm going to invest in you or someone else. And you are not being benchmarked with the best in your country.

You are being benchmarked with the best the world over." So it was an early warning signal.

Let me share another story. Those 23-year-olds—or maybe they were 26—were often people who had worked in the old ICICI and had in two has become an expert in everything. It was a double whammy, and your ego took a huge beating, because people you had recruited were telling you how to run your company. But I must tell you that they actually became our best friends. It was tough because a lot of people thought we were stupid, we were dumb. Why were we doing all this ahead of the pack? But here, five years later, everybody says, "Tell us your story." It does take three to four years, but at some point you get recognition.

Let me also talk about government and governance. I must say that the regulators in the last four years have been extremely proactive in setting up best standards. I don't think anybody has really gone to jail in corporate India, but that threat remains. Also we have a very powerful press. We are a vibrant democracy. Anybody can take pot-shots at you and you have to explain yourself.

Yet India remains high on the corruption list. We really have two Indias. We have a very rich India and a very poor India. We have a rich and poor India in the corporate governance sense too. We have state governments who are good at governance and others who are very poor. I think some of the states, particularly in the south, have done significantly better at being transparent. I am not saying they are non-corrupt. I don't want to give you the feeling that everything is hunky-dory in India. It cannot be when you have a billion people and a political system that is democratically elected and will move from being an emerging market to an emerged economy over the next 10 years. I think what Indian companies did in information technology—the government had nothing to do with their success or their transparency—taught everybody that you could be successful yet transparent. These guys had nothing to hide because they came from nowhere. They were not known in India five years or 10 years ago. In a way, the world recognised them before Indian stockholders did.

Some of the state governments are taking steps to bring the most corrupt areas of industry into transparency. For example, some are bringing land revenue records online. And there is a lot of public pressure because everybody talks about the heroes, the ones that are doing well. People have realised that you can now get re-elected if you are transparent.

Again, I don't want to paint a picture that we have achieved everything. We are a billion people and have 16 states, with 16 languages and millions of dialects and every religion under the sun. We are getting there, but it is a difficult task.

QUESTION: I refer to a comment that Mr Tung just made, a hypothetical, that if he were appointed to the board of a partially government-owned enterprise, on certain issues he would have difficulty voting. But isn't the issue clear that once the government, or family, as Mr Park so well expressed, takes other people's money, then you have a fiduciary obligation? I think the game is different once you take other people's money. Why are property rights so ambiguous in Asia? This is a problem everywhere in the world, as we know, but in Asia it is just a little bit more ambiguous. The attitude towards other people's money is, I think, not very clear.

KO-YUNG TUNG: Let me first clarify what I said. What I was trying to do was to sympathise with the difficult position such a director could be put in. As you know, everybody is an individual. You have to know their fears, their hopes and what are their drivers. If you don't do what the government tells you, you may lose your living. The situation that a lot of people find themselves in Asia is very different from what we are used to in the West. You know, if we lose our job we can get another one. But in certain places if you lose your job you are out of your house, your kids are out of school. Obviously the principles that ought to be guiding these directors are clear—you have a fiduciary duty to all shareholders. But what I am trying to get at is that you have to build in the infrastructure and the incentives to make sure that the ultimate goals that you want to achieve are aligned. Where you have problems is not in the enunciation of good principles and practices. Those are pretty easy to recite. The question is how you actually implement them. Everybody knows that it is not a simple thing of saying "Amen". It is making sure not only that the religion is accepted, but also that everybody practises it. Therefore, making sure that the incentives are aligned to what you want to achieve is very important.

VINCENT DUHAMEL: I just want to make the point that in Asia—and I think this is one of the reasons why we are a little bit behind the curve compared to some other regions—we do not have a large equity culture. In a place like Hong Kong, only about 5-6% of the population invests in equities. There is a very high turnover, meaning that the people who are playing in the stock market are punters who couldn't care less about long-term investing. A lot of the family or government-owned businesses in Asia rely often on friends for support. This will change as countries, because of demographic pressures, put in place pension reforms that will create, hopefully, some anchor investors in the market. Investors that are domestic, that have long-term interests, that cannot sell every two days or so when they don't like something about a company, and will be invested in the market for five, 10 or 15 years.

These anchor investors would not represent the interests of another family or friends of the family. They would represent the interests of millions of investors. This I think will probably bring some changes and more respect for the rights of minority shareholders, because they will become more vocal, much more organised. They will have the resources to get organised.

COMMENT: This is a comment about rent-seeking. I live in Indonesia and I own my own business. I can't resist making a comment about this because, as you know, my country doesn't enjoy a great reputation for corporate governance. The way to avoid rent-seeking is to avoid asking for favours from government officials. A lot of the conglomerates are suffering from rent-seeking because they spend most of their time looking for favours from government officials, trying to advance the cause of their own business. But if you are independent and you don't collude with officials as part of your business model, you can avoid a lot of difficulties.

COMMENT: I would like to comment on government as a shareholder. While there are variations around the region, this is one area where I think significant improvement is necessary. Governments have not been and are not model shareholders. They do a very bad job of managing even the state's interest in partially privatised corporations. And not only that, in many cases the government representatives on boards have a chilling effect on the other directors, especially the independent directors on the board. There is a need for uniform and transparent government policies with respect to the government as a shareholder.

A second point, not related to government ownership, is that one of the most significant forces for corporate governance change has been the changing patterns of corporate finance and the changing patterns of corporate governance in financial institutions. The story of ICICI is not just an interesting and important story of corporate governance change in a particular corporation, but as a financial institution it has an impact on others, such as its customers, not only as a model but in terms of the credit that it provides. I think that has been an even more powerful force elsewhere within the region, where significant changes have come about in banks as a result of the financial crisis and the need to re-capitalise those institutions.

I think it is significant that in each of the markets among the outstanding examples of improved corporate governance are financial institutions that have changed their financial practices. Banks such as Shinsei Bank in Japan. Interestingly, in one of our earlier meetings, Good Morning Securities of Korea was highlighted as a financial institution that had significantly changed its corporate governance patterns, had an influence on its customers and had also been a model in its market in the same way as we have heard with respect to ICICI.

QUESTION: I want to take up a comment by Vincent on quarterly reporting. It tends to be seen as a cure-all, but surely a company that is hiding something every six months is going to hide something every three months? And you mentioned Enron and Tyco, etcetera. These are companies that reported every quarter and yet were still caught out. Surely it comes down to basic honesty and integrity? And a few of the speakers have mentioned the notion of a free press, the fear of being on the front page of Apple Daily or The India Times or the FT or whatever. Surely it is not how often you report, it is what you report that is important?

VINCENT DUHAMEL: Absolutely true. Quarterly reporting is not the cure of all the issues and the ills of companies. Quarterly reporting allows you to engage more often with management and makes it more difficult for companies to hide things. Basically, by meeting managers four times a year rather than twice, we are improving the probability of catching bad numbers and anything that doesn't add up by 100%. Now I know the next objection is going to be: "Well, but that becomes a very short-term type of approach." It probably is short term. But it depends on the individuals. It depends on the pressures that are put on the fund managers. I have to report to a number of my clients here in Hong Kong, such as corporate pension plans, on a quarterly basis. I am not the one driving that effort. The companies are. But then the same companies will come out and argue that, well, we don't need to do quarterly reporting, we are only going to do it on a six-monthly basis. So it's give and take on both sides. I think quarterly reporting allows you far better flexibility, better transparency and better opportunities to engage with management and discuss their numbers. There is also the question of how quickly you can report those numbers? The suspicion I have come to about Hong Kong, and why it takes so long is that the delay in reporting is caused by a massaging of the earnings—not among the best companies but a lot of the other companies. Everybody can figure out that if it takes 60 days to report the earnings of a company that has about US$100m of business, it is probably because the chairman didn't like the numbers and wanted to rework them a little. But at some point this comes out. If you have to do it on a quarterly basis, you won't be able to massage them that quickly.

Session 2: Shareowner Activism

Moderator:

Pote Videt
Managing Director, Private Equity (Thailand), Bangkok

Does aggressive, US-style shareholder activism work in Asia? Pote Videt argues that culture inevitably shapes activism and, in his experience, a subtler approach involving "preventive measures" can help to align the interests of minority and majority shareholders in this region.

I would like to set the stage with some comments both general and personal. My knowledge of corporate governance issues in the US is not state of the art. I joined Wall Street in the late 1970s, when there was a lot of talk of good governance and shareholder activism. But very little happened until a Texan with a tall idea and a strange name appeared on the scene. This occurred in the early 1980's and his name was T. Boone Pickens. He had a simple message for the board of directors of a US company: "Do something to increase my returns or you're out of a job." That was my first direct contact with shareholder activism. I believe this type of action sparked greater activism among US shareholders, turning the threat of removal into a powerful incentive for better corporate performance.

I've been in Asia since 1987 and have viewed corporate governance developments in the US from a distance. I've noted with interest many of the new rule-based concepts—such as structure of the board, disclosure, transparency and accountability. What we observe from halfway around the world is the US market's constructive evolution and the appearance of new issues and new actors on the stage of corporate governance.

I'd like to tell you about some corporate governance issues that we have faced in our part of the world. I run a US$250m private-equity fund for investments in Thailand. We have taken significant minority stakes in Thai companies and try to make a difference. In making such investments we often ask ourselves, "How do we adapt all these Western standards on good corporate governance in a different setting? How do we make them work in Asia?" So I pose the question: "Would the T. Boone Pickens approach work in Asia?"

Culture shapes activism

There are three points worth making. The first is cultural. To quote from a long-term resident of Thailand: "One of the most pervasive aspects of Thai culture is the avoidance of social confrontation. One is expected to mask one's emotions, particularly anger, hatred and annoyance. Social harmony must be preserved. Thus a friendly smile often hides dislike, disagreement, distrust. A less-than-frank reply is given to avoid offence, an indefinite postponement rather than an abrupt refusal. The *farang* (foreigner) prefers to be told face-to-face if someone disagrees with him, or is hurt or offended by his behaviour. To a Thai, such confrontation is socially unacceptable." Does that sound familiar? I am sure that these comments apply to more than one Asian country.

When we talk about shareholder activism, would a vocal, in-your-face shareholder like T. Boone Pickens work in Asian countries like

Thailand or Japan? We've tried a subtler type of shareholder activism, what I'd call "preventive measures", that basically tries to align interests for the long term.

I'd like to elaborate on some practical "preventive measures": one is ownership of shares. We made a long-term investment in a securities company, whose real assets are its people. In making the investment we said to senior management, "You have to commit to hold this percentage of shares within one year, this percentage within two years, this percentage within three years." A lock-in concept that aligns interests is something we believe in. We're in negotiations for a quasi-investment buyout of a manufacturing company. Again, it's the same concept—the company's senior management has to commit to hold over a period of several years. Interestingly, we thought there would be resistance from the management, but they had no objections. They are committed to the company for the long term, and that has given us a great deal of comfort. We are also a big promoter of ESOPs[5] , to ensure that employee interests are aligned with ours.

Another issue (and frankly involving a basic concept) is that we want upfront agreement on the definition of the business we are investing in. Every successful Asian businessman, whether in chemicals or steel, wants to own a five-star hotel. We want to make sure our investment does not end up going into that five-star hotel business. Defining the business and getting an agreement on the scope of the business is very important in Asia. We do this on a non-confrontational basis, as partners.

The third concept is being able to have a positive input on the quality of the board of directors. Obviously, since our investment stake is generally 10% and over, we want to be represented on the board, but we also ask for a say in the nomination of independent directors and, in some instances, the right of veto. We also offer to educate the board, by encouraging attendance at the Thai Institute of Directors' certification courses and, in some cases, offering to pay for it. So shareholder ownership agreements, scope of businesses, board direction and board composition are examples of actions that we, as an investor, take to align interests.

Family ownership—who is in charge?

My second quick point is about corporate governance and family ownership. I'm going to make a generalisation, but in our experience family ownership seems to have worked fairly well. The issue is not about family versus non-family ownership, it's whether there is a clear chain of command.

One case where it works is when only one family member is in charge. Then you can judge whether that person is capable or not. For example, we invested in the second largest tuna manufacturer in the world. The son was clearly in charge. We thought he was pretty capable, and in the last five years he's proven to be very capable. He's probably the best guy in the tuna business. He's strategically oriented, focussed and works hard.

At the other extreme, we invested in a company where family ownership was dispersed to well over 50 family shareholders, many in the third generation. In such a case, there was a desire and a greater incentive for the family shareholders to professionalise management and to maximise shareholder value over the long term, with less emphasis on roles and positions for family members.

[5] Employee share-ownership plans

Relying on integrity, not legality

The third and final point I'd like to make is about adapting western standards to Asia. To paraphrase an American expression: "When the going gets tough, the tough get going." In the US the tough go to court and it generally works out within a reasonable time frame, because there is confidence in the due process of law and the fact that you see people go to jail more often than in any other market. I'm not saying that Asian courts are not making good progress, but in our experience you can't rely on them as much as courts in the Western environment.

What does that mean? It means integrity is probably the most important issue, because in Asian legal systems unpredictable issues often arise that go against your interests. Issues like nationalism or delays—of perhaps years—to resolve a situation. What those delays mean in practical terms is that the operations and the assets can deteriorate in value over time. There are issues of local labour being utilised against your interests, and finally—one that isn't talked about very much—there's the issue of government intervention, which can negatively affect your rights.

So the fundamental issue is the issue of who you're investing with. Obviously we all do the checkings before we invest, but it is difficult to predict how people will act in times of crisis. When people are pushed, they will do extraordinary things that are difficult to predict. So we do look backwards often to analyse a track record over a long period of time, including times of crisis.

Session 2 Speakers:

Taiji Okusu[6]
Managing Director and Vice Chairman, UBS Warburg (Japan), Tokyo

Taiji Okusu gives a concise overview of the pros and cons of new corporate governance rules in Japan, then describes the country's nascent shareholder activism—in particular the maverick investor, Yoshiaki Murakami.

Over the next few minutes I would like to touch upon the recent changes in the Commercial Code, which affect corporate governance, and the current status of shareholder activism in Japan.

First, the Commercial Code changes that became effective in April 2003. Under those changes, a large company is allowed to either retain the "statutory auditor"[7] system or choose the new "company with committees" system. These committees consist of audit, nomination and compensation committees and, I am happy to say, are in accordance with the corporate governance principles of the OECD.

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[7] The "statutory auditor" system has been the traditional means for achieving a degree of accountability within Japanese company boards. Based loosely on the German supervisory board system, these auditors are supposed to supervise the management board. Widely viewed as ineffective in governance terms—partly because the auditors were often retired company executives—the system is undergoing some reform. A proportion of auditors must now be independent of the company and its management. (Editor)

Some characteristics of the changes include: the separation of executive directors from the board of directors; ensuring a majority of non-executive directors on each committee; and giving the board authority regarding profit distribution. It used to be the role of the shareholders' meeting to decide on profit distribution, but now it's in the hands of the board.

Another important change is that issues such as finance and investment are now under the authority of management as opposed to the board of directors. So in the new "company with committees" system, CEOs in a sense have greater powers. They can make quick, effective decisions without first obtaining board approval. Later on they will get this approval, but basically they can decide what to do on finance or investment matters. What are the implications? Why the choice? This is a compromise between the old and new systems. We still have a lot of resistance from the business circles: the Keidanren, which is a CEOs' federation, strongly opposes the changes.

Some 40 companies out of about 3,000 listed companies in Tokyo have so far adopted the new system. But if you look at the list of those 40, they are notable companies, including Sony, Hitachi and Toshiba. They are very active in terms of improving corporate governance. Although it's still early days, I believe this will become a good trend in Japan. I think institutional investors prefer the new system, because it's transparent and it also gives power to the shareholders.

But we should note that good governance is not an alternative to good strategy. Look at Sony. Although regarded as having the best corporate governance in Japan, its stock price is not doing well. Mr Nobuyuki Idei, Sony President, once stated that Sony was no longer a manufacturing company, but "in the Internet business". I think they made a mistake. Mr Idei has changed course and is now placing more emphasis on manufacturing. So I'm assuming that the Sony stock price will improve. But good governance does not necessarily translate into good strategies.

I see some issues arising in the Japanese Commercial Code changes. One is the shortage of qualified non-executive directors. It is a new phenomenon to appoint non-executive directors in big Japanese corporations. The board used to consist of old employees or directors appointed by parent companies and it's difficult to find good, qualified non-executive directors. I think many companies are adopting a wait-and-see attitude to finding the right non-executive directors.

A more important issue is the loose definition of "independent director". The only requirement under the Commercial Code is that the non-executive director is not an employee of that company. So a parent company can send directors to its subsidiaries and they can be regarded as independent directors!

Hitachi and Toshiba have adopted the new "company with committees" system, but we suspect this is designed to control their listed subsidiaries. Both have many affiliated listed companies and this is a good way to control them. It will be interesting to see how minority shareholders respond to this.

Another issue relates to holding companies adopting the new system. Since holding companies do not have many employees, we questioned how effective the change would be.

Nascent activism in Japan

I became a member of the Japan Corporate Governance Forum in 1995 and, from the beginning, was a believer in market discipline. We tried to improve corporate governance in

Japan from the legal and structural points of view, but that didn't work. My conclusion was that unless market discipline became tougher, managements would not change and would not listen to their shareholders. I advocate promoting hostile takeovers in Japan. And I'm ready to advise any companies who want to acquire other companies on a hostile basis. So I'm a little bit different from the normal Japanese!

In 1998 I advised Cable & Wireless on its acquisition of a Japanese telecommunications company, IDC. The management was opposed to the acquisition and wanted to sell to NT&T, the largest telecoms company in Japan, but Cable & Wireless successfully launched a hostile takeover. I was happy and proud to be the first to advise on such activity. But since then we have had only a few similar takeover attempts, and none successful.

Why is that? Well, Japanese banks and corporations are against these kinds of aggressive moves. In Japan, somebody who rocks the boat is isolated. Even foreign companies are concerned about such perceptions. When I talk to a foreign company who is interested in a Japanese company, but cannot get agreement from the management, I say, "Why don't you buy the companies on a hostile takeover basis?" But the answer is usually, "Oh no, this is Japan. We don't want to rock the boat".

I think now the situation is changing. For example, the Japan Pension Fund Association is becoming vocal about corporate governance. At this year's shareholder meetings, the Association cast votes against 43% of the companies in its portfolio and demanded that its fund managers do the same. It's very rare to see this kind of thing and Japanese institutional investors are still reluctant to take aggressive action. In the meantime, Japanese corporations are starting to approach institutional investors and explaining what they're doing, how they are investing. This is a good trend. The merit of corporate governance, in my eyes, is to increase the volume of funds from investors and reduce capital costs. This is in the interest of management.

One exceptional maverick, Mr Yoshiaki Murakami, President of M&A Consulting, appeared three or four years ago. He rocks the boat and doesn't mind doing it! He graduated from Tokyo University and majored in law, then began a career in government. But after 14 years in government, he quit and started his own company. He identifies under-performing companies, with huge cash or cash-equivalent assets, and accumulates a stake. Then he goes to the management and says, "Why don't you buy back the shares? Why don't you negotiate dividends?" At the beginning, he was ignored. But he made a great impact when he launched a hostile bid for a company called Shoei, although the bid failed. I advised Mr Murakami during his proxy fight against Tokyo Style, a garment company, last year. For those who don't know Tokyo Style, its president is infamous for his lack of corporate governance. He has no meetings with analysts or shareholders, except banks and suppliers. Yet I think he has managed the company well—he has accumulated the cash equivalent of ¥100 billion (US$950 million), but its market cap is a little bit less than ¥100 billion. Mr Murakami wanted to see the president of Tokyo Style, but he refused. At a shareholders' meeting, when Mr Murakami asked, "Why don't you distribute the profits?", the president replied, "Go away, I have no intention of reducing my cash balance." So I think Mr Murakami had no choice but to wage a proxy fight. He lost this fight, but management has since changed its practices. The president has appointed two non-executive directors, increased dividends and also promised to buy back up to 10% of the company's shares. Yet he still is hostile to Mr Murakami's approach.

Mr Murakami then filed three lawsuits against the company. One of the accusations was that the president of Tokyo Style invested in market bonds without obtaining the board's approval and then lost money. He made the investment by himself and even publicly acknowledged it at a shareholders' meeting. Mr Murakami asked, "How did you make the decision?". The president said: "I don't need to consult with the board. I make my decisions." It was a very public statement. The verdict from this lawsuit should come sometime early next year, so it will be interesting to see how things develop.[8]

Mr Murakami also accumulated stock in Nippon Broadcasting, a radio broadcasting company. The market cap of Nippon Broadcasting is ¥150 billion (US$1.4 billion). It is the largest shareholder (33%) of Fuji TV, whose market cap is ¥650 billion. So the value of its Fuji TV shareholding exceeds its own market cap. Why is that? That was a question Mr Murakami asked the president of Nippon Broadcasting. He couldn't answer. "I do not determine the market price. The market will dictate". So Mr Murakami's proposal was: "Why don't you merge the two companies and then buy back shares? Then the shareholders of Nippon Broadcasting will benefit". I think the company is considering it.[9]

There are many other similar examples in Japan. Toyota Motors is one of the best and largest companies in Japan. Its founding shareholder, Toyota Industries, owns 10% of the company—the value of which exceeds the market cap of Tokyo Industries. So there are some discrepancies here.

Mr Murakami attacks these sorts of discrepancies. His performance is astounding. He beats the TOPIX[10] by 50% constantly. 50%! Because he has no competitors. I said his business method was very simple. I expected that somebody would follow suit, but nobody has.

CalPERS[11] , meanwhile, is ready to create corporate governance "focus funds" in Japan. It has selected Sparx Asset Management as its fund manager and given it ¥30 billion (US$286 million) as a start. The Sparx investment approach is a little bit different, more quiet. They approach management, interview them and, if they believe in a company's strategy or think the management culture is good, they will then accumulate stock. So it's not as active as Mr Murakami, but a new type of corporate governance fund has been created.

The last issue I want to share with you is stock lending. When you hear about stock lending, you may think, "How is it related to corporate governance?" Stock lending involves the lending of stocks to other parties, who sell the stocks short and hope to make some money. But in a proxy fight over Telecom Italia, some dissident institutional investment managers failed to deliver enough votes because some of the stocks in their portfolio had—unknown to them—been lent out by their custodian banks (acting on the instructions of the beneficial owners—the ultimate owners). The investment managers (who make the investment decisions) believed they still had voting rights over the shares. In fact, the management of the company had successfully

[8] It was still pending as of August 2004.

[9] In the end, Nippon Broadcasting issued new shares to Fuji TV, which resulted in an increase in the cross-shareholding and a dilution of the outside-shareholder portion.

[10] A weighted index of the 1,500 shares on the first section of the Tokyo Stock Exchange.

[11] California Public Employees' Retirement System

borrowed the shares from the custodian banks and used these to get enough voting rights to win the proxy fight! This is a real phenomenon. The International Corporate Governance Network (ICGN), of which I am a director, set up a committee to discuss how to regulate these activities. This is a serious issue for institutional investors.

Robert Storer
Executive Director, Alaska Permanent Fund, Juneau, Alaska

Bob Storer explains the quieter approach of the Alaska Permanent Fund to investor activism, then outlines the ways in which it plans to become more actively involved in governance issues through its investment managers.

I'm going to start by describing what the Alaska Permanent Fund is. We're a US$26 billion public fund in the State of Alaska. About 80% of all state revenues come from oil royalties from the North Slope and decision-makers decided a long time ago that they wanted to create a fund, a legacy for future generations, once the oil was depleted. So 25% of all the money that comes to the State of Alaska from mineral wealth goes into the Alaska Permanent Fund and we manage those assets.

Our asset allocation is pretty much the same as any other public retirement plan, but maybe slightly more conservative. We divide the fund into two portions. We have internally managed fixed income and some internally managed real estate, while all of our equities are managed externally. We delegate our proxy votes to our external investment managers and they vote on our behalf.

I want to talk about our board structure and staffing, because that's important to how we make decisions. Our last three governors have replaced virtually all the board members after assuming office. We have six board members. Two are cabinet members in the administration and four are appointed. When we vote something, we have to vote a policy that has some sort of legacy and continuity to it. The last board was more activist-oriented. This board is activist and slightly more pro-business, so there is a subtle change in how we go about our business. What we are not is CalPERS or one of the large funds. We don't approach corporate governance the way they do. A good professional friend of mine in a large public fund told me they have four people (and they're trying to get a fifth) to deal with corporate governance issues, which I assume includes voting all their proxies internally.

We only have 32 employees, with just one person addressing corporate governance as a part-time job (and it's primarily an oversight role). We delegate voting to our external investment managers and have a policy that we expect them to follow. Then we have them report on an annual basis on how they've voted.

We do sell our proxy vote in the public arena through securities lending. We lend our securities for a myriad of reasons. We get a fee. You get the dividend interest, but you don't get to vote your proxy. But our investment managers do not know what is out on loan. They may think that they're voting all the stock in a certain way, but they're not. If securities are out on loan, they're only voting that portion of stock that is still held in our custodian bank under our name. We don't yet have a mechanism to create a dialogue with our managers about which issues are really important (and should be voted on). And we simply don't have a mechanism to call back those securities. I think securities lending is an important issue that is not unique to our fund.

One of the ways we've become involved in good corporate governance is by joining the Council of Institutional Investors (CII)[12] . There are some funds that are very aggressive in how they approach their membership of CII. We're not as aggressive as others, but we are a reasonably active member. We'll send at least one or two staffers, usually an outside counsel and a staffer, to its biannual meetings. We receive a lot of information from the Council and we use that as we deem appropriate (which may include responding to the SEC[13] on a regulatory issue).

One thing that perhaps separates us from some of the other members, or larger funds, is that we're not going to tell businesses how to run themselves in a public arena. We do think it's important, though, to find vehicles that create dialogue with corporations around the world. We want corporations to listen and to appreciate the importance of good corporate governance. That's a big issue on our agenda.

Pote noted that I mentioned to him earlier that we found a profit industry in government. That's not all—many of the state attorneys-general in the US are going out, suing a lot of folks and getting a lot of money. They get one heck of a good press conference out of it and they bring money in (it's a funding source to some degree). Embedded in this issue is class-action litigation. We're seeing a lot of outside legal counsel advising investors not to go through the class-action process, but to opt out and go through the state—an example would be Worldcom bonds. I mention this because at least one law firm, and I think there are many more, is creating a fee structure where it benefits X amount for a successful negotiation and gets a bonus if the corporations being sued agree to improve their corporate governance. That may be all well and good, but the semi-cynical bureaucrat in me says that these legal counsel are probably mostly interested in a quick settlement that looks good in corporate governance terms, but may not be in the best interests of the participants.

How are we going to get more active? As I noted earlier, we spend a lot of time reviewing the proxy voting policies of our investment managers—articulating what matters to us—and then querying them after they vote. I see us getting more involved through our managers in active corporate governance. I see it as a three-part process. The first part is that when the investment managers vote, we'll ask them, "Why did you vote for that—what did you do besides vote for independent directors? What did that mean? How did you come to that conclusion?" I assume we'll get okay answers.

The second part is having a dialogue with our investment managers that says, "We think you ought to be more active—not just voting 'yes' for independent directors, but talking to companies (about their governance), talking to everybody, getting out there. If you truly believe that matters, then why aren't you out there engaging companies more?"

The third part is saying, "We're tired of this. This is what you're going to do". We'll be

[12] CII is based in Washington, DC. See its website: www.cii.org

[13] Securities and Exchange Commission, Washington.

more explicit in directing our investment managers. You might say that's somewhere between naive and arrogant, but over a one-, three- and five-year time span, it would be my expectation that our managers will play a more active role.

I will close with one simple thing that applies to our managers. Every single one signs a contract that they accept fiduciary responsibility, and embedded in that is a duty to ensure we are well served. Good corporate governance is part of that.

QUESTIONS & ANSWERS

Questions and comments from delegates covered the following issues:

- Reallocating investment managers to keep them honest.
- Supervising the governance of institutional investors.
- Mutual fund scandals in the US and shareholder responsibilities.
- The view of institutional investors on class-action lawsuits.
- The growth of shareholder lawsuits in Japan.
- Keeping investment managers to your governance objectives.
- The tiny proportion of institutional investors in Japan without conflicts of interest.
- The chilling effect of the corporate pension-fund business on institutional investor activism.
- How to incentivise your investment managers to be more proactive.

QUESTION: I have a quick question for Bob Storer. Your policy relies primarily on the action—if I understand it right—of your outside investment managers. How often do you reallocate your managers to keep them honest and in line with your objectives? Would 10%, 20% per year be a rough ballpark figure?

ROBERT STORER: That's an important question. We're essentially a "buy and hold" fund and we may dismiss one manager a year. By the way, embedded in our policies are some explicit directions to managers on issues we think important, so we don't simply delegate everything to them. It's a fairly low turnover, and not much of an issue. But what we have not done, and something we need to do, is to make our investment managers more accountable in how they vote. To be frank, that's been somewhat perfunctory.

I'd like to add a comment on passive management. We believe that we should play a larger role, given our passive portfolio, in how voting occurs. We should see more activity in that area. The problem is you expect more from investment managers, but passive management becomes ever cheaper—our marginal rate on fees is half a basis point. So at some point, if we're going to be more active with our passive portfolios, we're going to have to acknowledge some sort of cost to that.

QUESTION: There is the concept now of auditing the external auditors. What about the ongoing debate on the governance practices of institutional investors? Who should, or could, be the overseer?

ROBERT STORER: That's a great question. I don't know the answer, but one of our concerns is separating fad from what's really important. This is one reason for our conscious decision not to take a higher profile on a number of issues, but instead evaluate what we believe is in our best interests and that of good corporate governance. I think you bring up a myriad of issues, including how we conduct business. Does the corporate governance of our fund withstand the test?

POTE VIDET: Do you want to comment on the controversy with mutual funds, and the governance of these funds, in the US right now?

ROBERT STORER: We've had a debate whether corporate governance in mutual funds is under our purview. Should we respond to SEC enquiries when we don't get involved in mutual funds? A concern that we have is whether the recent headlines are the tip of an iceberg? What are the implications in lost faith among private investors in funds?

TAIJI OKUSU: I'd like to make a comment. I attended last week's OECD preliminary discussion of its revised corporate governance principles. There were three themes. One was market integrity. The second was enforcement and implementation. The third was shareholder responsibilities. We talked about shareholder rights, but now new light is being shed on shareholder responsibilities and obligations. Many institutional investors do not vote. But soon fund governance itself is going to be a new area of discussion.

QUESTION: The last session briefly touched upon class-action lawsuits by shareholders. In Korea, that's one of the keenest debates right now. How easy should it be to file class actions, what's the threshold amount, what's the size of the company, and so on? My question to the panel is whether institutional investors would see class actions as positive to a company's financial health and conduct and, eventually, a better bottom-line? Or, as opponents of class action in Korea like to say, it will lead to too many frivolous actions, resulting in too much waste of company resources, time and management energy. What's the basic attitude of institutional investors?

And my second question: Taiji Okusu mentioned Mr Murakami's campaign for corporate governance in Japan. Is there any civic movement in Japan similar to the shareholder activist NGOs in Korea? Have they tried to install a broader, wider, stronger class-action regime in Japan?

ROBERT STORER: I'm seeing more and more institutional investors trying to take the lead (in corporate governance), not just as part of a class-action lawsuit. But here's the issue—what law firms do is try to aggregate enough clients together so that they are awarded the lead counsel position in a class-action suit. I'm seeing more and more public funds—funds that were previously adamantly opposed to initiating actions—participating in them. Although we haven't initiated anything to date, we have put together a cadre of law firms to assist us. So I see it becoming an ever bigger issue in the United States, and this will inevitably spill over in some capacity around the world.

TAIJI OKUSU: Apart from Mr Murakami, there is a group in Japan called the Shareholders' Ombudsman that has also been very active in bringing to court corporations that have committed malpractice, illegal actions and sometimes crimes. Some of their cases are successful, and some are not. Lawsuits are not popular in Japan, but in extreme cases I think they are very effective.

QUESTION: Mr Storer, you were saying that when you farm out funds to investment managers, embedded in your contract is something about them taking corporate governance into account in their investment process. How do you determine whether they are doing that? Should trustees be looking for minimum governance standards in companies that are being invested in?

ROBERT STORER: I'd suggest we're probably half way along. We do set guidelines. Some of them are broad guidelines that give the investment manager discretion. Others are more explicit, where there's no discretion. For example, they must vote for independent directors. We also ask the investment managers to report. We aggregate their answers on an annual basis and make a full report to our board. We don't go through vote by vote, but we try to highlight all the main issues and any exceptions. On a quarterly basis, staff may sometimes evaluate managers—though, to be honest, it doesn't happen very often. What is missing, I think, is that—unless some headline news has occurred—we're not delving into specific companies the way we ultimately should be. I think it will be a partnership with staff and the investment managers, and we'll spend more time on this issue in future.

On a related point, turnover in staff can be a plus because corporate governance is no longer a side issue for new employees. It is becoming an integral part of each person's duties and new employees are far more enthusiastic to help, where previously there was some reluctance from older staff.

I would add that, as a fund manager, there is always a difficult distinction between form and substance. My experience has been that good governance awards, for example, are often based on a checklist of issues, such as composition of board, committees and so on. But finding substantive performance measures for corporate governance is difficult. Generally, what you know about substance comes after the fact and is often negative. It's difficult to measure positive governance. Obviously, we hope that form will lead to the better running of companies, more transparency and fewer conflicts. But that is difficult to measure.

QUESTION: What would you estimate is the proportion of institutional investors in Japan who do not have a conflict of interest? People who are truly interested in acting for the benefit of their beneficiaries and pensioners. What's the proportion of institutional investors in Japan that fall under that category? How tiny is it?

TAIJI OKUSU: I don't have answers to your questions, but I think it must be tiny.

QUESTION: This question is to Mr Storer and relates to how you select managers. One issue being debated in the United States is whether investment managers who actively solicit companies for pension fund business can be relied upon to take a strong line, when necessary, towards those same companies on corporate governance. A few public-sector funds are beginning to look for investment managers who are not engaged in the pension business and who are willing to agree not to invest in companies whose pension funds they are actively managing. What do you feel about that, and what do you think is the future direction? Are we going to see a distinction between managers who do just pension money and those who don't?

ROBERT STORER: You may see some separation, but I'd be surprised, at least for the foreseeable future, if we see a lot of change in this area. In my opinion, we have to ask better questions of our managers and follow up to get better answers. Being cynical again, we ask our managers a lot of questions and we often get well-practised answers. We need to go to that next layer, which is the follow-up question, go deeper and hold them more accountable.

QUESTION: Mr Storer, what incentives do you believe are needed to get your investment managers to devote more resources to research on corporate governance, and to take action when there are sufficient grounds to do so? There are fund managers who will do it in a pro forma fashion, and there are those who take it seriously and devote the necessary resources to challenge management to do better. What kind of incentives need to be fashioned to encourage a more proactive role?

I also want to comment on something you said earlier about the measurement of corporate governance performance. Yes, this is difficult. But we have to measure corporate governance not just quarter to quarter, or even year to year, we have to measure it over time—five, six, seven, eight years, particularly for investors who have a long-term view, such as pension funds. If the fund managers were doing their job and really looking into corporate governance practices, I'm sure many of them could have saved hundreds of millions of dollars by getting out of situations such as Enron and WorldCom long before they imploded.

ROBERT STORER: One incentive I have found helpful in dealing with managers is that if you make your expectations clear, and then follow up and make sure they are quite clear, then the managers tend to respond. The big incentive, I think, is simple: if they do it, you don't fire them! In the large-cap US markets, asset managers are like commodities. I'm not talking about passive management. I'm talking about large-cap active management. If they weren't inclined to do what you wanted, or give me a good reason for not doing so, then I would find somebody that would. There are many good firms out there. We use about 16 firms and the list of good ones is significantly larger than that. I think it goes back to, "Be clear, and make sure that the manager truly understands and appreciates where you're coming from." Many of our managers talk about "value-added" and "strategic relationships". They recognise that you have to do more than just manage assets. It's a very competitive world, and corporate governance is an area where they can be value-added and should be value-added.

COMMENT: I manage two large investors and in every quarterly report that I have to sign my name to there is a disclosure statement that says we're managing the fund according to their objectives. These include no investments in companies that are involved in armaments and tobacco, and things like prostitution and slave labour. That sounds kind of crazy, but these are specific issues that people investing in Asia care deeply about. Even though I know we don't have any of those investments in our portfolio, I think about it every time I put my name down. It's amazing what having to sign a piece of paper does to a manager. You think again, "Have I ever, in the last three months, come across anything that would lead me to change my opinion since I signed my name three months ago?" So Mr Storer, I think your point about taking specific steps makes a lot of sense.

Luncheon Keynote Speech:

"The Critical Role of Company Courts in Fostering Good Corporate Governance"

Jack B. Jacobs
Justice, Supreme Court of Delaware, United States

When the Asian Corporate Governance Association (ACGA) invited me to speak at this conference, I asked what topic would be of greatest interest to an audience as distinguished as yourselves. ACGA suggested discussing the role specialised company courts play in promoting better corporate governance. That topic, they said, is very relevant to Asia. To me that sounded like a great idea, because after serving 18 years on a Delaware court having an expertise in corporate and business law, I believed this subject would flow quite naturally.

I could not have been more mistaken. Once I began to focus on this topic, it became clear that the assignment was much more daunting than I had imagined. To start with, the concept of "company courts" (we call them "business courts" in the United States) is itself relatively new. At present such courts are found only in the US and a few European countries. Some US business courts have been successful in that they have shown themselves capable of resolving intra-corporate disputes rapidly, in depth, and in a manner satisfactory to the parties and the larger business community. But even so, there is very little scholarly literature that analyses in a systematic way whether—and if so, how—specialised business courts influence corporate governance. Moreover, even if one could find a linkage between company courts and corporate governance in America, it hardly follows that the American experience could be replicated in the quite different commercial environments of Asia. Indeed, I am informed that to date no company courts yet exist in any major Asian commercial centre.

Ultimately, it became clear that this subject required focusing on two quite separate questions. One, what is the relationship (if any) between specialised business courts and corporate governance in the community I am personally familiar with—the United States and specifically, the State of Delaware? Two, how, if at all, can the American experience be made relevant to the corporate governance systems of those Asian countries that have major public capital markets? If you will indulge me for the next few minutes, I would like to share with you my thoughts on those questions. I begin with my conclusions, and follow with the reasons that led me to those conclusions.

First, the historical experience of the Delaware courts in the corporate governance area shows that company courts are capable of profoundly influencing the direction of corporate governance. Second, although the major Asian commercial countries do not have specialised business courts, I view the recent Japanese experience in the Daiwa Bank case as evidence that, in the right circumstances, properly motivated and empowered Asian courts can influence corporate governance in their respective countries. Third, and finally, in Asia that will be possible only if certain conditions exist. I conclude by identifying three of those conditions.

I.

The natural starting place for me is our experience with American business courts. Even here, however, the experience base is thin, because to date only a handful of states have established courts that specialise in corporate and business law. With the exception of Delaware, those courts are administratively created, specialised divisions of already-existing courts of general jurisdiction. As such, they must be distinguished from independent courts of limited, specialised jurisdiction.[14] To understand the American experience with business courts, a moment or two of background is helpful.

The success of Delaware's business court—the Court of Chancery—led other states to attempt to create their own business courts during the past several years. That movement was driven by the business communities of those states, who expressed a need for specialised courts capable of resolving business disputes faster and more expertly than courts of general jurisdiction, which normally are hampered by large backlogs of criminal and other non-business cases. In the few states that have business courts, those courts have proved advantageous to the business community. Their judges have been afforded the time to develop expertise in business law and to create processes for resolving complex business disputes more quickly and accurately than non-specialised courts. Thus far, however, this movement is limited to a few states. Many American states have declined to create business courts because they are perceived to be elitist—affording one class of justice to wealthy businesses and a lesser kind of justice to ordinary individuals. That perception, plus the added cost of creating specialised courts in states now experiencing significant budgetary crises, were formidable political barriers to creating business courts in those jurisdictions.

Because these few specialised commercial courts are new, and their jurisdiction often comprehends more than corporate governance matters, there is insufficient data—at least at this point—to generalise broadly about the relationship between company courts and corporate governance in America. Indeed, the only "company court" whose experience can reliably be viewed as instructive on that subject is the Delaware Court of Chancery, which, ironically, was created 200 years ago, not as a business court but as a court of traditional equitable jurisdiction in a small rural state. Only during the past 80 years did that court develop expertise in corporate and business law matters—not because of a formal decision to specialise, but because of the large number of public US companies that are incorporated in Delaware, and because the jurisdiction to resolve the intra-corporate disputes in those companies became vested in the Delaware Court of Chancery.[15]

[14] In New York, for example, the Chief Judge of the Court of Appeals created a Commercial Division of the New York Supreme Court, which is that state's trial court of general jurisdiction. New Jersey assigns to its Chancery division cases that are denominated as "complex litigation." North Carolina has created a separate Superior Court Judge for Complex Business Cases. Illinois has created (for the Chicago area) a commercial litigation division of the Cook County Circuit Court. Wisconsin also has a special business court. I purposefully omit to discuss the Commercial Division of the Queens Bench of the English High Court of Justice because of my unfamiliarity with that institution. See Ember Reichgott Junge, Business Courts: Efficient Justice or Two-Tiered Elitism?, 24 Wm. Mitchell L. Rev. 315 (1998); Report of ABA Ad Hoc Committee on Business Courts, Business Courts: Toward a More Efficient Judiciary, 52 Bus. Lwyr. 949 (May 1992).

[15] Bus. Lwyr. at 956.

In our country, under the internal affairs doctrine, courts apply the law of the state of incorporation to resolve governance disputes. Thus, governance disputes arising in Delaware corporations are governed by the law of Delaware. Over time, each court decision which interprets or applies that law becomes a part of what is now perhaps the most developed body of corporate and business law precedent in the United States. Because over half of the major public companies are incorporated in Delaware and do business nationally and (in many cases) multinationally, the effect of Delaware court precedents extends far beyond the borders of that state. For these reasons, in the corporate and business law area the Delaware Court of Chancery (and the Delaware Supreme Court which reviews Chancery decisions) although technically authoritative only in Delaware, are regarded de facto as courts of national corporate law.

Because of the extensive body of Delaware corporate governance case law carefully developed over many decades, those decisions provide a meaningful database to assess whether there is a meaningful connection between judicial corporate governance decisions and corporate governance as actually practised in the real world. In my view there is such a connection. In the following brief discussion of a few well-known Delaware corporate cases and their real-world effect on governance, I will attempt to show you why.

It has always been hornbook doctrine that corporate directors owe a fiduciary duty of care to the company and its stockholders. Despite what the law books said, however, before 1985 no corporate board had been found liable for conduct amounting solely to a breach of the directors' duty of care, as distinguished from their duty of loyalty. The reason, I submit, is that at that point in time, the role of corporate boards was that of passive advisors, with the CEO being completely dominant and taking all important initiatives, and the board having no prescribed role other than to give advice when asked and to approve executive proposals when made.

All that changed after *Smith v. Van Gorkom.*[16] There, the board of a public Delaware corporation was found liable for money damages for approving an acquisition of their company, arranged solely by the CEO without board authorisation or approval, at a price that was neither negotiated at arm's length nor validated by a formal financial valuation of the company. The board's approval occurred at a short meeting at which no documents had been provided to the directors, and at which the directors made no critical inquiry about the merits of the transaction, instead relying upon an oral presentation by the CEO. In these circumstances, the Delaware Supreme Court held the directors liable for breaching their fiduciary duty of care.

Van Gorkom sent shock waves throughout the American corporate community, and it also had profound effects on corporate governance. The case changed the corporate culture of American public company boards by sending a strong message that all corporate boards, including independent directors, had an affirmative duty to act with due care and to make an informed decision that any transaction to which they commit their company is in the best interest of the company and its stockholders. Personal liability could result from a breach of that duty. Second, *Van Gorkom* prompted a national insurance crisis by raising the cost of directors' and officers' liability insurance. The result was legislation that authorised Delaware corporations to exculpate

[16] 488 A.2d 858 (Del. 1985).

their directors from money damage liability for adjudicated breaches of the duty of care, by including an appropriate provision to that effect in their charters. Thereafter, almost all of the remaining 49 American states adopted similar legislation.

In 1996, the Court of Chancery decided a second landmark case—*Re Caremark Intern., Inc. Derivative Litigation*,[17] which announced that Delaware corporate boards had a duty of care not only in making decisions, but also in overseeing decisions made by management. *Caremark* was a settlement of a derivative action against the board of a public company, where the plaintiffs sought to recover a multimillion-dollar criminal fine assessed against the company for violating certain federal laws. In *Caremark*, the Court recognised that although corporate boards are not required to micromanage decisions made at the management level, they must attempt, in good faith, to implement a system that will keep the directors informed about whether management decisions and practices are in compliance with the laws that govern the company's business.

Like *Van Gorkom, Caremark* has also profoundly affected the governance of American public corporations. Almost immediately after *Caremark* was decided, many public companies began taking steps, including hiring experts, to institute compliance systems designed to assure that their boards would be properly informed about actions taken by their managers, and whether those actions were placing the company's compliance with law at risk. A multitude of law firms have now developed subspecialties in this field. In 2002, the *Caremark* rule was federalised (at least in part) by the Sarbanes Oxley Act, which requires that in companies covered by the Act, compliance systems be put in place and that the CEO publicly certify whether those control systems are properly functioning. Following the recent scandals involving companies such as Enron, Global Crossing, and Tyco, the board's duty of oversight, first recognised in *Caremark*, has now become a permanent fixture in the American corporate governance landscape.

Similarly influential Delaware corporate governance decisions were issued in the area of corporate takeovers. In this setting, what is at stake is not whether the board of the target company will be liable for money damages, but whether the board will retain or lose control of the company. Until the mid-1980s, the legal standards governing what boards could and could not do in response to a hostile takeover bid were not well developed. To fill that gap, the Delaware courts, in the late 1980s, developed new standards that had a profound effect nationwide, during a period in which entire industries were consolidating.

In *Unocal Corp. v. Mesa Petroleum Co.*[18] the Delaware Supreme Court held that a target company board can properly oppose a hostile takeover, (in that case, by T. Boone Pickens) but only if the board concludes in good faith and after a reasonable investigation that the takeover poses a threat to corporate interests and policy, and if the board implements defensive measures that are not disproportionate to the threat. In the famous *Revlon*[19] case and its progeny[20] , our Supreme Court held that once a target company board commits to a sale or change of control of

[17] 658 A.2d 959 (Del. Ch. 1996).
[18] 493 A.2d 946 (Del. 1985).
[19] MacAndrews & Forbes v. Revlon, Inc., 506 A.2d 173 (Del. 1986).
[20] QVC Network v. Paramount Communications, Inc., 637 A.2d 34 (Del.1994).

their company, the board's duty is to obtain the maximum available value for the shareholders, and not to interpose any obstacles to receiving that value, even if the result is that the company is sold to a bidder the directors personally oppose. In the *MacMillan*[21] case, where the target company board resisted a takeover attempt by Sir Robert Maxwell, the Delaware Supreme Court held that in conducting an auction to sell the company for the highest available value, the board had a fiduciary duty actively to oversee the fairness of the auction. In *MacMillan*, the board was found to have violated that duty by abdicating that responsibility to a senior officer whose personal interests were in conflict with that objective.

Lastly, in 1998, the Court of Chancery, *in Carmody v. Toll Brothers*,[22] and the Delaware Supreme Court, in the *Mentor Graphics*[23] case, announced rules for how a target board must conduct itself in a contest for corporate control, where the board adopts a controversial variation on an anti-takeover mechanism popularly known as the "poison pill". In *Toll Brothers*, the Court of Chancery outlawed poison pills that could not be redeemed (i.e., rendered inoperative) except by the directors who originally adopted the pill. Defensive measures of that kind would discourage shareholders from exercising their right to elect a new board in a control contest. Similarly, in *Mentor Graphics*, both the Court of Chancery and the Supreme Court invalidated a poison pill that could not be redeemed until six months after the incumbent board had been replaced.

These decisions, all arising in the context of a fight for corporate control, also had governance effects that extended far beyond Delaware. Technically, those decisions were legally binding on all public companies, wherever located, that were subject to Delaware corporation law. But those rules were also applied by courts in jurisdictions outside Delaware that were not governed by Delaware law, yet chose to follow Delaware's rules in the corporate governance area. As a result, when American public companies engage in change of control transactions, their boards are often counselled not to erect disproportionate defenses to hostile bids, including poison pills of the kind proscribed by *Toll Brothers* and *Mentor Graphics*. And, when directors decide to sell their public company, they are often counselled to do so in accordance with *Revlon* value-maximising precepts.[24]

Thus, to the question: can "company courts influence and improve corporate governance?" I submit that the answer is yes. But that only raises the second question, one of more direct importance to you, which is: can company courts similarly influence the public company governance systems of the major commercial countries of Asia? That issue is far more complex.

[21] Mills Acquisition Co. v. MacMillan, Inc., 559 A.2d 1261 (Del. 1988)

[22] Carmody v. Toll Brothers, Inc., 723 A.2d 1180 (Del. Ch. 1998).

[23] Quickturn Design Systems v. Mentor Graphics Corp., 721 A.2d 1281 (Del. 1998), affirming on other grounds, Mentor Graphics Corp. v. Quickturn Design Systems, Inc., 728 A.2d 25 (Del. Ch. 1998).

[24] Moreover, and on a more macroscopic level, these Delaware decisions ignited a national debate about what governance rules should (or should not) apply to boards of public companies, wherever incorporated, in the context of a takeover. It also resulted in state legislation. Many states chose to follow Delaware's system of takeover rules; several did not. But whatever the outcome of the governance debate, there is no question that because of their peculiar role in our country's legal scheme, the Delaware courts have influenced the manner in which public companies in the United States are internally governed.

II.

A prime reason for that complexity is that the corporate governance systems of the major commercial Asian countries and cities I have studied—Japan, Korea and Hong Kong—are the product of histories, structures, and value systems quite different from those of the United States and other Western countries. Moreover, the governance systems of these Asian countries are different, and none of them has a specialised business court.

The countries that do have such courts—the United States, the United Kingdom, and certain other European states—have a different governance system—an equity-based system, in which the financing source for public company growth is the equity capital market. In American public companies, public stockholders (mostly, institutions) often own a large (and sometimes a controlling) stock interest, with the directors and managers owning far smaller amounts. The Western equity-based system depends critically upon accounting transparency and detailed periodic disclosure of the financial status of all listed companies. That system also depends importantly upon governmental agencies to enforce these mechanisms—in our country, the Securities and Exchange Commission and the courts. In our society, litigation is an accepted mode of enforcing shareholder rights against directors and officers who owe statutory and fiduciary duties to their company and its public stockholders. Litigation is not the norm in Asia, however.

As those of you in this room know far better than I, the major Asian commercial countries and centres have very different and diverse corporate governance models. To be sure, although Hong Kong, Japan, and Korea have public securities markets, their companies have not historically depended upon outside capital for their growth to the same extent as US companies. The fiduciary duty concepts in those Asian communities are not as well developed. And, transparency of accounting, and accurate disclosure of the financial status of public companies to outside investors are not as firmly established in Asia as in Western capital markets. Importantly, also, and with one exception that I will shortly discuss, in Asian countries, the courts are not regarded as mechanisms to enforce the rights of public investors in Asian companies.

Hong Kong is a case in point. Hong Kong has no specialised business court, although it does have an active stock exchange and has adopted corporate governance principles that are enforced through Hong Kong's Securities Exchange Listing Rules and its Securities and Futures Commission. Although the Hong Kong Listing Rules now require listed companies to have at least two independent directors and to follow certain disclosure requirements, Hong Kong does not have an equity-based corporate governance model. In Hong Kong, most listed companies tend to be controlled by families. As of 1996, 53% of the companies listed on the Hong Kong Stock Exchange had a single stockholder or family group of stockholders that owned over half of the company's issued stock. In this family-based structure, the majority stockholder normally occupies the position of CEO, and in those companies the board of directors is not a major factor in corporate governance. For that reason, some have predicted that the new independent director requirement will have little impact on the governance of most Hong Kong public companies.[25]

[25] Stephen Y. L. Cheung, Corporate Governance in Hong Kong, China: Rising to the Challenge of Globalization (2000).

Because of the marginal role of corporate boards in this environment, it has been suggested that corporate governance reforms in Hong Kong should focus not so much on having independent directors as on ways to protect minority shareholders from expropriation, usually in self-dealing or related party transactions, by the majority stockholders who operate the corporation.[26] After a Hong Kong company goes public, its founders normally retain a major stake as controlling shareholders, and they often tend to treat the company as their own private property. They view the investing public (who are the minority stockholders) as mere providers of funds, rather than as shareholders or co-owners to be treated equally.

At present in Hong Kong, there is no effective judicial remedy for minority stockholder expropriation. The legal literature on this subject suggests that in limited circumstances, controlling shareholders in Hong Kong are permitted to vote, in their capacity as shareholders, to ratify a self-dealing transaction, although in other circumstances independent stockholder approval is required. I am also informed that the Hong Kong case law on fiduciary duties is not well developed, there are no class actions in Hong Kong, and although derivative actions are allowed, there is little economic incentive for shareholders to bring them because of the absence of contingent fees and because the company, not the shareholders, obtains the recovery.[27] These factors, plus the absence of Western-style accounting transparency, help explain why investors in Hong Kong-listed companies often purchase their stock in those companies at a discount.

Despite that, an active, vigorous corporate governance debate is taking place in Hong Kong. Proposals for reform have been advanced by the Standing Committee on Company Law Reform and by other groups. The 1999 reform package included proposals to create a Market Misconduct Tribunal (which has since been adopted), and to recognise private rights of actions against market misconduct and false disclosure of information. But, because to date there is no indication that Hong Kong intends to use courts and judges to enforce internal corporate governance requirements, the Hong Kong experience does not advance our inquiry about the usefulness of company courts.

A second possible candidate for testing whether company courts can foster improved corporate governance is Korea, whose major companies, organised into huge conglomerate groups called chaebol, were traditionally financed by banks. That bank financing, which came at relatively cheap rates, created debt-heavy capital structures that made the chaebols vulnerable to economic downturns. Only after their capital demands outstripped the domestic capital supply did the Korean banks and chaebols turn to foreign capital. At that time foreign capital was readily available because everyone assumed the government would not let the major banks or chaebols fail. The Asian crisis of 1997-1998 exposed the flaw in that assumption. At that point, major banks became insolvent and eight large chaebols went bankrupt.

[26] Betty M. Ho, Restructuring the Boards of Directors of Public Companies in Hong Kong: Barking up the Wrong Tree, 1 Sing. J. Int'l & Comp. L. 507 (Oct. 1997).
[27] Say H. Goo and Rolf H. Weber, The Expropriation Game: Minority Shareholder Protection, 33 H.K.L.J.71 (2003).

That crisis led to the realisation that Korea would have to become a more attractive market for foreign capital, and that view created a need to consider changes in Korean corporate governance. A Commission of experts, including Professor Bernard Black of Stanford Law School, was formed and in May 2000 submitted a set of legal reform recommendations to the Korean Ministry of Justice.[28] The Commission's recommendations were far reaching. They proposed a host of American-style reforms, including a more precise articulation of directors' fiduciary duties, requiring a majority of independent directors, and requiring accounting transparency, in Korean corporations. Of greatest relevance here is the Commission's proposal that "consideration…be given to creating in Korea's major cities a separate bench of the District Court to handle large or complex commercial and financial disputes, including stockholder litigation".[29] It remains to be seen whether that will happen, and, if specialised business courts are created, how effective they will be in improving the corporate governance of Korean corporations. Accordingly, at this time, the Korean experience does not yet afford a useful basis to predict the impact of company courts on corporate governance in Asia.

The third, and final, Asian country on which I focussed is one that I initially thought would be the most resistant to the creation of company courts—Japan. Yet, Japan's recent experience with the Daiwa Bank case suggests that Japan may be the first Asian country to utilise its courts to effect corporate governance changes.

Conventional wisdom holds that Japan's corporate governance system is the keiretsu model, where a "main bank" assembles its large public company clients into a "keiretsu" (corporate) group. In that group, the bank has an ownership interest in each company, and each company, in turn, is part of a cross-shareholding network with all other companies in the group. Under that model, the bank polices each company's corporate governance by monitoring that firm's performance, and if the firm falls into trouble, that bank takes control. Thus, in normal times, under this arrangement the keiretsu firms would be free to ignore the risks of hostile acquisitions and the stock market.

[28] Bernard S. Black, et. al., Corporate Governance in Korea at the Millennium, a Final Report and Legal Reform Recommendations to the Ministry of Justice of the Republic of Korea, May 15, 2000, 26 Journal of Corporation Law, 537-608 (2001)

[29] Id., at 569. By way of commentary the Commission explained that:

> It is common in many jurisdictions for the courts in the major cities to have a specialized "bench" or court which handles commercial, corporate and financial disputes…The judges on such a court hear a continuing stream of cases involving commercial, corporate, and financial issues, and develop expertise in adjudicating these often technical matters. Specialized courts also tend to have fewer backlogs than courts of general jurisdiction, permitting speedier disposition of time-sensitive commercial, corporate and financial matters.

Although the factual support for the keiretsu model is disputed by some scholars,[30] what is not disputed is that as a result of the Asian financial crisis, the keiretsu bank financing system began to unravel, because the banks themselves were either failing or in distress. As a result, Japanese firms began to seek equity financing from American and European firms, and in the late 1990s, Japan instituted certain "Big Bang" reforms designed to make Japanese firms more attractive to foreign investors. At that time, many believed that Japan might require its public companies to adopt Western forms of corporate governance wholesale, and that the Japanese and Western forms would eventually converge—if not formally then at least functionally.[31] But that did not happen. Japan did amend its company law to give its firms the option of moving to an American-style system, which would include officers and boards of directors with three major committees. Some large firms, such as Sony, Toshiba, Nissan Motors and Japan Airlines, opted for that system, but many Japanese firms did not. Indeed, some influential groups within Japan continue to resist these changes.

The resulting impression was that if Japan changed its traditional corporate governance system, it would do so only marginally. Moreover, there was little evidence that the Japanese courts, which had discouraged derivative actions against managers by typically requiring the plaintiff to post a sizeable security bond for costs, would be a useful source of corporate governance change—that is, until the Daiwa Bank case came along in the late 1990s. After that case, the Japanese corporate governance world now begins to look different.

For those of you who may be unfamiliar with the Daiwa Bank case, I will briefly summarise it. Between 1985 and 1995, a local manager of the New York branch of Daiwa Bank accumulated trading losses that ultimately totalled US$1.1 billion. For a period of time, the manager concealed those losses, but in 1995 he wrote the Bank's President a letter confessing what he had done. Rather than immediately notify the American and Japanese banking authorities, Daiwa's President decided to cover up the losses. In furtherance of that scheme, in August 1995, the top management of Daiwa Bank met informally with Japanese Ministry of Finance officials and supposedly obtained those officials' informal approval for taking that approach. Daiwa continued to conduct business as usual in New York until mid-September, at which point its management disclosed the losses to US and Japanese regulators.

[30] Two noted scholars dispute the factual accuracy of this model, and claim that at least since the 1980s, the keiretsu model has had no factual support. Yoshiro Miwa and J. Marc Ramseyer, The Myth of the Main Bank: Japan and Comparative Corporate Governance, 27 Law & Soc. Inquiry 401 (2002)

[31] See Matthew Senechal, Reforming the Japanese Commercial Code: A Step Towards An American-Style Executive Officer System in Japan?, 12 Pac. Rim L. & Pol'y J. 535 (Mar. 2003); Luke Nottage, Japanese Corporate Governance at a Crossroads: Variation in Varieties of Capitalism?, 27 N.C. J. Int'l L. & Com. Reg. 255 (Winter 2001); Ronald J. Gilson, Globalizing Corporate Governance: Convergence of Form or Function, Working Paper No 174, Columbia Law School Center for Law and Economic Studies (May 2000).

That delayed disclosure had several fallouts. First, the US authorities closed down the New York office immediately. In November 1995, a grand jury indicted the Bank and its New York general manager. The manager pled guilty to the charges, and Daiwa Bank entered into a plea bargain in which it pled guilty to 16 of 24 criminal counts and paid a US$340m criminal fine. Second, Daiwa's top officials resigned, the Japanese Ministry of Finance imposed sanctions against the Bank, and the Bank's shareholders initiated derivative actions against the Bank's directors and statutory auditors to recover the losses resulting from their alleged breach of fiduciary duty.

In both derivative cases, the Japanese High Court rejected the District Court's imposition of a high security for costs bond—a ruling that allowed those cases to go forward. In the first case, the directors were found liable for failure to create an appropriate risk management system for the New York branch. In the second case, the directors were found liable for (i) breaching their duty of care by failing to ensure that the Bank conformed to foreign law, and (ii) breaching their duty of loyalty by not notifying the regulators immediately of the Bank's losses. In arriving at that result, the District Court held that the directors were not entitled to rely upon informal Ministry of Finance advice as an excuse for not making immediate disclosure. All told, the directors were held liable for US$775m in damages.

These unprecedented court judgements created shock waves throughout Japan, like the *Van Gorkom* and *Caremark* cases did in the United States. The Daiwa Bank case also generated significant corporate governance changes in Japan, including strengthening the derivative suit system, emphasising the importance of board-instituted compliance programmes and internal controls, increasing the demand for directors' and officers' insurance coverage, and amending the Japanese Commercial Code to create a Delaware-like exculpatory charter provision to shield directors from judgements for duty of care violations.[32]

The Daiwa case is viewed by some as persuasive evidence that Japanese courts, like those in the United States, can influence the direction of corporate governance by their rulings. One scholar has noted:

> "Viewed in a positive light, these court decisions could have an educational effect by improving corporate governance practices. Executives' strong reaction to and fear of such cases, combined with the role of lawyers in advising corporations on new risks and preventative measures, can act as an important tool for improving corporate governance practices.... Regardless of whether Delaware courts consciously count on this effect when rendering decisions, the result is that corporate governance practices can be affected and presumably improved by a small number of cases which find potential or actual liability on the part of directors."

[32] Bruce E. Aronson, Reconsidering the Importance of Law in Japanese Corporate Governance: Evidence from the Daiwa Bank Shareholder Derivative Case, 36 Cornell Int'l. L. J. (2003).

The author then goes on to express skepticism about whether Japanese courts can play a similar role, because the opinions of those courts are generally short, they often do not cite court precedents, and they rarely engage in the kind of policy discussions that are common in US court decisions. Having said that, the author, nonetheless, observes that:

> "[S]omething clearly is going on in the Daiwa Bank case—it is unlikely a coincidence that a decision that grants an enormous damage award based on a breach of the duty of oversight for the first time is an amazingly lengthy decision…One certainly suspects that the Daiwa Bank court had motivations, akin to those sometimes ascribed to Delaware courts, of setting corporate norms and showing the "bad" behavior of defendants to legitimize its exercise of judicial power…"[33]

If that is correct, then the Daiwa Bank case can be regarded as evidence that courts in Japan, even though not specialised company courts, can play a role in fostering good corporate governance, similar to that played by courts in the United States.

III.

I conclude with one question and two brief observations. If courts have influenced corporate governance in Japan but not in other Asian countries, is that because the conditions for fostering such influence exist in Japan but not elsewhere in Asia? If so, then what are those conditions? To be candid, I do not know the answer, and to fashion a complete list of those conditions is an undertaking outside my area of expertise. Of three conditions, however, I am fairly certain. First, there must be a policy judgement to make Asian public companies and capital markets sufficiently attractive to encourage significant foreign investment from Western sources. Second, there must be a policy judgement that Asian court enforcement of investors' rights will be an essential ingredient in that process. And third, those courts must be sufficiently expert and competent to handle complex business disputes, so as to assure investors in Asian companies that these tribunals are willing and capable of protecting their investment against expropriation by management or by majority stockholders.

I thank you very much for your kind attention.

[33] Aronson, supra note 19, at 40.

Session 3: Stakeholder Imperatives

Moderator:

James Prieur
President and Chief Operating Officer, Sun Life Financial, Toronto

James Prieur argues that, over the long term, a principles-based approach to corporate governance works better than a rules-based one. And he calls the Sarbanes Oxley Act a "political response to the wrong problem".

We are all products of our environment, as Justice Jacobs said at lunch, so I thought I would start with a bit of background on Canadian corporate governance. In some respects, Canada is a lot like quite a few Asian countries. First, it has a colonial history. And second, it is close to an extremely large neighbor that tends to have a big influence on the way business is done.

The Canadian corporate governance context is not quite American nor is it quite British. It is a mixture of the principles-driven environment of the UK and the rules-driven environment of the US. The hope in Canada, of course, is that we take the best out of both, although I cannot say that we always do!

My answer to the main question of this session is that Asian companies should do all in their power to create for themselves, their industries and, indeed, their countries a system of governance that is transparent, consistent and accountable for all stakeholders. It is not only the right thing to do, it is the smart thing to do.

By nature, I tend to favor the principles-based approach. I think that it is more likely to survive changes in the environment than a rules-based approach and my view stems in part from the corporate history of Sun Life Financial. We have been around since 1865 and the word "integrity" has been one of our prominent corporate values since the outset of the business.

But I must acknowledge that it is better to have strong national laws and good governance generally, particularly in the economy. The rapid rise in corporate governance regulation in recent years has been, at least in one sense, an attempt to eliminate ambiguities and to create a way for companies to consistently demonstrate, in a measurable way, that they adhere to the rules that are set for their industries.

Good corporate governance, whether it comes historically, by regulation or by principle, is a good thing to have and, in times of crisis, can result in companies being given the benefit of the doubt. If people know that you have been forthright throughout, and you then encounter some financial difficulties, you will have much more credibility when you explain those difficulties.

Corporate governance systems are, even at the leading edge, not etched in stone and far from foolproof. Corporate governance is going to be a moving target and no system is ever going to cover all the bases. Principles, therefore, are what I always come back to. They are always what is going to be most important.

Sun Life Financial is in the business of managing a lot of money—about US$320 billion worldwide. About $110 billion of that is life insurance money and the balance, over $200 billion, is client money. When you have that amount of money, you really care about corporate governance because you are putting money at risk with the hope that the financial statements you are looking at are reliable and sound.

In America—Sun Life Financial is listed on the New York Stock Exchange—we have to comply now with the Sarbanes Oxley rules. A lot of them are foolish, I believe. Sarbanes Oxley is, in part, a political response to the wrong problem.

The US stock market fell because it was overvalued. It fell because there was a technology bubble. And yet politicians have basically treated the problems of Enron and Worldcom as if they were the main factor in the decline. When you read the press in America it always focuses on the evil things that happen in corporate governance, as opposed to the simple fact that the market was excessively valued. The pre-Sarbanes Oxley rules, if followed, would have been sufficient to solve existing problems. In fact, today's corporate criminals—who indeed committed fraud in many of those cases—are probably going to be judged guilty under the older laws and will suffer the appropriate consequences. I do not think we needed anything quite like Sarbanes Oxley. What we need is the will to enforce rules and, I believe, to have better corporate governance generally in the community and a stronger sense of ethics.

Session 3 Speakers:

George Tahija
President Director, PT Austindo Nusantara Jaya, Jakarta

George Tahija describes the challenges of trying to manage a transparent organisation in an opaque community. He also lists the reasons why many Asian family businesses do not see the benefits of corporate governance. Those that do, however, will ultimately become "society's partner of choice".

I represent a family business from a developing country. That does not seem like a great combination for corporate governance after what I have heard this morning, but maybe there are some exceptions!

We have a reason for being, a family philosophy as to why we are in business and what our objectives are. It is our belief that the fortunes of the community that we live and work in are inextricably linked with the fortunes of our business. If the community does well, we will do well. If the community suffers, we too will suffer. We feel that we have to be an asset to the society, not a liability, and I think the Asian crisis was example enough of what happens when the interests of the few override the interests of the many.

The crisis and its effect in Indonesia was not a result of globalisation. For the most part it was caused by irresponsible capitalism that thrived in a corrupt environment. Given the philosophy that we have, we set about establishing a set of values and a mission for the corporation to ensure that our philosophy was carried out in day-to-day operations. Our core values are integrity, respect for people and continual improvement.

When a business is small, it is relatively easy to communicate these things. But as the business grows and the number of employees increases, it becomes more difficult. So we asked PT. Dunamis Intermaster, a local licence holder from the Franklin Covey Institute in Indonesia to put together workshops, which we call "value workshops", where each of our core values is studied, and supportive or unsupportive behaviour is defined as it pertains to those individual values. We also have case studies that cater to our different businesses, so that employees have some sense of connection with what we are talking about.

Trying to manage a transparent organisation in an opaque community is quite difficult, but it can be done provided there is an alignment between the values of the individuals and those of the corporation. When there is not alignment, that is where there is a problem. That is the function of our workshops and, as you can imagine, it has an impact on recruitment because the best way to solve a problem is not to have it in the first place. So we are going to change the way our recruitment process works to make sure that, for the most part, everybody coming into the group will have the same values as we do.

In travelling around the country and talking about corporate governance, the language is becoming more and more complex (with different terms and jargon). I prefer to tell our people, "Just remember three things. The first is tell the truth, don't lie. The second is keep your promises. Do not promise anything you do not want to, or cannot, deliver. And the third is be fair." We are a multicultural society and I feel these principles transcend time, culture, religion and race. I think that telling the truth has the same meaning in China, Canada and Indonesia.

Why governance lags in Asia

In recent years, particularly after the Asian crisis, the term "corporate governance" has become much better recognised and frequently used, but the practice of corporate governance still lags far behind. One of the reasons is the legal system. Without a good legal system, corporate governance flounders. Another reason is that in family businesses generally, the majority owner is the founder and old habits die slowly. "Family comes first" is still the motto, even if the company goes public.

In the last few years in Indonesia, and other countries around us, governments have brought in numerous new regulations to enhance corporate governance. Listed family businesses are required to comply with these regulations in order to maintain their listing, but for the most part compliance remains a reactive measure to regulatory pressure, rather than something that is voluntarily adopted based on its merits.

For the foreseeable future, I believe that the dominant force pushing corporate governance is still going to be external forces and third-party pressure, rather than internal appreciation, for a variety of reasons. The compensation system focusses people on short-term gains. A lot of family businesses really do not see the benefits of corporate governance. They say, "What is the bottom line? I cannot see the benefits." And in developing countries a level playing field does not often exist. Often it is the ones who follow the rules that are penalised.

I think, over time, there will be better appreciation. Somebody said the second generation, who are educated in the West, are coming back. I think this generation has a better appreciation and understanding, but it is going to take time and it will take real examples of people who have succeeded through practising good governance to convince most people.

Eight years ago our company took an historic move—at least for us. We published an annual report with all our financials. We are a private company, we did not have to do that, but we wanted to make a statement. It was an important signal to all our staff that we intended to run a transparent, professional organisation and we expected them to behave accordingly. I still do not know if there are many privately held companies that publish their accounts in my country. So, while I am optimistic that family businesses will intensify their efforts in corporate governance, the practice is seen as an optional commitment—there really is no consequence, strong consequence, for not doing it. If the legal environment is weak, and there is no consequence, then it is up to each family to decide whether they think it is worth it or not. But I believe that those who choose to practise good corporate governance will be better positioned for long-term growth because, ultimately, they will become society's partner of choice.

In closing, I was recently in a meeting in Manila on corporate social responsibility and an eminent gentleman, Washington Sycip, commented that in developing countries businesses often had to partner with government in nation building. I think if we—the private sector, family businesses—are going to take part in such a noble cause, then we should behave accordingly.

Gary Coull
Executive Chairman, CLSA Asia-Pacific Markets, Hong Kong

Taking Mark Twain as his starting point, Gary Coull asks whether most business success today isn't based on some degree of dishonesty? To expand the scope for business success through honesty, he suggests educating people to be honest from the start and to recognise their wider responsibilities within society and to their various stakeholder groups.

The two speakers before me have both touched very seriously on corporate governance. I am not going to be unserious, but I want to try and take a slightly different look at it in my 10 minutes.

When you read about corporate governance over the last three or four years, it is normally about the relationship between the investor and the company. That is probably the most tangible and, for most people, the most important relationship. But actually the management and boards of most companies have much broader corporate governance responsibilities.

I think good corporate governance boils down to fundamentally honest behaviour. If you better understand the broader corporate governance links that you have as an executive or director of an organisation, it might be possible to set up a framework to monitor at all different levels what your honest responsibilities are to the constituencies in your "corporate governance wheel".

I am just going to run through a couple of quick slides and make that general point more laboriously in the next five minutes.

"Honesty, the Key to Corporate Governance", this is a slide with a couple of quotes from Mark Twain:

- "Honesty is the best policy when there is money in it".

- "Honesty, the best of all lost arts"—he was also a cynic!
- "All my life I have been honest, comparably honest. I could never use money I had not made honestly. I could only lend it."

Dishonesty and business success

You could argue that fundamentally most business is, in a sense, dishonest. This is a rather provocative statement for a banker and a businessman, but to be successful in business you have to find an edge. You have to find something, either earlier or differently, that your competitors have not found. And a lot of companies and entrepreneurs take that to the widest possible margin in order to be successful. Hence, you could argue that successful business, in its very essence, has an element of dishonesty about it. But what you want to find in an ideal world are successful businesses where the principles and practices of management and governance are as honest as possible.

For example, who here thinks that Microsoft is an honest company? This is a fabulously successful company, but the Supreme Court of the US, all its competitors and many people feel that at one time or another it has abused its effective monopoly in some form—which I think most people would say is a little bit dishonest. Microsoft is not a good example of corporate governance on about 10 or 15 different levels. It is a good example of how to make money and of how you have to push the edges of honesty in order to be successful in business.

What about the big US investment banks? Are these honest businesses? Eliot Spitzer does not seem to think so. He has fined them more than a billion US dollars. I am in that camp as well, so I am going to say that they probably are honest businesses. But there are excesses on the side. Greed and dishonesty have pushed these businesses into profitable areas, but also into questionable legal, moral and corporate governance areas as well.

Let's go to the next slide. The notion of honesty, the Western icons of honesty. If you are an American, you might think of George Washington ("I cannot tell a lie"), or honest Abraham Lincoln. You have a kind of simplistic notion, an unrealistic notion of honesty—"I can never tell a lie." Yet fundamentally in the West, you have that belief. Is that really embodied in business? Are companies really honest, at all levels, in how they relate to their customers, their competitors and their counterparties in the corporate governance world? I do not think they are.

Next slide: Asian concepts of honesty. If you are Chinese, or read Chinese, you will probably be able to get this more than me, but the characters read: "Honesty, genuine and true", "Loyalty from the heart", "Frankness, open and full", "Integrity", "Morally correct". There is nothing inherently dishonest about business in Asia. We have in Asia the same moral principles and definitions of honesty that companies in America or Europe have. The great Confucius commented that if you put the honest in positions of power and discarded the dishonest, you forced the dishonest to become honest.

I think at the heart of the corporate governance debate is something not talked about enough—and that is the fundamental concept of honesty and decency. That may sound rather simplistic and too basic to mean anything, but in fact it is fundamental because no legislation in the US was able to prevent the excesses of the technology crash—the Enrons and the Worldcoms. No regulator is going to be able to completely govern bad corporate governance, any more than laws against murder can totally stop murder.

So it is a cultural and an ethical issue. You have to raise people not to be murderers and robbers. You have to educate people to be good, honest corporate citizens and to recognise the interactive responsibility they have as an individual within society—and if they are business people, within their companies and society at large.

The corporate governance wheel

The next slide will introduce a very basic "corporate governance wheel". In the centre of a company is management and I think there are at least 10 main counterparties that management has to relate to on corporate governance, including: solicitors, media, suppliers, investors, employees, society, bankers, customers, accountants and regulators. There are a few more, and you could group one or two together. If managers and business people think of themselves as having these responsibilities in one form or another, at one time or another, at one level or another, through the course of their business year, and that they have an obligation to act in an ethical, responsible and honest way to those 10 entities, then you would start to have a fundamental change in the approach to corporate governance—it would be from the bottom up. Then you could begin building sustainable relationships and sustainable behaviour, instead of having to rely on regulators to tell us, "You can't do this, and you can't do that", because that is only going to be as successful as laws are against murder or robbery.

The next slide is an internal corporate governance issue, which also does not get talked about enough in my view: the relationship between a board and a company. Company management has a responsibility upwardly in corporate governance terms to be transparent, to be accurate and honest with the board of directors. The board has a responsibility down to the management to be clear, have vision and give empowerment to the executives.

This leads to my final slide, which is an abbreviated wheel, where a board of directors itself has a different set of corporate governance relationships. The board has a relationship with society as a whole and with accountants, regulators and investors. This is another level where a company can double check itself in relation to vested related parties and its corporate governance relations.

Our company is not at this stage yet—we are not a public company—but we are going to put more emphasis on this in 2004 and try to identify people in our organisation who will be responsible for our company against all these constituents at a board level and also at an executive level. And to make sure, even if it is just ad-hoc in the first year, that someone is thinking, "Are we touching all the basic points of honesty, decency and ethics within the bounds of law with each of these constituencies?". Hopefully, we will build in our group, from the bottom up, a better and deeper understanding of corporate governance, and what we ourselves promote. Our company is quite big in promoting corporate governance rankings that are very investor related.

My purpose in these brief minutes today is to try and broaden that debate to a wider group of stakeholders.

QUESTIONS & ANSWERS

Questions and comments from delegates covered the following issues:

- Will the second generation of family managers really be more trustworthy in Indonesia?
- Translating principles into action—how do you make good governance happen?
- How is CLSA practising good governance?
- How does CLSA manage the potential conflict between broking and investment banking?
- Dealing with forces of resistance to corporate governance.
- Can we expect at-risk ethnic groups, such as the Chinese in Indonesia, to fully respect other people's property?
- Should Asian companies draw inspiration from European governance models?
- In parts of Asia, ethical companies are often penalised for their honesty.
- Why aren't banks driving corporate governance more in Asia?
- The future shape of corporate governance reform in Asia.

QUESTION: I have a question related to family succession for George Tahija. In Indonesia, the family founder of a company almost always passes control to the second generation, rather than to outsiders. I was curious as to why you are optimistic about the second generation after they take control of the family business. If the institutional environment in Indonesia has not changed much, if you have to deal with a corrupt government, why should we expect the better-educated second generation to successfully practise better corporate governance?

GEORGE TAHIJA: This issue of corporate governance and whether the family business adopts it or not. It is about a way of life and a matter of choice. At present in Indonesia, if you want to borrow a lot of money from a bank and do not pay it back, you can actually get away with it. If you borrow a little bit of money, you won't (get away with it). But you borrow a lot and you can.

Why are there grounds for optimism? Because looking at some of my colleagues, I can see they are operating and thinking in a different way to the first generation. There are not a lot of them, but there are some and there are signs that give me confidence that there will be some more in future.

What is the impetus for change as long as the institutions remain weak? It takes a long time for institutions to grow strong. You have to have a very powerful "civil society" before the institutions will carry out their obligations; and we are talking decades—15 or 20 years. Indonesia has all the institutions, but they never had a chance to develop under the Suharto government, because it was a one-man show. But our civil society is getting stronger. People are speaking out, we are embracing democracy, the press is much more free. So I am optimistic, but I am not saying it is going to happen in five years. I am saying look at 15, 20 years from now.

QUESTION: Gary Coull spoke about honesty being the core value and everything centering on honesty and ethics. George Tahija spoke about the impetus or the incentives to adopt corporate governance. But what does it take to actually make it happen? What does it take to embody corporate governance in your entire organisation? Is it just statements at the top level? Is it guiding principles and vision? Or does it actually take something within your company to make it happen? What has been your experience?

GEORGE TAHIJA: You have to lead by example. People will follow what the boss does and that is the key. Senior management has to embody the values, which is why in our value workshops the trainers are all senior managers and they are responsible for making sure that every employee participates. Then you can ask, "Okay, they followed the workshop. They said, "Yes." They pinned it up on the wall. But are they going to put it into practise day by day?" That is when the tyre hits the ground and you have just got to lead by example. I do not know any other way.

GARY COULL: The first important point is leading from the top, but I think you can also do a number of other things. When recruiting new staff you should be trying to interview people who are on, for lack of a better description, "the honest side of the fence". Is it more important to be honest or to make money? How far would you go to make money? How far would you go to meet your budget—to the borderline of being in some way unethical or illegal? Are the principles that the company stands for enacted in the day-to-day operation of the business?

In our company, for example, one of the things we do is execute many millions and billions of dollars in stock trades. We do not trade around our customers. That is what I say to our customers and I make sure it does not happen through the organisation with a series of controls and measures, because that is a fundamental value for us. If I said that and no one checked that it was being done, then that would be an example of where we were not living up to our principles. So I think measures can be mechanical as well as being policy and statements.

JAMES PRIEUR: I think that is right. The first time your staff sees you standing behind your principles during an awkward situation is when it really sinks home with most of them.

QUESTION: Mr Coull, how are you incorporating better governance within CLSA? Are you following best practice ideas? Are you appointing independent directors to your board? Do you have any plans to do that? Are you setting up audit committees or compensation committees? Are you going on training courses? Are you sending your staff on training courses? What are you actually doing to implement it?

GARY COULL: A very fair question. The first thing is we are not a public company, so the ability to have outsiders in our company is a little more constrained than it would be for a public company, which has an obligation to share.

I think the research work that we do in our ranking of companies we also apply to ourselves. We try and see whether we are living up to some of those stakeholder issues that I spoke about. Are we where I outlined today? No.

We have a set of core beliefs as to how the business should be operated, which is very different to the way most American investment banks work—and it was different before the problems arose in the US. In our businesses—investment banking, broking, private equity—we have a clear set of principles on which we conduct seminars and training sessions. We give frequent reminders through compliance, through audit and through management to ensure that they are adhered to.

We also try, in the course of recruiting people, to deal with the issue of whether a person is going to fundamentally be within the bounds or not, because we are in a trading business where people can cause a lot of damage if they are not consistent.

I think we need to do a lot more. This came home to me when I was producing the corporate governance wheel, because there are people—counterparties—that I realised we had not actually thought of before and that we do not do enough with. So I have learnt something from my own talk.

That was a nasty question as well, by the way!

QUESTION: My question is to Gary Coull. How do you separate stock broking and investment banking where both of the departments, most of the time, have a conflict of interest?

GARY COULL: The policy that we have taken, the core value that we have taken, is that we are on the side, basically, of investors. Although we do investment banking business, and we may raise money through placements for companies that we have buy recommendations on, we do only a few. We don't try to make most of our money from raising capital for companies, because you can either do that or you can be independent and honest in the research that you do. I am not saying a research note from us is better than a Goldman Sach's note, but it comes from a different direction. The business that we do is 60% or 70% related to the brokerage business and only 10% or 15% related to the banking business. Banking is an ancillary business, rather than a driver. The conflict is when 30% or 40% of revenue comes from both and one wants the upper hand.

American investment banks—although they would say they stand for independent research—get 6% to 7% of the capital raised in an IPO, which is still a huge amount of money in this so-called liberalised age of financial intermediation. Whereas in the execution side of stock broking, for every million shares you get a nickel a share, which is almost impossible to break even on. So America has a very biased approach towards companies and it now has a more, I suppose, independent approach towards research, which will be a better model going forward. But the US comes from a very different perspective to us. We come from the point of view of investors, so if our investment banking business is not making money or is not dominating our business, that would not bother me.

There is a conflict between the two businesses, but it is about how you run them. It is about how important one is relative to the other. Our analysts do not get rewarded for investment banking deals. They never have. So it is quite different.

QUESTION: I have a question for the two panellists on forces of resistance. To George Tahija I would ask: Indonesia has had some more highly publicised cases of courts going the wrong way. The tax court routinely overrules the tax bureau—which leads to some scepticism about the latter—and you must confront this from time to time. I wonder, to the extent that you are willing to share, what are the sorts of approaches that you can take to this problem?

And then to Gary Coull: CLSA was heroic in some of its publications, but you get resistance as well from some of those organisations and from some of the countries that do not like your ratings. And yet you are continuing to do it.

So if the two of you could just touch on the forces of resistance to corporate governance in the cultures in which you operate?

GEORGE TAHIJA: Yes, the best way to avoid them is try to participate in businesses where there is the least contact with government and government contracts. For example, if you are doing business such as selling palm oil, you have your own plantation and you sell to the open market, so there is really no contact with the government. In consumer finance, we lend money to the consumer, so I think you avoid a lot of these problems by not dealing with the government.

With regard to an earlier question about the rent-seeking society, if you try to expand your business based on your contacts with government officials then of course you are inviting problems. So it is best just to avoid that. The consequence is that your business will not grow as fast as your competitors, but that is a choice one makes.

GARY COULL: Our interest in corporate governance started after 1997, when the Asian crisis threw up some appalling examples of corporate behaviour in Thailand, Indonesia, Malaysia and Korea, to name a few countries. In those days it was easy to pick off corporate governance offenders and, if you did it, you were not particularly chastised. But in the last couple of years people have started to realise that there is money in corporate governance.

If you do all the things that have been talked about this morning and the things we have recommended—some of our reports deal with very basic issues such as transparency and honesty within the market place—you actually get a better rating, so there is money in corporate governance.

Now when you criticise someone for lacking in corporate governance, as we do in our polls and rankings, it suddenly becomes a big deal. Companies take business away from us, they deny access to our analysts. I don't know whether "heroic" is the right word, but certainly "unprofitable" has been our experience with corporate governance rankings. Although we generally do it to raise the profile of the issue in Asia, it has been an unprofitable exercise for us, which is the reason I encouraged ACGA to join CLSA in jointly producing these rankings. That way the heat is a little bit off us and a little bit more on them!

GEORGE TAHIJA: Just a quick comment on the forces of resistance. I think the investment banks and the banking community can assist a lot in improving corporate governance standards because, prior to the Asian crisis, investment banks and commercial banks were driven by pure greed and completely forgot the "C" that stood for "character" in the "five C's of lending". They were just driven by income from fees. It was odd, because you often had a very transparent and ethical fund-raising exercise overseas, but then this money was used to fund a morally and ethically flawed project. And it kept on going because the intermediary did not practise sound judgement.

QUESTION: A question for George Tahija. If we look at corporate governance, especially in Southeast Asia, aren't we overlooking a crucial point, namely that most economic activity is concentrated disproportionately in the hands of minority groups? How can you expect people —I am talking about Overseas Chinese—whose property is continually at risk to respect other people's property when it comes to corporate governance?

Obviously, prudent risk management in those situations would stipulate that you load up on loans from government banks and hopefully equity from politically influential people, so that you can walk away if the worst comes to the worst and in the next ethnic expropriation, riot or whatever, they take away your property. I have probably overstated the case, but there is something to that.

GEORGE TAHIJA: There is some truth in what you say, but in this effort to develop mutual trust, it has to start somewhere. Somebody has to take the first step, otherwise it will never end. I think people who use that (cultural or ethnic conflict) as an excuse are overstating it.

QUESTION: Almost all the speakers have been taking a very American perspective on family owned businesses. I would just like to point out an observation that family owned companies into the fifth and sixth generations dominate the business environment in Germany and Italy (and, to a lesser extent, in Switzerland), while state-owned businesses constitute a very large proportion of the economy in France and a few other countries. So these are not situations particularly unique to Asia. I was wondering, Mr Tahija, when you were developing your training programmes for your family owned business, did you look at all at the regulatory environments in, say, continental Europe for inspiration? Or were you more focussed on the US or the British concept (of corporate governance), which lies somewhere in-between?

GEORGE TAHIJA: We didn't look at any particular model. We just had a firm belief that it was possible to do business honestly and we focussed on developing a programme to help our employees understand what our three core values were. As I said, I think these are principles that transcend everything: time, culture and religion. We just said, "This is what we want. Help us develop a programme that will cascade the values throughout the organisation."

QUESTION: Mr Tahija, at one point during your talk you almost got sidetracked by a story about being disadvantaged by being too careful about your ethics. Is that a story you can share with us?

GEORGE TAHIJA: It is quite a simple story. We used to own a majority shareholding of a bank, which we luckily sold before the crisis came. I was on the audit committee of the bank and we always made a point of disclosing our non-performing assets. As it turned out, our non-performing assets as a percentage of the performing ones always turned out to be higher than our competitors. We knew that that was not the case, but the analysts and the public market took it as such, so we were always rated less well. And why were the others able to get away with it? Because you can essentially compromise whatever you want.

JAMES PRIEUR: Even in North America, it is interesting how corporate governance can be turned on its head to become something you have to worry about. Some people are turning the current focus on corporate governance to their own advantage. For example, in response to a drive by the SEC to have investors reveal how they vote on every proxy, the union movement is trying to influence people who might have pension fund contracts with them. They want to get involved on a vote-by-vote basis.

QUESTION: I have a question for the whole panel. We hear a lot about how investors and regulators are driving corporate governance, but the one stakeholder we do not hear a lot about is banks. Why aren't the banks driving corporate governance? They certainly have a lot at stake when they are lending to corporations. Are banks really an active stakeholder?

GARY COULL: I think that is a good point. In the Asian Corporate Governance Association we do not have banks flooding in the door trying to be members. We have insurance companies, we have investors, we have a few brokers, but in fact the banks don't join. I don't know why that is, because when you buy stock in a public company you can sell its shares if you don't like its corporate governance. But when you have lent a company a lot of money, it is not that easy to get out if you find a problem. You can sell down the loans, but the syndication market in Asia is a little thin and you cannot always get out. I think bankers in particular are a group that should be more vocal about corporate governance, and also more active in groups like ACGA to promote it.

I suppose one other thing is the effect of collateral. Most of the time banks view their lending only as a financial transaction, where their risk is attached to assets. They only really get stuck in a big crisis like in 1997, when the assets collapsed and even good quality credits were going down in places like Korea and Thailand. But I think you are right, banks are under-active in this area.

I would just add one more thing: a lot of the American banks not only do commercial lending, they are also in investment banking. So I guess if the commercial side was too loud about corporate governance, they would be criticised by the other side of the house. That is kind of an obvious comment.

COMMENT: I think one reason why banks are not active in corporate governance is that increasingly in recent years, at least in the US, you have the business of syndicated loans. One lead bank would do a US$100m loan and then parcel it out to the juniors—the regional banks, the smaller banks and so on. They collect a nice fee, but they certainly do not feel a responsibility to look into things deeper. If it was $100m of their own money and not syndicated out, they probably would pay more attention.

I feel that it is up to the regulators, and particularly the institutional investors, to ask sharper questions of banks as to what they are doing in the field of corporate governance and what due diligence they are do as they extend credit lines. I always say that investment bankers have to bear a much deeper responsibility—and it is possible. I have known people, particularly in the private placement area, who have said to companies, "Well, there are certain practices you have that we don't feel very comfortable with. If you would do x, y, z to improve them, then we will try to do the private placement for you." That is often quite effective and I do hope that investment bankers, even in their public placements, will play that role as well. As for the regulatory authorities, they really should look even deeper into the behaviour of investment bankers, what they do when they place shares and how they arrange those deals.

JAMES PRIEUR: That's a very interesting comment. I think insurance companies care because they are always investing for a long period of time, so you have an exposure that also lasts for a long time. Banks are frequently lending against short-term assets and will very quickly cut off a company and liquidate short-term assets. Therefore, they are not as concerned about developing a long-term, viable capital market, whereas insurers are leaning that way all the time.

GARY COULL: Just to add to the previous comments, and as I mentioned before—this may sound a little cynical—but I think there is actually money in corporate governance today. If you present companies properly, if they are organised correctly, as a banker, as a vendor of shares, or if you own a company, you are going to get better prices and have a better after-market PE if you appear in the first instance to adhere to those corporate governance principles that we have been discussing today. And you will continue to have that rating by remaining faithful to those principles on an ongoing basis.

My impression over the last five years of surveying companies in Asia is that, in general, the awareness level is now very high. Hence my point that there is money in corporate governance. We have a view at the moment that a lot of companies are "faking it". They are going through the motions, but they don't actually believe it—which is why I have tried to talk a little bit about the fundamental issue of honesty today.

In our private equity business, I think we have done 11 deals in the past couple of years. We take the public corporate governance rankings and apply them to private companies—their average score was only about 36%. One of the things we have tried to do with our investee companies is to raise their score. After one year we try and get them into the 50% to 60% zone, and after two years into the 60% to 80% band, so as to prepare them for public listing and future investment.

There is a lot of work being done, maybe not from the right moral point of view, but because there is money in it for a lot of bankers and promoters, they want to get their company looking right. At least that is better than it used to be. I hope that is not too cynical.

QUESTION: I have a question about the future of corporate governance in Asia. I wonder if the members of the panel could each talk about different parts of the region. Suppose you moved out of Asia and came back in three years, what are the most dramatic corporate governance changes or improvements you would like to see? May I ask Gary Coull to comment on Hong Kong and China; George Tahija on Indonesia; and maybe Jim Prieur on Asia in general.

GARY COULL: That's a good question. Hong Kong and China are totally different, so you probably have to divorce them. I think in China, on the regulatory side, there is still a lot of room for improvement in the consistency of regulation and how that is applied to companies. In the banking sector at the moment there has been a huge increase in the seniority and quality of people involved in banking regulation in China. This will go a long way towards improving the corporate governance of Chinese banks, which has been pretty unimpressive to say the least. But it is changing very rapidly and the high quality of regulators going into the banking sector would be one example of a recent change.

If I was going away and coming back, I probably would like to see the quality of those regulators spread over a wider range of industries in China. There is still a lot of inconsistency in terms of how rules and regulations are applied.

The thing in Hong Kong I would really like to see is better behaviour on the part of private, family owned companies and their publicly listed vehicles. If you are a public company in a certain sector, I think you have an obligation to do that business only through the public company. So if you are a Hong Kong property company, for example, even if you have wide family interests, you should not have private property interests outside your public property company. Hong Kong is the biggest violator of that principle. It is not a law. It is just that I think there is a conflict. I would really like to see, not only in Hong Kong but in Asia in general, outlawing families running private and public businesses in parallel. This would be a huge step towards better corporate governance.

GEORGE TAHIJA: For me, it would be equitable and consistent enforcement by the courts. As long as the judges can be compromised there will be no change.

JAMES PRIEUR: Greater transparency in state-owned enterprises (SOEs) in China is something I would like to see happen. I agree with Gary about the Chinese banking system. Appointing Liu Mingkang[34] as a regulator is a huge step forward—he is a man with a record of fixing things. Right now nobody believes the financial statements of the SOEs and that is a fundamental problem. Corporate governance could really have a huge impact in Asia.

In America you have always had rules and some transparency. Sure there are people cheating on the side, but it is difficult to imagine how you could create a good public market for securities when people are so sceptical and cynical about all the financial statements they read. When you read the annual reports of some Asian companies, you sometimes discover that they bought something early in the year and sold it to another family-owned company later in the year without any real notion of what the true value should be. You have to ask: Was there an independent committee that helped set the values? As someone who is primarily a Western investor, it is just terrifying. I mean, one cannot imagine wanting to put money into that kind of situation.

[34] Liu Mingkang is the first Chairman of the China Banking Regulatory Commission, a new banking regulator established in China in early 2003.

Session 4: Thinking Strategically about Governance

Moderator:

Douglas Pearce
Chief Executive Officer/Chief Operating Officer
British Columbia Investment Management Corporation, Canada

Douglas Pearce speaks about the modern malady of the "faceless investor" and what can be done about it. He suggests that pension funds develop a strategic corporate governance policy that represents the values and beliefs of their beneficiaries—and then communicate this to companies.

Where shall we begin looking at corporate governance strategically? And why has it become increasingly important?

I think there are three reasons. First, institutional investors can no longer easily avoid or sell stock when companies pursue a course of action that is not in the best interests of shareholders. Second, companies today are accessing capital and selling their products globally. Third, globalisation is forcing international standards and a global set of values. We have spoken a lot about values today and I am going to come back to that.

In my mind a large part of corporate governance is about communication and engagement across many cultures and market places. It is not only communication between companies and investors, but how investors communicate with companies—and we need significant improvement here.

I will speak about what I call the "faceless investor". When we look at what Ko-Yung Tung said earlier about the gatekeepers at Enron, I have to ask where were we, the investors? There has been a lot of debate about how this communication should occur, its tone, and how prescriptive it should be.

To digress a little, the debate in Canada is between the principles-based universe and a word-based universe. Like Jim Prieur, I am hoping in Canada that we come back to a more principles-based set of fundamental values and guidelines. Yes, we need to have some rules, but let's go light on them. We also understand that one size doesn't fit all. We have set up a bunch of rules, but in multiple markets and cultures you have issues with translation and rules that hardly apply in those various, different market places.

Know your clients, know their values

The starting point for why we need to communicate about corporate governance is that it fundamentally speaks to today's reality about the nature of capital formation. Our firm manages capital on behalf of about 400,000 individuals who regularly place part of their income in a pension fund. These individuals don't have the time, skills or economies of scale to properly manage these monies or be active in corporate governance. We have become their agents and it is incumbent upon us, as agents, to meet the task that has been in place for decades—to know your clients and know their clients, know their risk tolerance, the asset classes and the investment strategies they are interested in and, just as importantly, know their values and beliefs. Our job is to maximise the returns of the fund, but not in isolation of the clients' values and beliefs.

What do we mean by these beliefs? In the pensions context the most fundamental goal is to invest in the best interests of each of the funds we manage. In pursuing this we often develop a set of investment statements and principles for each plan and each client. In these statements we usually begin by talking about their beliefs and philosophies.

What do we mean here? One example may be a statement saying that the more information we have that is timely, truthful and complete, then the better decisions we will make. Another may be that well-managed companies that consider all their stakeholders should perform better over the longer term.

There are also some unwritten beliefs that are no less important. One of them is that pension funds don't want to be embarrassed by scandals or events that erode trust. We have heard about trust all day and it keeps coming back into this discussion. Clearly we were embarrassed by our positions in Enron and some other companies, and that trickled up to the trustees and out to the 400,000 stakeholders for whom we manage assets.

It comes down to this word "trust". When we invest in a company, we have expectations that the management and board of directors will take care of our capital, grow it, and exercise a high standard of fiduciary duty. Part of that is continuous reporting on the health and prospects of the company in a truthful and complete manner. When this is not forthcoming on a voluntary basis, investors need to take action—and society puts in place guidelines, regulations and rules and, yes, we have had to introduce and initiate class-action suits. We don't like doing this; it is timely and costly. But that is part of our role.

One thing we do is set a corporate governance policy. We believe this is very strategic, because it speaks to and should reinforce the fundamental beliefs and values of our pension plans. Today institutional investors are far more important, not only because of their size in the market place, but also due to the nature of the formation of their capital. We represent the values and beliefs of these pensioners.

Rebuilding the lost ownership link

When we look at developed capital markets around the world, we see companies can raise capital in a number of different markets and shares trade constantly. Investors are basically faceless. Companies don't know their owners or to whom they are responsible; they only know there is a collective group of shareholders out there. We have lost an historic linkage—whether it was through the family investor or local communities—between the investor-owner and the board and management. This is why I believe it is strategically important for investors to communicate with companies as owners and convey their beliefs, values and objectives.

We also recognise that boards of directors, who we hope are independent and objective, will need to consider other stakeholders' views. But until we investors communicate with boards about how we expect our voices to be heard, how can we expect to be heard when there is management, employee and community interests that are far more audible?

What should we do to fill this gap? Number one: institutional investors need to publish. We post our corporate governance and proxy voting rules and guidelines on our website. We annually publish a complete list of all the companies we invest in. We try to privately meet and engage companies with whom we have issues—we don't like to debate these issues in front of the media. We participate in industry forums such as this and try to convey to the marketplace a consistent message from all investors. In Canada we have a new organisation, the Coalition for Good Corporate Governance, and this is the first time we have linked institutional pension investment with mutual fund investors and fund money managers. It is one consistent voice. We have published corporate governance guidelines and done something similar to CLSA, by rating companies within Canada on their corporate governance. So we participate.

Finally, to highlight the difference between what Bob Storer does in Alaska and what we do. From Victoria, BC, we vote all our holdings in North America and most of our international holdings. It is a consistent policy, and it doesn't matter whether we have external fund managers, we vote based on our policy.

Session 4 Speakers:

Varun Bery
Managing Director, Telecom Venture Group, Hong Kong

Varun Bery argues the benefits of taking controlling stakes in investee companies if you really want to improve their governance, then describes his reporting "food chain".

Most of you probably don't know much about the Telecom Venture Group (TVG), but we have been in business in the Asia-Pacific region for about 10 years. We have roughly US$600m in assets under management and have made 20 investments across the region in developed and emerging markets. We have been in all kinds of partnerships with institutions and families around Asia, and also state-owned enterprises in China. In terms of the spectrum of governance, I think we have seen a good range.

With private equity, by definition, we have an activist investment agenda. In fact the documentation for our fund is pretty explicit. We are not permitted to buy passive stakes on the open market in publicly listed companies. Our investors expect an investment thesis every time we make an investment, and that requires getting involved with the company and creating value from where we went in to the point of exit. In that sense, I guess we can't be faceless. We have got to be there.

This leads to another point, which is that we cannot survive without good corporate governance. All our portfolio companies, except for one, are in countries other than our Hong Kong head office. We have a small location in Australia and the rest of our portfolio is spread out. We make it our business to be able to manage by remote control through having good governance systems. We visit every portfolio company pretty frequently, but we are not in a shoulder-to-shoulder position with the top management, so we have to rely on corporate governance mechanisms to achieve our mission.

As has been said in different forms today, good governance in investee companies is a great strategy. If investee companies are good about practising reporting and other forms of governance, they become popular with bankers. That makes it much easier to access both debt and equity markets. Also, as strategic buyers in our businesses look to come into the region, they are extremely encouraged by companies with transparent modes of management (where there is a clear paper trail for important decisions). So that is a non-negotiable when we go into new investments.

Another aspect of governance and strategy, and how they are connected, concerns investment policy. We seek potential partners with a history of good governance. When people have bad habits, they don't shake them easily. Companies and managements are on their best behaviour when they are looking for money, so our due diligence into their governance history tries to maximise the odds that such good behaviour will continue beyond the point of investment.

Good governance through control

We have gravitated to a model where TVG, or a group of like-minded investors, have a controlling stake in an investee company—most of the financial investors we deal with have the same interests as us, they need the same information flow. If we collectively have a controlling stake in a company, our interests are aligned on that point.

There are situations where we don't insist on control, but are clearly the largest equity holder or very close to the largest. For example, where you have an entrepreneurial management team that is professional and that recognises the value private equity brings. Or when a management team is not in a position to fund its upward growth, but respects the requirements for private equity and does what it can to attract and retain money from funds like our's.

We have also found that it is easier, in terms of imposing governance on companies, to focus on investee companies that have export-driven models. This is true even when we invest with families. Generally families that are looking to fund companies with an export model recognise they have a reputation to create and uphold in international markets. Whereas in their domestic market they are in a fishbowl, with probably sympathetic financial institutions that will rally to their side in times of trouble.

The reporting food chain

Moving on to things we do on the management and monitoring side, private equity is like a food chain. We need monthly information from our portfolio companies, and that template is quite similar to the sorts of things Doug Pearce and our limited partners both need. They in turn may have limited partners or a board that they need to respond to. We have in-house templates that we literally deposit on the desks of investee companies from day one. This is an area where our limited partners are not faceless—it is clear to us what their reporting requirements are (unlike in some other aspects of corporate governance where it is hard for limited partners that are invested across a range of funds to get involved).

In basic governance rights, there is usually a series of negative controls embodied in standard shareholder agreements that we have and, by necessity, these need to be incorporated also into the Articles of Association of investee companies. We generally participate, not only on the board, but also on the audit and remuneration committees.

The other thing we do is to offer standard toolkits on budgeting procedures and to train companies on how to bring capital projects to the board (including inculcating the concept of hurdle rates). You may be surprised, but some of these techniques can be new for management teams, even in some of the more developed parts of Asia. We also have toolkits on human resource incentive plans.

These are areas that portfolio companies generally do need a fair amount of help on.

Some concluding comments: In our experience, we have done better with investments where the company is basically well-governed, but may have some issues that need to be dealt with on the management or the market side, rather than vice versa. That is to say, if at the beginning of an investment a company looks well-positioned, but the controlling family views private equity as a vendor of capital rather than a partner, there is a much higher likelihood that everything is going to end in tears; as opposed to a situation where the management and other shareholders embrace us as partners and, even though there may be market or management issues, we can work through those together.

Having been in this region for over 10 years, it is clear that investee companies have recognised the value of good governance in both public and private markets. With regional trends towards more entrepreneurial start-ups in areas like outsourcing, people recognise that to attract private capital it is very valuable to be able to demonstrate that you have good governance systems in place.

V-Nee Yeh
Chairman, Hsin Chong Construction, Hong Kong
Co-founder, Value Partners, Hong Kong

Despite taking the radical step of removing all executive directors from his board, V-Nee Yeh questions whether today's corporate governance prescriptions are more fad than substance? Getting your "corporate culture" right, putting in place good risk management and treating all stakeholders fairly is paramount.

I wear two hats, as an investor with Value Partners and the other as a controlling shareholder with Hsin Chong Group.

Value Partners is a boutique fund management firm founded in 1993 by me and my partner Cheah Cheng Hye, and is focussed on value investing in Asia. We started with US$3m. Today we manage about US$1.5 billion, still focussing on value investing and, in some cases, on distressed situations. We have always looked at small-cap companies and, being of a value mode, have been very dependent on qualitative assessments of management teams, how they perform and what we thought of their integrity. That has given us some insights and experiences, which have been painful at times.

My other hat is with my family-controlled company, the Hsin Chong group, which has two public companies. Hsin Chong Construction is involved in construction, while Synergis is a property management and facilities management business. I will highlight two points on how we have dealt with corporate governance in these two companies.

Synergis went public last week and I think we are the first public company in Hong Kong to have a chairman who is a non-executive director. He is a retired professor from one of the leading universities in Hong Kong.

The board of Hsin Chong originally had a balance of independent and executive directors, but about a month ago we asked all the executive directors to resign except for the managing director. The reason had nothing to do with their competency or performance, but with our philosophy. After taking advice from my independent directors, we decided that the board's function was to monitor, while the management's function was to manage. By having executives on the board you are, in a way, asking them to be both judge and jury, and I do not think that is logically consistent. The board now consists of five independent directors, one non-executive director (who is a family member), myself as chairman and the managing director. I think only then can the board be an impartial and effective monitor, and not biased by its own management decisions. Executive directors on a board will always tend to be biased, because, after all, the reason the company performs in a particular way is due to their decisions.

As far as thinking strategically, Varun Bery has touched on how an investor would look at it. I would like to touch on how a controlling shareholder would look at corporate governance.

Think about substance first

Do we at Hsin Chong or Synergis think about corporate governance as it is defined today? I must say we don't. We have thought about the substance of corporate governance for a long time, but we never phrased it that way. We think about "what is the most desirable corporate culture or mindset within a company?" That should be the logical starting point, because the principle beneficiary of any corporate culture or mentality should be the company itself. That to me, ultimately, is what corporate governance should be about.

Having defined it that way, we think the best corporate mentality for us, the best corporate culture, is one which has the most effective risk management procedures and fair treatment of all stakeholders, including employees, business partners, shareholders and bankers or financing institutions. I find the recent corporate governance focus, which talks principally about minority shareholders and listed companies, is a little misdirected. The starting point for corporate governance should be what kind of corporate culture should a company adopt, regardless of whether you are listed or not, because the principle beneficiary—as I said—should be the company itself. What kind of procedures do you have in place? What kind of risk management or treatment of your stakeholders do you have?

The only change with being a listed company is that you have added a new category of stakeholders, that is the minority shareholders. If you believe a publicly listed company should have a certain set of corporate governance procedures that a private company doesn't need, then are all these new, or more rigorous, sets of corporate governance procedures simply there to protect minority shareholders? If you think about it that way, then some of the inconsistencies may be apparent. We need to differentiate between what is cosmetic and what is substantive; between what is really effective and what could be perceived as part of a fad.

This is the way we looked at how Hsin Chong and Synergis should approach corporate governance. It is in terms of how we best put in a corporate culture and mindset, which is most effective in a risk management sense and produces the most equitable treatment to all the stakeholders.

QUESTIONS & ANSWERS

Questions and comments from delegates covered the following issues:

- Is the view that governance is a good strategy widespread?
- How can companies, especially non-listed ones, best assess their own governance standards?
- How difficult is it for private-equity funds to find potential Asian investee companies with a history of good governance?
- How important is disclosure of individual director compensation?
- While some see the corporate governance debate in Asia as too focussed on minority shareholders, isn't this in part a practical proxy for wider governance issues?
- What is best corporate governance culture?
- Despite the constant criticism of form over substance in the corporate governance debate, it is important to recognise that "form" can play an important role in shaping substance.
- One reason why finding independent directors is so hard is that companies employ advisors who over-specify what is required.
- Despite an alleged shortage of independent directors in Hong Kong, a recent survey has found that very few companies employ women or younger men as directors.
- Is a direct approach to companies more effective than public criticism?
- Should more companies in Hong Kong rapidly increase the proportion of independent directors on their boards?

DOUGLAS PEARCE: I would like start off this Q&A by asking the two panellists a question. In your experience, how widespread is the belief that governance is a good strategy in each of your industries?

VARUN BERY: If you look at private equity fund management, the entire investment thesis has evolved from minority stakes in family-owned companies or pre-IPO type stakes to control/buy-out models. That isn't exclusively the case, but if you look at where the money is going, that is the direction in which it is headed. I think the governance requirements imposed by these fund managers are every bit as rigorous, if not more rigorous, than they have been in the past.

I think all the publicity on the various scandals in the US is having a ripple effect on boards throughout Asia. Even private company boards are thinking much harder now about governance than they did before. Our D&O[35] insurance has gone up!

Let me toss in one brief digression. Governance is probably the most important thing we look for in making an investment, but it is also important to remember that in our business it is a 'necessary, but not sufficient' condition. You also need talented management, the ability to influence your investment and to have a management that is willing to listen to you. You need all of those things to make a successful investment.

V-NEE YEH: If you are looking at it from a construction or property management viewpoint, these are relatively small industries, especially property management, so I am not sure that it is very widespread.

Putting on my hat as a member of the listing committee of the Stock Exchange of Hong Kong, and looking at companies being listed and whose prospectuses are being vetted, I think people still see corporate governance

[35] Directors & Officers insurance

largely as a requirement to list, as part of a regulatory burden, and that is unfortunate. They don't seem to appreciate that if you believe in good corporate governance, and it becomes a culture that permeates through all the layers of management down to the staff, the principal beneficiary is the company itself. Because as things become more transparent, you have better risk management procedures and the company as a whole is better managed.

Take for example an audit committee. Regardless of whether you are public or private, having an audit committee means better internal risk controls. If a private company can persuade people from different fields of expertise to serve on the board, they can provide the company a lot of insights.

All these things are commonsensical, but it seems a lot of the focus today is on cosmetics rather than on substance. It is rather like bringing up a child and inculcating in him or her the idea of good manners. Basically, good manners mean that you are sensitive to other people's concerns and approaches. With corporate governance today, it is as if you have teenage children and you have never taught them manners or consideration for people, and you are taking them out to dinner. Now all of a sudden you tell them about etiquette. They may be able to go through the actions, but they won't really understand why. You cannot expect to teach and inculcate consideration into your children in a year or two if you haven't done it for the last 15 years. People must appreciate that it takes a long time to change a mindset, to develop a culture.

QUESTION: I totally share your concerns about listed and non-listed companies. The gap between these two groups, I am afraid, is going to get broader in terms of good corporate governance practice. What sort of benchmarking in terms of self-assessment would you advise? What do you expect for those non-listed companies, be they family-owned, partnerships or something else? Also, what do you expect from international organisations in terms of promoting the self-assessment of the non-listed companies, so as to avoid a gap in terms of corporate governance practices?

V-NEE YEH: What I hope would be the message from various organisations is that the principle beneficiary of good corporate governance is the corporation itself. Sometimes the message says, "If you have good corporate governance people trust you, so you will have high evaluations", and that is like dressing yourself up to go to the ball. It is like dressing yourself up for sale, because you want to attract private equity. Regardless of a high valuation or not, if you have good corporate governance, you should have better risk controls, better operational efficiencies and probably better staff morale, because things are more transparent within the company. People don't see family hierarchies or nepotism in there and it makes for a stronger company.

QUESTION: Varun Bery, you said that when you look for partners you look for a partner with a history of good corporate governance. How difficult is it to find a partner with that kind of history in Asia? And, when you think you have found one, how good is their governance really? Do you find a lot of form and not a lot of substance? And that to get the governance you are looking for is sometimes like pushing water uphill? What kind of struggles do you experience?

VARUN BERY: That's a great question and I do think this is an area where things in Asia have evolved for the better. When we started 10 years back, in a lot of countries, including places like India and a lot of the Southeast Asian countries, you had single families that were involved in a whole range of businesses and were able to eke out a living or survive in all of them.

With WTO being accepted in a number of these countries, that is no longer the case. You are starting to get companies that need to be specialised, or families that need to become more focussed on what they are good at. When we looked for partners in the old days, some of the family-owned enterprises had the attitude, "whether we get your money or not, we are going to be successful anyway". I don't think that same arrogance exists today.

You asked what are we looking for? These days we are looking for situations where outside investors have made money with the family or partner before. You don't want to be the first one in and have to figure out for yourself whether the party you have chosen is going to allow you to make money. From our experience, the most painful aspect of our business is when an investee company does well but you don't get your share of the upside. That is a situation you absolutely want to avoid.

What you are looking for is that track record of others having made money with the partner that you have selected. If you do due diligence in this more modern, competitive environment, generally there aren't as many surprises once you approach the partner. There are tough negotiations for shareholder agreements, but at the end of the day when they sign an agreement they understand what it means.

QUESTION: Mr Yeh, wearing your stock exchange hat, how important do you think it is for companies in Hong Kong to disclose specifically their executive compensation levels? In recent months CLP Holdings has gone the extra distance and started to release exact figures for its executives, but there seems to be quite a lot of resistance to this. Do you think this is important, and why or why not?

V-NEE YEH: Personally, I do not think it is that important. I can see from a company's viewpoint that if you disclose executive remuneration packages by name, you run a higher risk of them being lured away. The converse is, "people always know who to headhunt anyhow". But I know from my own experience that it can happen.

There have been some egregious cases where controlling shareholders have paid themselves very large salaries, even when their company was loss-making. But I am not so sure that disclosure would have added anything, because everybody knew who these shareholders were. You already have disclosure in "bands" and have to state how many directors are in a certain band.

In the really egregious cases you can pretty much surmise which directors are being paid what amount. As a consequence, these companies trade very cheaply and people remain sceptical. I am not sure disclosure adds much. Putting on my investor's hat, I think additional transparency for investors is good. But I can also see the other side of the argument and, on balance, I would tend to say you should not need to disclose remuneration packages.

QUESTION: V-Nee, you said you are concerned about the corporate governance debate being too focussed on minority shareholders, but isn't the treatment of minority shareholders in a sense a proxy for the entire governance of a company? In other words, if you treat your minorities well, you are probably more likely to treat all your stakeholders well and, conversely, if you treat your minorities badly, you may well treat your other stakeholders badly. So in a way the two issues are linked and that speaks to Gary Coull's "corporate governance wheel". When we talk about minorities, we are not necessarily only focussing on minorities. It is just that we as corporate governance activists need to get a grip on something, and that is something tangible you can talk about. It is not that we are not concerned about all the other issues in running a company.

V-NEE YEH: That is a fair comment. As I said earlier, I think corporate governance is really about a company's culture. Once you have set your corporate culture and mindset, it becomes part of the company's character. And these character traits are applicable in all situations, whether in dealing with minority shareholders, suppliers, joint venture partners or employees.

On the issue of minorities, I think in some instances minorities have been very vocal when something goes wrong. But sometimes fund managers make wrong investment decisions—and we should try not to blame the company for it. Sometimes it is we who have not done sufficient due diligence. Let's say you buy in and the company does a big share issue that dilutes everybody equally. That has nothing to do with minority abuse, fraud or anything. It has nothing to do with conflict of interest. It is that we haven't done our due diligence properly. The management may have made a wrong business decision, but that is different from not protecting minority rights. As long as there is no conflict, you should only blame yourself. You assessed management's competency incorrectly.

QUESTION: I would like the panellists to comment on some live case examples of what constitutes best corporate culture. I ask that question because I absolutely agree with Mr Yeh that central to corporate governance is how you grow a corporate culture. There is a globalisation of standards today and one of the key issues is executive pay. On the one hand, you can understand that in some of the more developed economies CEOs have become too greedy and there has to be a redressing of the balance. But there is also an argument for making private and state-owned enterprises as well as family listed companies more accountable. Maybe developing a corporate governance culture is at the heart of the issue.

VARUN BERY: The example that comes to my mind was a situation where the company had some trouble on the business side. It was in the difficult cellular business of an emerging market and in the initial days prices were too high, take-up rates weren't what we expected, so the company was behind in its business plan. It was a partnership with a family-owned business, but as it had aspirations overseas it was very keen to build an international reputation—and the family thought expansively about that. In the early days, there were a lot of families in emerging markets that we dealt with who saw our involvement as a zero-sum game—and consequently they tried to reduce our share of the pie. But these people thought about growing the pie. What really helped us all in this difficult market, and made a successful and winning investment out of it, was that there was a sense of partnership. There was complete disclosure of what was going on, and open and frank discussions about the problems we faced.

The points you raised about executive compensation and related items were issues that we discussed. There were three of us acting as partners: a local partner, a strategic partner and a financial partner. In situations like that it is important to tailor a solution that is suited to the local market. There are certain markets that are just not ready for the stock culture, and the market I am talking about wasn't. Yet, to pull the company out of the difficult market situation it was in, we went and hired the best talent available and paid the person a very attractive compensation by local standards. I think that if you have good information systems, and you have a consultative culture between the shareholders, it makes a huge difference in terms of governance and the eventual success of the business.

It turned out that we improved the fortunes of the company. We collectively decided that a sale of the business was right and we managed to exit the investment at the height of the telecoms boom.

I can give you plenty of other examples of where things can go wrong. For example, it is very hard to get a controlling shareholder to sell if you are not the controlling shareholder. But here was a situation where we were all on the same side, looking to maximise value for shareholders as a unit, and it worked wonders.

V-NEE YEH: I am somewhat conflicted, because I am a shareholder in the company I will use as my case study. This is a company not listed in Hong Kong, but in Singapore. It was a company that was taken private, then re-listed and, at first, the chairman and managing director were the same person. It is involved tangentially in the commodity trading business, so risk management controls are very important. After it was re-listed, there was one substantial shareholder in there—not myself—who was not part of the management. They formed a very strong risk management committee. After a couple of years, the independent director became the non-executive chairman and the other shareholder became the managing director. They made an exceedingly good, well thought out business plan and handled the Asian financial crisis very well. The company grew. So financially it is a success.

This to me is an example of good corporate governance procedure and, from the viewpoint of risk management, I think they would have done it regardless of any minority shareholders. They didn't do any share placings or anything. It was simply that because the ultimate beneficiaries were themselves, they managed to sail through the Asian financial crisis and the various liquidity squeezes relatively unscathed. That is the best corporate governance example I can think of.

DOUGLAS PEARCE: Maybe I will jump in with another perspective to this. I think it comes back to communication and how consistent that communication is through meetings, annual reports, websites and how transparent it is. In North America we have gone through a transition where we put a lot of trust in boards of directors that have failed us. So we are a bit sceptical and we want to see for ourselves what is happening in the company. How do we evaluate the boards of directors if, again, this information isn't reported to us? We are looking for this transparency. We are looking for executive compensation. We are looking for the company to communicate to us how well it is doing compared to best-practice guidelines on governance. We want them to commit.

Somebody said earlier that when you have to sign a quarterly or annual report, these internal controls make you think. We would like to see that.

I will pose a different question: in North America it is getting increasingly hard to find good board members, to find the independents with the skill sets you want. How is it in Asia? Is there any educational programme for directors?

VARUN BERY: Because of economic and other considerations, we haven't used independent directors much when a company is truly private. In the lead up to becoming a public company, obviously we get in independent directors and a year or so prior to listing we will install them.

To date it has not been difficult, because there are people who are well recognised in the countries they work in, and who are willing to play the role. But I think what people have read in the press—about the implications of being on boards that don't discharge their responsibilities the way they are supposed to—has caused people to become more careful about the boards they sit on. Believe it or not, D&O insurance is not a standard thing in a number of countries. We have invested in companies that did not have D&O policies. But now directors expect that insurance.

We don't have an explicit independent director training programme, but generally the people that we bring onto our boards will have been directors in companies of repute. In interviewing them we get a sense of whether they can effectively discharge their responsibilities.

V-NEE YEH: In Hong Kong it is getting increasingly difficult to find good independent directors. The responsibilities of independent directors are much greater and people are less willing to take the role on. For example, if I was looking for an independent director, I could find a lot of people who would come in, be very rigorous and take almost an adversarial approach. They see their principle duty as complying with regulations. But if I already run a clean company, one with a culture for integrity—and where I know I comply with all the regulations and do not try to take advantage of anybody—having such people as independent directors adds very little to my company. Conversely, companies that are crooked will not invite police to sit on their boards. They will invite crooks to sit on their boards.

A clean company already has a detailed regulatory regime, so the moment an independent joins the board all they try to do is to tick the boxes. They are so concerned about their own liability, and making sure you fulfil the legalistic form, that there is very little value being added. They are not trying to voice a different opinion or think about how to help you manage the business or develop company strategy. They are just there to tick the boxes.

I feel that the pendulum is swinging to an increasing amount of regulation and duties. You have more and more committees, which are all concerned with the cosmetics of governance. I find it very difficult to find independent directors who will come in with a view to helping the company as a whole, instead of just making sure the company complies with rules and regulations.

COMMENT: I would like to challenge that view. In architecture there is a saying that "form follows function", and I think you have that in corporate governance as well. Form is very important and I think behaviour sometimes follows form.

I'd like to pick up on your metaphor about teaching teenagers about how to use their knives and forks. Unfortunately, that is the business we are in here sometimes. There are companies that are 50 or 100 years old in Asia and we are the first ones coming in and teaching them about good governance. But they are not teenagers, they are adults. Fundamentally I agree with you when you say that the culture is most important. If you are taught how to use a knife and fork the night before you get engaged, then you may do well at the party but you probably would not understand the purpose of the party. And I think it is important to understand the purpose.

But I wouldn't underestimate the importance of form, especially in a crisis situation—whether it's the Asian financial crisis or a business crisis. When people are acting under pressure, it is helpful to have the form and the institutions in place. I think that is sometimes what keeps a company together.

COMMENT: I'd like to add a comment on the difficulty of finding independent directors. I have sat on a number of committees to help companies find directors, particularly in North America in the past, and the biggest problem I see is not a lack of talent. If people were going after what V-Nee had mentioned—that is, people who could actually add value to the operation of the company—there is no shortage.

The real problem is that a lot of the professionals advising boards are setting out a list of very specific criteria. "We want a director who has been a director of another NYSE listed company for so many years". "We want a director who has been in the industry for 20 years". "We want a director…". By the time you add up all of these supposed minimum standards it makes it extremely difficult to find the right candidate.

The problem that I see with corporate governance in being applied to Asia is that these same advisors come in, sit with a company, charge a large fee and they say, "If you find a director with this, this and that criteria, he will be a good independent director." That is fine if you have got someone with a great resume. He is probably sitting on five or six other boards and is not going to have any time to look at the business. But the fact is a lot of younger talent in Asia is being missed out. People who could really make a very strong, positive contribution to the company are not being selected when it comes down to the final tallies on these committees. Much of the reason is because of a report from McKinsey or one of the accounting firms that says your candidate needs to have such-and-such qualifications. Well, sometimes you have to give people an opportunity to start to generate those qualifications, and that is what we seem to be lacking in the last couple of years here. People are going for the quality resume at the end of the day, rather than taking a gamble on someone who may be able to build and develop those qualities in the future.

DOUGLAS PEARCE: I think this is a good point that also applies to North America.

COMMENT: Just to follow up that last comment with some statistics. The Hong Kong Institute of Company Secretaries recently did a survey of independent directors on boards of Hong Kong companies and found that most were older men. There were very few people under the age of 40 on boards and almost no women. These are two sources of independent directors that potentially could solve some of the supply shortage in Hong Kong. And I think if you paid independent directors better, that might solve the rest of the shortage problem.

COMMENT: I think the previous delegate has touched a point that is not unique to Asia. In North America one half of the population—women—is overlooked. Even today in Fortune 500 companies, who are supposed to be leading lights, you still find that in most companies you might only have one woman. There are plenty of professional women who have strong managerial talent and experience, but they are overlooked because they don't belong to the old boys' network. This is particularly acute here in Asia. Yes, we have a shortage of independent directors defined by the traditional guidelines, but we certainly don't have a shortage of good, independent directors if you bother to get rid of those traditional guidelines and really look for talent.

However, I see some good signs in Asia because in China, Singapore and Hong Kong, for instance, many companies are pretty open in terms of recruiting independent directors who are non-citizens, even in financial institutions. Many of the regulators in Asia have the wisdom to say, "Well, maybe we could recruit some people from abroad to fill the gap for the time being."

QUESTION: A question for Doug Pearce: in your speech you mentioned that you would sometimes visit companies privately, rather than make a big public pronouncement about concerns. I was wondering if you could share with us whether you felt that that was an effective means of persuading them, because in some sense all you could do otherwise is sell their shares, right?

DOUGLAS PEARCE: I think it is the most effective way, rather than trying to have a debate through the media and have that voice somewhat tainted by the media. We found that having dialogue directly with companies, particularly if they have an issue or a resolution going forward that we disagree with, can often encourage them to remove or rethink the issue. As owners—and we are not going to be able to sell some of these companies totally—I think they appreciate that input early on, so having these meetings works well.

QUESTION: But ultimately the threat is that you oppose the resolution?

DOUGLAS PEARCE: Yes, absolutely.

QUESTION: V-Nee, you mentioned that in your new board for Hsin Chong Construction, there is only one executive director, the managing director. All others are non-executive or independent. This is more typical of American boards than Asian boards. Do you think other companies in Hong Kong should move in the direction of having a larger proportion of independent directors? And how much do you see the independent directors on your board? How much time do you expect them to give to your company, so that they have enough knowledge of the company and the industry to be really effective?

V-NEE YEH: In answer to your first question, we did it not because of any corporate governance but principally because our construction business was doing terribly and we were at a loss. After discussions with the independent directors, we felt that having the management, the executive directors, on the board meant there was a diffusion of responsibility and it was very hard to measure their performance as objectively as possible. That is why we asked most of the executives to resign from the board, leaving only the managing director on the board, because we felt then we could measure performance in a much tougher way. If a company with more executive directors on the board is doing very well, then perhaps you should leave it that way. This is why I say it is about what you think is best for your company.

To your second point about whether independent directors can really give time to a company. I have been very fortunate. This idea of asking the executives to remove themselves from the board came from an independent director who assured me that he would spend a lot of time on the company. We would have monthly meetings of our independent directors, who would closely examine and monitor management performance with the managing director, albeit informally, but also on a very rigorous monthly basis; and they were all willing to commit their time. Not all our independent directors are going to be meeting monthly, but we have a sufficient number who have given their personal commitment that they will do so. It was very difficult. If they had not given this commitment to me, then this re-juggling of the board would have been meaningless and totally cosmetic. And I would not have done it!

Conference Summary

Peter Sullivan
Chairman, Lombard Investments, Inc., San Francisco

I had the opportunity to present the closing remarks two years ago at the first "Asian Business Dialogue on Corporate Governance" (in Hong Kong in 2001). This session is much harder to try to summarise! I think this is because the depth and level of dialogue has become much greater this year.

Asia resurfaces and reforms

Today's session began with a presentation by the Asian Development Bank's Vice President Jin Liqun, former Vice Minister of Finance in China. In his keynote remarks Vice President Jin set the stage for the discussions that were to follow, with his own descriptions of the need for corporate governance, touching on the diverging goals and needs of shareholders, managers and regulators, and the asymmetries of information and the costs thereof. He noted the bottom-line value of corporate governance, demonstrating the premium that is placed on companies that practise good governance, a theme reiterated towards the end of the day by Varun Bery (Telecom Venture Group) in our last session. Incidentally, Mr Jin also reminded us that poor corporate governance, on the other hand, impacts not just the company involved but can dramatically affect a whole sector or even economy.

One of his comments particularly captured my attention: that Asia led the world in growth for some 30 years, from the 1960s to the mid-1990s, and yet for most of that time corporate governance wasn't even in the vocabulary of most Asians. As he said, he had read almost nowhere about corporate governance and it was certainly not a topic of discussion in Asia until the Asian economic crisis of 1997 and 1998.

Although that crisis was devastating for much of the region, it may have been a mixed blessing because it did reveal, as Mr Jin pointed out, the need for improvement in regulatory and supervisory systems in the banking and financial sectors; the need for improvement in the rule of law; the need for greater transparency in financial disclosure; and, for our purposes, the need for improvements in corporate governance at the company level and at the national level.

Today most Asian countries have recovered from the crisis and Asia, again, leads the world in growth. In fact, the IMF and the Asian Development Bank (ADB) project Asia this year will grow at about twice the rate of the world as a whole, and about six times faster than the European Union. Next year ADB and IMF project growth for Asia ex-Japan of over 6%. And investors have seen this. There is now more foreign direct investment pouring into China than into the US. And this year, for the first time, there will be more foreign direct investment in Asia than in Europe. But this raises the question: have improvements in corporate governance kept pace with this remarkable growth? Can they keep pace? Our speakers today helped answer that question.

An uneven report card

Our first session was a report on the progress of corporate governance in Asia. Has it kept pace with growth? Where is it going? I think we learned from our speakers that there has, in fact, been considerable, though certainly uneven, progress. We received assessments on a number of countries.

Vincent Duhamel (State Street Global Advisors) touched on a few countries. We have seen progress in China, India, Korea, Malaysia and Singapore, and perhaps less so in Indonesia and the Philippines. Hong Kong is still in neutral, based on some of the comments that we have heard. But we also heard first-hand comments, in particular about Korea, India, Japan and, for that matter, the US and Canada.

Jinwon Park (Shin & Kim) pointed out the sea change in Korea since he attended his first board meeting as an independent director in 1997—an event he described so vividly as wholly lacking in corporate governance. He noted that there had been a multitude of new laws and regulations adopted in Korea in the last five or six years. But he was concerned that many of the reforms may, in fact, be form over substance. And there remain many areas for improvement, such as empowerment of boards of directors; empowerment of minority shareholders; making class-action suits possible; and, indeed, increasing the pool and training of capable independent directors.

Lalita Gupte (ICICI Bank) presented a very interesting case study, not so much of corporate governance itself, but of the difficulties an individual entity faces trying to improve its own corporate governance in India. She took us through the six years of moving ICICI from a development bank into a leading private-sector financial institution. Ms Gupte noted the changes that were required on all levels: voluntary policy decisions; meetings with employees, with clients, and with stakeholders. And, despite her comments on the painful transition ICICI went through, she showed how much progress could be made in a very difficult environment.

Later, in other sessions, George Tahija (PT Austindo) described similar pains in a different context for a family-owned corporation trying to develop good corporate governance in a very difficult environment in Indonesia. And Taiji Okusu (UBS Securities Japan) explained the recent changes in Japan's commercial code and the trend towards the new "company with committees" system. But he also reminded us that this has been a slow-moving process, that there are issues with the new system, and resistance from the old system.

Ko-Yung Tung (O'Melveny & Myers) reminded us that the recent corporate crisis in the US, including the scandals surrounding Enron and Tyco, has led to a new push in the US and elsewhere for further corporate governance reforms. He noted that the Sarbanes Oxley Act has further advanced the moving target of best practices for corporate governance; and that the impact of the Act on Asian companies and jurisdictions was very real. But he reminded us of some of the critical differences when trying to apply Western corporate governance concepts in Asia, including greater state ownership and the larger role of the family in corporations in this region, versus the greater role litigation plays in the US. Similar points about the greater role of state-owned corporations, family corporations, and the greater role of litigation in the West were reiterated by several speakers during the day, including Pote Videt, George Tahija and The Honourable Justice Jacobs.

The convergence conundrum

Another theme during the course of the day was raised by Ko-Yung when he noted that progress on corporate governance did not necessarily mean copying US, Canadian or British laws and regulations. Nor did standardisation or convergence of corporate governance practices necessarily equate to progress. And I must say I agree: too often Western laws and regulations have been enacted here in Asia without adaptation to local cultures and systems. To bring in a US law without the background of common law precedence, without a similar judicial system, and an understanding of how to enforce these laws, is not going to be effective. In fact, when we look at the codes of best practice that most Asian countries have adopted, some of them have to go far, far back into the system and raise issues that are taken for granted in the West, such as the need for financial disclosure, annual reports, or the one-share, one-vote concept.

We not only heard about corporate governance in Asian countries and the US, but we also heard from several Canadian speakers about Canada's approach to corporate governance—an interesting balancing of the prescriptive regulatory system in the US with the principles-based approach of the UK. It seems that many Asian countries are moving towards an Anglo-American version of corporate governance, rather than a European civil law-centred culture. But standards do have to be adapted, as I said, to Asian cultures. Lalita reminded us that there is pressure in India for convergence with US-UK rules and regulations, and that pressure is very real indeed.

Shareowner activism

In our second session, Pote Videt (Private Equity Thailand) reminded us of how Western-style corporate governance needs to be adapted to the cultures and legal systems of Asia. He also pointed out the difficulties and possibilities for a minority investor trying to make a difference, an issue that Varun Bery came back to later. Pote did outline an effective approach to long-term investment in a culture where confrontation is avoided and reliance on legal sanctions is not usually an option.

Taiji Okusu noted that Japanese financial institutions were still hostile to takeovers and confrontation, despite his own efforts to improve the situation. But he gave us some reassuring news that the picture was changing; that pension funds were becoming more vocal on corporate governance; that individuals were beginning to stand up; and that management, itself, was becoming more responsive.

Bob Storer (Alaska Permanent Fund) presented a very realistic and down-to-earth view of how many large institutional investors in North America deal with corporate governance issues. He outlined how the Alaska Permanent Fund (APF)—a very, very large fund—delegated its proxy rights to its asset managers and he noted, parenthetically, that some of these managers might not be able to vote the proxies delegated to them because of securities lending. Bob did note APF's recent decision to join the Council of Institutional Investors in the US and its likelihood of becoming more directly involved with its asset managers in future. I think his description probably reflects the common approach of most pension funds, rather than the more interventionist approach of the publicised few.

Company courts

Our luncheon speaker, the Honourable Justice Jack Jacobs, discussed the role of specialised company courts in promoting corporate governance. He revealed, by taking us through a number of cases like Van Gorkom, Caremark and Revlon, how court decisions in Delaware have profoundly and positively impacted corporate governance. Not just in the US, by the way, but internationally as well. He reminded us that both the corporate governance systems and the legal structures of the major Asian commercial centres were the products of history and value systems that were very different from the US, and that there were neither comparable specialised business courts in Asia, nor the typical resort to litigation which is the norm in the US for resolving business conflicts. The family-owned corporations of Asia create issues that are very different from those faced in large US corporations. But his concluding comments on the Daiwa case in Japan suggest that courts could play a positive role in promoting good corporate governance in Asia, too.

Stakeholder imperatives

Our third session dealt with stakeholder imperatives and how companies in Asia should respond to these new demands. They also brought some clear warnings that corporate governance, especially if narrowly focussed, is not a cure for all corporate problems. Jim Prieur (Sun Life) and later Doug Pearce (British Columbia Investment Management Corporation) described the Canadian approach, a mixture of rules and regulations on the one hand and principles and ethics, if you will, on the other. Jim, like others, noted that corporate governance was a moving target and that all improvements were not necessarily foolproof or positive. He reminded us that it may not be the Sarbanes Oxley legislation, but rather a healthy dose of realism and integrity, that provides us with better corporate governance.

George Tahija (PT Austindo) described the difficulties of trying to—and I loved his phrase—"manage a transparent corporation in an opaque community". He pointed out that if the playing field was not level, then those trying to play by the rules would suffer. And he reiterated the need for a functioning legal system if corporate governance was to be anything other than an optional commitment.

Gary Coull (CLSA) was the next speaker. I fully share the comments that were made, I think, by Jim, when introducing Gary—that CLSA having the courage to rate companies is an act of pure heroism. (I admire Gary for doing that, but I must admit I was petrified when he started asking for a show of hands regarding who thinks various companies are honest. He asked about Microsoft. I was worried that he would ask about my own firm, Lombard Investments! Lombard, I feel certain, is an honest entity, but it is named after the crookedest street in San Francisco!) Gary painted an interesting picture of corporate governance wheels for both boards and managements, showing that both must deal with all stakeholders, ethically and honestly, as well as with each other.

Thinking strategically

Our final session dealt with thinking strategically about governance: how are companies and investors integrating corporate governance into their business strategies? Doug Pearce chaired that section and began by asking, "why corporate governance now?" And, as part of his own answer, he pointed out that one of the large parts of corporate governance was communication, including communication to investor communities and companies. He said that British Columbia had learned that, to be effective, a pension fund must know what its clients wanted and what their values and beliefs were. And as an investor, it must know relevant information about its investee companies and enforce its right to know. But in today's environment much of that communication linkage has been lost, he said.

Doug also made some good points on how a fund like the British Columbia Investment Management Corporation could reconstruct that chain of communication, and he pointed out that they did so by publishing rules and guidelines; by meeting companies where necessary when issues had arisen; by participating in meetings and seminars like the one we are at today; by having the courage to rate companies, as CLSA does; and, in its case, by voting all its holdings, at least in North America.

Varun Bery (Telecom Venture Group) articulated well why corporate governance was important to a private equity firm. He noted that a private equity firm simply couldn't function without good corporate governance because of the distance and management problems that it faces. He pointed out that, as a venture investor, he participated, or his firm participated, on boards and various board committees of investee companies. He pointed out that TVG usually sought a controlling stake, either by itself or with other investors, except in specific cases where there was a true entrepreneurial team that he had faith in. (My own firm, Lombard, doesn't necessarily seek a controlling stake, but we try to deal with these issues through veto rights and other shareholder rights. But I think the point is clear that these kinds of protections are necessary for equity investors.) Varun's ultimate conclusion, I think, was the lesson that corporate governance was probably the most important factor in successful investments—and much more critical than many of the other management issues we might face.

V-Nee Yeh (Hsin Chong) raised some interesting points at the end that probably could have set us off on a new day of discussions. He started by describing arrangements in a company to free the board of executive directors, allowing the board to monitor and management to manage. But then he raised the argument as to whether good governance should be viewed as just instilling a corporate culture of risk management and fairness, rather than strong emphasis on protecting the rights of minority shareholders? The principle beneficiary of corporate governance, he noted, should be the company itself, and perhaps that brings us right back to Vincent Duhamel's earlier comment that good corporate governance is really good risk management.

As a last comment, reflecting on the discussions we have had today, I am struck by the fact that corporate governance has, indeed, come a long way in a very few years in Asia. We are no longer spending time at a conference like this discussing what corporate governance is, and we are not arguing any more whether it is necessary or valuable. Instead, we seem to be focussing on differences and approaches to corporate governance and how to provide the legal, institutional and stakeholder support to move it forward within the various cultural and political environments in Asia.

The issue we now face is to ensure that that progress continues. That reforms are more than just form over substance. That they do enhance shareholder value, improve the companies involved and benefit all shareholders. Thus, while it seems that corporate governance has come a long way in Asia, it still has a long way to go. We are chasing a moving target, but I don't think that is necessarily a bad thing.

SPEAKER BIOGRAPHIES

VARUN BERY
MANAGING DIRECTOR
TELECOM VENTURE GROUP

Mr. Bery is a co-founder and Managing Director of Telecom Venture Group Limited, a private equity firm that invests in the communications industry in the Asia-Pacific region. Mr. Bery has been involved with the communications business as both a financial/strategic advisor and as an equity investor. He currently serves on the Board of Directors of several Asian communications companies including CNK Telecommunications of China, Suntel of Sri Lanka, SpeedCast of Hong Kong, Saehan Enertech and Initech, both of South Korea.

Mr. Bery was formerly Director of Telecommunications at the Asian Infrastructure Fund (AIF) in Hong Kong. Prior to joining AIF, Mr. Bery was Director of Investment Banking in the Telecommunications Group at Credit Suisse First Boston (CSFB) in New York. Mr. Bery started his career as a management consultant with McKinsey & Company in New York and Tokyo.

Mr. Bery graduated with a BA degree from Yale University. Mr. Bery also received a Masters in Business Administration from Harvard Business School. Mr. Bery currently serves on the Executive Committee of the Hong Kong Venture Capital Association.

STEPHEN JULIAN BLASINA
SENIOR VICE PRESIDENT
SPECIALTY INSURANCE MANAGER, ASIA PACIFIC
CHUBB GROUP OF INSURANCE COMPANIES

Stephen J. Blasina, Bsc (University of New South Wales), MBA (Australian Graduate School of Management) is Senior Vice President of Federal Insurance Company.

Presently based in Singapore, Mr Blasina is responsible for 12 branches in the Asia Pacific region that offers financial liability products through Chubb's Executive Risk Department and the Department of Financial Institutions.

The Risk and Financial Institutions department offers a wide variety number of specialized executive protection and professional liability products for privately and publicly owned companies, financial institutions, professional firms and healthcare organizations.

Mr Blasina has been an active member of the Asian Corporate Governance Association since 2001 and participates in many forums and speaking engagements organized for the industry.

He joined the Australian operation of the Chubb Group of Companies in 1993 as its Regional Manager.

Prior to making a career in insurance, Mr Blasina was a Merchant Banker with Citibank of New York, USA.

GARY COULL
EXECUTIVE CHAIRMAN
CLSA LTD

Gary Coull is co-founder and Executive Chairman of CLSA Ltd., an award winning brokerage, investment banking and private equity group specialising in the markets of the Asia Pacific. CLSA, a unit of France's Credit Lyonnais banking group, has over 700 specialised emerging markets staff. The group is headquartered in Hong Kong and has a substantial staff ownership.

Mr. Coull was born and raised in Vancouver, Canada and graduated in 1976 from the University of British Columbia with a Bachelor of Arts degree. He was editor of the university newspaper, the Ubyssey, one of Canada's largest student publications and worked for the local professional daily newspaper group during his school days.

After university, Mr. Coull set out on a world tour that began in Europe and the Middle East and ended up, by chance, in Hong Kong in 1977. He began work on Hong Kong's leading English language daily newspaper, the South China Morning Post, covering China and local business news. In 1980 he joined the Far Eastern Economic Review, a weekly news magazine, as an assistant editor and continued to cover Asian business.

In 1983, Mr. Coull left journalism and undertook a variety of different business and investment projects, including business publishing, China trading and sourcing, and property investment. In 1987, he joined Hong Kong brokerage firm Winfull Laing and Cruickshank, a joint venture between an established Hong Kong financial family and the UK brokerage group. French bank Credit Lyonnais subsequently took over Laing, bought out Winfull and the platform was created for what became today's CLSA.

CLSA operated throughout the 1990s with a high degree of autonomy and a staff shareholding of 35%. During this period, the group expanded first into Southeast Asia, then North Asia and India. The group was also an early investor in the Chinese capital markets, providing macro research since 1990, being amongst the first to join the Shenzhen and Shanghai Stock Exchanges, and being involved in the very first equity fund raisings involving foreign investors. CLSA was No. 1 ranked for China Research for the entire decade. Regionally, CLSA grew from its equity research and brokerage base, Mr. Coull moved the group into corporate broking, investment banking, corporate advisory, mergers and private equity. Always known for its innovative research, CLSA has won numerous awards for its coverage of Asian economics, strategy and corporates. Also a leading proponent of better corporate governance, CLSA publishes an annual ranking of corporate governance rankings for Asian companies. CLSA is also known for its annual investor conference programme, widely regarded as the industry's best. The main conference is held in Hong Kong each May and is the world's largest emerging market investors forum. Each year it draws over 1,000 institutional investors, hundreds of senior corporate executives and speakers from Asia and around the world.

Mr. Coull is also Executive Chairman of CLSA's private equity group, whose investors include General Electric Pension Trust, Sony Life, Verizon Communications, the German insurance group Allianz and Credit Lyonnais. He is also a director of the Hong Kong publicly quoted New World Infrastructure; a governor of the Canadian Chamber of Commerce in Hong Kong; a director of the Asian Corporate Governance Association, a member of the Hong Kong Trade Development Council Financial Services Advisory Committee and a member of the Hong Kong Securities Institute Corporate Advisory Committee.

Mr. Coull is an avid golfer, scuba diver and keen racehorse owner and breeder.

VINCENT DUHAMEL, CFA
CHIEF EXECUTIVE - ASIA
STATE STREET GLOBAL ADVISORS ASIA LTD, HONG KONG

Mr. Duhamel is a Senior Principal and Chief Executive of State Street Global Advisors Asia Limited. He is responsible for all of State Street's investment management activities in Asia excluding Japan. He is also a member of the Senior Management Group of State Street Global Advisors (SSgA). Mr. Duhamel is a Governor of the Board of the Association for Investment Management and Research (AIMR), a member of the Korea Corporate Restructuring Fund Investment and Supervisory Committees, a member of Hong Kong's Securities & Futures Commission Shareholders Group and a member of the Advisory Group of the Hong Kong Securities Institute. Mr. Duhamel joined State Street Global Advisors (SSgA) in January 1993 as Managing Director and President of State Street Global Advisors Canada Limited. Before joining SSgA, he was Vice-President at Pictet International Management where he managed international portfolios in Montreal, Geneva and London. Prior to 1989, Mr. Duhamel worked at a leading Canadian Brokerage firm and at the Canadian Federal Government.

Mr. Duhamel holds a BA in Economics and Politics from the University of Ottawa and is a Chartered Financial Analyst.

LALITA D. GUPTE
JOINT MANAGING DIRECTOR
ICICI BANK LTD

Mrs. Gupte is the Joint Managing Director of ICICI Bank, the largest private sector bank in India, since May 2, 2002. Prior to that, Mrs. Gupte was the Joint Managing Director and Chief Operating Officer of the erstwhile ICICI Limited, which was India's leading financial institution before its merger with ICICI Bank in March 2002.

Mrs. Gupte has more than three decades of experience in the financial sector, beginning her career with the erstwhile ICICI Limited in 1971 in the project appraisal division. Since then she has held various leadership positions in areas of Leasing, Planning & Resources and Corporate Banking. Mrs. Gupte was appointed Executive Director, on the Board of Directors of the erstwhile ICICI Limited, in 1994 and subsequently Deputy Managing Director in 1996.

Mrs. Gupte was instrumental in transforming ICICI Bank from a primarily term lending institution into a technology led diversified financial services group with a strong presence in India's retail financial services market. Having established itself as a leader in the domestic market, ICICI Bank is now increasing its presence in international markets. Mrs. Gupte is at the helm of ICICI Bank's global foray, which includes operations in the USA, UK and United Arab Emirates, with operations soon to be set up in China and Singapore. She is responsible for ICICI Bank's international relationships and businesses in the retail, corporate and technology areas and for forging international alliances required for the domestic businesses.
ICICI Bank is today a technology and retail banking leader in India and in 2002 was named Best Managed Bank in Asia by Euromoney, Bank of the Year from the Emerging Markets by The Banker Magazine of UK, Excellence in Retail Banking by Asian Bankers' Journal and Best Bank in India and Best Trade Finance Bank in India, both by Global Finance.

Mrs. Gupte has received numerous awards during her career, including "The Woman of the Year Award" for 2002 presented by the International Women's Association for her achievements in the corporate world, "The 21st Century for Finance & Banking Award" by the Ladies' Wing of the Indian Merchants' Chamber (1997) and "Women Achievers' Award" from the Women Graduates Union (2001). In July 2003 in recognition of her outstanding achievement in the corporate world, Mrs. Gupte was awarded the "Most Influential Marathi Woman Award" by the Maharashtra Foundation of U.S.A.

In addition, Mrs. Gupte has been a member / chairperson of various expert groups. Currently, she is Chairperson of Women Empowerment Committee constituted by the Confederation of Indian Industry, the apex chamber of commerce of Indian industry. Prior to that, she has been a member of "The Expert Group on Foreign Exchange Markets in India" formed in November 1994 by the Reserve Bank of India and Chairperson of the "Confederation of Indian Industry - National Committee on E-Commerce".

Mrs. Gupte holds a Bachelor's Degree in Economics and a Master's degree in Business Management. Mrs. Gupte has two children and lives in Mumbai.

DOUGLAS HENCK
PRESIDENT
SUN LIFE FINANCIAL ASIA

Douglas Henck is President, Sun Life Financial Asia. In this capacity, he leads Sun Life Financial's development in all Asian markets. He joined Sun Life Financial on April 3, 2000 as Executive Vice President, Asian Operations, with overall management responsibility for Asian operations. Sun Life Financial, listed on the Toronto and New York Stock Exchanges among others, is a Fortune Global 500 financial services company offering insurance risk and wealth management products.

Prior to joining Sun Life Financial, Mr. Henck was Senior Vice President of the AIG Life Division of the American International Group. Based in Hong Kong, he was responsible for various strategic initiatives, such as merger & acquisition work and new country entries, as well as certain business line responsibilities and Asian country operations.

Mr. Henck moved to Hong Kong in January 1987, and established the Asia Regional office of the US-based Aetna Inc.; he remained as the senior executive in the region for the next ten years before he joined AIG. He first joined Aetna in 1974 after graduating with a B.S. Mathematics from Rensselaer Polytechnic Institute in New York. Mr. Henck qualified as a Fellow of the Society of Actuaries in 1978.

Mr. Henck is a Past Chairman of the American Chamber of Commerce in Hong Kong, having led the organization during the historic 1997 calendar year. He also served two terms as Chairman of the Asia Pacific Council of American Chambers of Commerce from 1993 – 1995. A frequent spokesman for American business interests, Mr. Henck testified before the U.S. Senate Foreign Relations Committee in 1996 and has appeared numerous times on local and international television as well as in print media. He serves as Vice Chairman of the Asian Corporate Governance Association.

JACK B. JACOBS
JUSTICE, SUPREME COURT OF DELAWARE, UNITED STATES

Before his appointment to the Supreme Court, Jack B. Jacobs served as Vice Chancellor of the Delaware Court of Chancery since October 1985, after having practiced corporate and business litigation in Wilmington, Delaware since 1968. Justice Jacobs holds an undergraduate degree from the University of Chicago (B.A., 1964, Phi Beta Kappa) and a law degree from Harvard University (LLB., 1967).

In addition to his judicial activities, Justice Jacobs serves as an Adjunct Professor of Law at the Widener University School of Law; a director of the American Judicature Society, and as a member of the American Law Institute, where he is an Advisor to its Restatement (Third) of Restitution. He is also a member of the Delaware and American Bar Associations (where he is a member of the Committee on Corporate Laws of the ABA Business Law Section). Justice Jacobs has authored several legal articles and participated in national symposia and programs related to corporate and securities law sponsored by various law schools and legal and Continuing Legal Education organizations, including the American Bar Association, ALI-ABA, and the Practising Law Institute.

Justice Jacobs has authored (or co-authored) several law review articles, including: "Function Over Form: A Reassessment of Standards of Review in Delaware Corporation Law," 56 Bus. Lawyer. 1287 (2001); "Realigning the Standard of Director Due Care with Public Policy," 96 N.W.L. Rev. 449 (2002); "The Great Takeover Debate: A Meditation of Bridging the Conceptual Divide," "69 U.Chi.L.Rev (2002); "Comments on Contestability," 54 U. Miami L. Rev. 847 (2000); 7 Del. J.Corp.L. 251 (1982); (Co-Author), "The New Delaware Director-Consent-To-Service Statute, 33 Bus. Lwyer. 701 (1978).

LIQUN JIN
VICE PRESIDENT
ASIAN DEVELOPMENT BANK

Mr. Liqun Jin was appointed Vice President for Operations Group 1 of the Asian Development Bank on 1 August 2003.

Mr. Jin had years of experience in the Ministry of Finance of the People's Republic of China (PRC) where he held several important posts including Director General of the World Bank Department in 1995 and then as Assistant Minister of Finance until his appointment as Vice Minister of Finance in 1998. As Vice Minister, Mr. Jin was mainly in charge of the budget for administrative expenses of education, science, culture and external economic affairs. He took charge of the supervision of PRC's financial sector and of raising funds from both international and domestic capital markets.

Mr. Jin also served as Alternate Executive Director for PRC at the World Bank Group from 1989 to 1992, and was involved in policy discussions on the World Bank's Development programs and deliberations on investment and structural adjustment loans for borrowing member countries.

Mr. Jin was born in Jiangsu Province, PRC in 1949. He graduated from the Beijing Foreign Studies University with an MA in English Literature in 1980. He was a Hubert Humphrey Fellow in the Economics Graduate Program in Boston University from 1987 to 1988. He is married and has a daughter.

Education

1988	BOSTON UNIVERSITY Hubert Humphrey Fellow, Economics, Graduate Program
1980	BEIJING FOREIGN LANGUAGES INSTITUTE M.A. in English Literature

Experience

2003-Present	ASIAN DEVELOPMENT BANK Vice President (Operations Group 1)	Manila, Philippines
1998-2003	MINISTRY OF FINANCE Vice Minister	Beijing, PRC
1995-1998	MINISTRY OF FINANCE Assistant Minister	Beijing, PRC

MR. LIQUN JIN (continued)

1995	MINISTRY OF FINANCE Director General, World Bank Department	Beijing, PRC
1993-1995	MINISTRY OF FINANCE Deputy Director General World Bank Department	Beijing, PRC
1989-1992	WORLD BANK Alternate Executive Director for PRC	Washington, D.C., USA
1985-1987	MINISTRY OF FINANCE Deputy Director World Bank Department	Beijing, PRC
1983-1985	MINISTRY OF FINANCE Section Chief World Bank Department	Beijing, PRC
1980-1982	WORLD BANK Staff Assistant Executive Director's Office for PRC	Washington, D.C., USA
1980	MINISTRY OF FINANCE Staff, External Finance Department	Beijing, PRC

Personal Information

Born in Changshu City, Jiangsu Province, PRC on 30 August 1949; married and has a daughter.

TAIJI OKUSU
MANAGING DIRECTOR & VICE CHAIRMAN
UBS SECURITIES JAPAN LTD

Education

Mar 1971	BA, University of Tokyo, Major: Law

Professional History

May 2000	UBS Securities Japan Ltd, Vice Chairman
Apr 1997	Schroders Japan Limited Joint Branch Manager & Head of Corporate Finance
Dec 1995	Morgan Stanley & Co. Incorporated Executive Director, Corporate Coverage Group
Jan 1991	Morgan Stanley & Co. Incorporated Executive Director – Investment Banking Division Corporate Finance Coverage
Mar 1988	Morgan Stanley & Co. Incorporated Executive Director – M&A Department – Tokyo
Apr 1987	Morgan Stanley & Co. Incorporated Vice President – M&A Department – New York
Jan 1985	Bankers Trust Co. (New York) Vice President – International Finance Department - Wholesale banking business
1982	The Sanwa Bank Ltd. Manager – International Finance Department, Tokyo Project Finance Group
1978	The Sanwa Bank Ltd. Seconded to Baring Sanwa Ltd, Hong Kong, a joint venture between The Sanwa Bank and Baring Brothers, which later became a wholly-owned subsidiary of The Sanwa Bank, Ltd.
1977	The Sanwa Bank, Tokyo. International Finance Department
1974	The Sanwa Bank, Tokyo. Corporate Finance Department
Apr 1971	The Sanwa Bank Ltd.

Mr. Okusu was born in September 1947.

JINWON PARK
SENIOR FOREIGN LEGAL CONSULTANT
SHIN & KIM, ATTORNEY-AT-LAW

Jinwon Park, Attorney-at-law, admitted, 1990, New York Bar (Not admitted in Korea). Currently Senior Foreign Legal Consultant at Shin & Kim (Since 1995).

Education: Seoul National University (B.A., 1970): Columbia University (M.Phil., International Economics, 1980); Brooklyn Law School (J.D., 1990). Lecturer, International Contracts, Ajou University Graduate School of International Studies (1999-2000).

Associate, Paul, Hastings, Janofsky & Walker, New York (1990-1993). Associate, Gibson, Dunn & Crutcher, New York (1993-1995).

Independent Director, Hanil Synthetic Fiber Corporation (1998-1999). Independent Director, Ileun Securities, Co. Ltd. (1998-1999). Independent Director, Sambu Construction Corporation (1998-2000). Independent Director, Hyundai Heavy Industries (2000). Commissioner (Non-Standing), Financial Supervisory Commission of the Republic of Korea (1999-2002). Board Member, Committee for the Reform of Corporate Governance (Korea Stock Exchange) (2002-present). Arbitration Commissioner, Arbitration Board under the Corporate Restructuring Promotion Law of 2001 (2002-present). Independent Director, GoodMorning-Shinhan Securities Corp. (2003.6-present).

Member, New York State and American Bar Association. Languages: English and Korean.

DOUGLAS PEARCE
CHIEF EXECUTIVE OFFICER/CHIEF INVESTMENT OFFICER
BRITISH COLUMBIA INVESTMENT MANAGEMENT CORPORATION

Mr. Pearce is the Chief Executive Officer and Chief Investment Officer of the British Columbia Investment Management Corporation (bcIMC).

(bcIMC) is a statutory company established in 1999 by the Province of British Columbia. The corporation is responsible for the investment of public sector pension funds, sinking funds and other trust funds in the Province of British Columbia. Total assets under administration are approximately $60 billion in a range of diversified assets, domestic and foreign.

Mr. Pearce is the Chairman of the Pacific Pension Institute based in San Francisco and a past director and chairman of the Pension Investment Association of Canada (PIAC). He is a member of the University of British Columbia Faculty of Commerce, Faculty Advisory Board and a member of the business council for the Global Asset and Wealth Management (GAWM) program of Simon Fraser University. More recently Mr. Pearce is pleased to be a founding board member of the Forum for Women Entrepreneurs, an education and networking venue for women entrepreneurs and investors.

Mr. Pearce is a graduate of the University of Calgary.

C. JAMES PRIEUR
PRESIDENT & CHIEF OPERATING OFFICER
SUN LIFE FINANCIAL

Jim Prieur graduated from College Militaire Royal de St. Jean and earned his MBA from the University of Western Ontario in 1975. He earned his Chartered Financial Analyst designation in 1982.

Mr. Prieur joined Sun Life in 1979 in the Private Placement section of the Investment Department in Montreal and subsequently worked as an equity analyst before becoming a portfolio manager of bonds, and then of equities. In 1985, Mr. Prieur became head of the Canadian Private Placement section and in 1988, was appointed vice president, Securities Investments for Canada.

In 1991, Mr. Prieur was appointed Vice-President, Investments in the Sun Life corporate office in Toronto. He transferred to the U.S. operations in September 1992 as Vice President, Investments. His appointment to Senior Vice President & General Manager for the United States Operation followed in 1997.

In April 1999, Mr. Prieur was appointed President & Chief Operating Officer. Mr. Prieur has overall responsibility for the organization's activities in the United States, Asia and Britain.

Mr. Prieur is affiliated with the Newton Wellesley Hospital on their Board of Overseers and is a Director of the Canadian Opera Company and LIMRA International.

ROBERT D. STORER
EXECUTIVE DIRECTOR
ALASKA PERMANENT FUND CORPORATION

Robert D. Storer was appointed to the position of Executive Director by the six-member Alaska Permanent Fund Corporation (APFC) Board of Trustees and began his duties as the Corporation's chief executive on February 16, 2000. The Executive Director oversees the management of the Fund and the daily operation of the Corporation, and acts as spokesperson for the Corporation along with the Board Chair.

Previously, in May 1983, Mr. Storer worked for the APFC for nine years as an Investment Officer. During that period he assisted the Chief Investment Officer in managing the marketable debt portfolio, provided oversight of corporate equity managers and assisted with strategic planning and supervised APFC portfolio managers.

He left the APFC in 1992 to accept the position of Chief Investment Officer for the State of Alaska Department of Revenue, Treasury Division. While there he was directly responsible for overseeing the management of 18 public funds, which during his tenure reached an aggregate value in excess of $19 billion.

PETER H. SULLIVAN
CHAIRMAN & CEO
LOMBARD INVESTMENTS, INC

Peter H. Sullivan is Chairman and Chief Executive Officer of Lombard Investments, Inc., a San Francisco-based private equity firm. He directs the overall international operations of Lombard and its various investment funds. Prior to joining Lombard, Mr. Sullivan served for more than 25 years with the Asian Development Bank (ADB). He was Vice-President of the ADB from 1994-2000.

Lombard and its affiliates invest in selected private equity transactions in the Asia-Pacific Region and in North America. Lombard has made equity investments in management buyouts, corporate acquisitions and expansion financings, generally in partnership with institutional investors. Lombard's current partnerships include the Lombard Asian Private Investment Company, LDC, formed by the ADB and Lombard to make equity investments in developing countries of Asia, and the Lombard Thailand Intermediate Fund, LLC, formed with the International Finance Corporation of the World Bank Group and the ADB, for the purpose of private equity investments in Thailand.

Mr. Sullivan held various management level positions during his 25-year career at the ADB, including Vice President (Region East), Vice President (Operations) and General Counsel. Mr. Sullivan was appointed as Vice President by the ADB's Board of Directors, representing its various member countries, in 1994, and was re-appointed by the Board as Ranking Vice President in 1999.

As Ranking Vice President and Vice President (East), Mr. Sullivan was responsible for supervising a lending program ranging from $3 billion to $7 billion per annum, and a technical assistance grant program of $75 million per annum, for the developing countries of East Asia (including the People's Republic of China, Indonesia, the Republic of Korea, Malaysia, and the Philippines), the Pacific, and Central Asia. He was also responsible for administering a loan portfolio of about $24 billion for those countries.

During the Asian currency crisis, Mr. Sullivan was actively involved in the IMF-led rescue packages and financial and corporate restructuring programs for Korea, the Philippines and Indonesia, and participated in the Manila Framework program (established by the U.S., Japan, other Pacific Rim nations, and the IMF, World Bank, and ADB) to address the financial and economic crisis. He also participated in the establishment of the Bank's Regional Economic Monitoring Program and its Good Governance and Anti-Corruption Policies, and chaired the task forces which developed the Bank's Poverty and Private Sector Policies. During his terms as Vice President, Mr. Sullivan was also responsible for overseeing all procurement and consultants contracts awarded or financed by the Bank, and all co-financing activities of the Bank.

Mr. Sullivan is currently an active member on the board of directors of a number of corporations and entities in the United States and Asia, including the Pacific Pension Institute, an organization established to assist pension funds, corporations and institutions worldwide to carry out their fiduciary duties, especially with respect to the Asia-Pacific region.

Mr. Sullivan began his business career as a lawyer with Sullivan & Cromwell. He received a Bachelor of Arts degree from the Woodrow Wilson School of Public and International Affairs, Princeton University, in 1967, and a Juris Doctor from Yale Law School in 1972. Mr. Sullivan is married and has one daughter.

GEORGE S. TAHIJA
PRESIDENT DIRECTOR
PT. AUSTINDO NUSANTARA JAYA (ANJ)

Mr. George S. Tahija is the President Director of ANJ and the Group's Chief Executive. He holds a B.Sc. in mechanical engineering and an MBA from the Darden School at the University of Virginia. He is responsible for planning, leading and developing the activities of the ANJ Group

PT. Austindo Nusantara Jaya (ANJ) is a private Indonesian company wholly owned by the Tahija family. It is the holding company for core investments in financial services, oil palm, gold and oil & gas

He is a member of the National Advisory Committee for the Indonesian Institute for Management Development, the Plenary Committee of the Trisakti University Foundation, the PSKD Mandiri School, the Board of Advisors of Centre for Strategic & International Studies and The Nature Conservancy (TNC).

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KO-YUNG TUNG
SENIOR PARTNER
O'MELVENY & MYERS LLP

KO-YUNG TUNG is Of Counsel in O'Melveny & Myers LLP's New York office. Returning to O'Melveny & Myers LLP in June 2003 after serving since 1999 as the Vice President and General Counsel of the World Bank and as Secretary General of the International Center for Settlement of Investment Disputes (ICSID), Ko-Yung practices in the international arena, representing the firm's clients in cross-border transactions. During his previous tenure with O'Melveny, he concentrated on mergers and acquisitions, investments and financings involving Japan and the Pacific Rim. With his experience at the World Bank and ICSID, Ko-Yung's practice is expanding to include matters involving sovereign debt, investments in developing countries, particularly Latin America and South East Asia, and international disputes.

At the World Bank, Ko-Yung was responsible for all legal aspects of the Bank and a key senior member of the Bank's management team regarding its policies and operations. During his tenure, he was involved in many major operations of the Bank, including the financial crisis in Argentina, the Chad-Cameroon oil pipeline, the Bujagali dam project in Uganda, banking sector reform in Mexico, the resumption of membership of the Federal Republic of Yugoslavia, and reconstruction of Afghanistan. In addition, Ko-Yung took the initiative in promoting the Rule of Law through legal and judicial reform projects in its member countries and will continue to play a leading role as Chairman of the World Bank's International Advisory Council on Law and Justice, whose members include U.S. Supreme Court Justice Stephen Breyer, UK Chief Justice Harry Woolf, and former Indian Chief Justice Bhagwatti.

During Ko-Yung's tenure as Secretary General of ICSID, ICSID became the premier forum for the settlement of investment disputes between foreign investors and host governments. Other than the traditional ICSID cases, ICSID has become a preferred arbitral forum for NAFTA cases involving the United States, Canada and Mexico. Of about 2000 existing bilateral investment treaties, over two-thirds select ICSID as their method of dispute settlement.

Ko-Yung was born in Beijing and grew up in Japan. He studied physics at Harvard College, graduating magna cum laude, and received his J.D. from Harvard Law School in 1973. He spent a year as a Fellow to study Japanese law at the University of Tokyo, Japan. During his previous tenure with O'Melveny & Myers, Ko-Yung was Chairman of the firm's Global Practice Group and a member of the Management Committee.

In addition to his private practice, Ko-Yung serves on the Boards of Transparency International-USA, the Morin Center for Banking and Financial Law at Boston University Law, the International Development Law Organization based in Rome, and the London Forum of International Economic Law and Development of the University of London; and is a member of the Council on Foreign Relations and the American Law Institute. He has served as Chairman of the East-West Center in Hawaii, on the Advisory Council of Human Rights Watch/Asia, and on the Board of the Asian–American Legal and Education Fund; and was a member of the Trilateral Commission. President Clinton appointed him to the Presidential Commission on International Trade and Investment. Ko-Yung also taught Japanese law and international business law at New York University School of Law.

Education
Harvard College, B.A., 1969, magna cum laude, Phi Beta Kappa, Detur Prize
Harvard Law School, J.D., 1973, Editor, International Law Journal, 1970-1973
Tokyo University, Faculty of Law, 1971-2, Fellow

Languages
Japanese and English

POTE P. VIDET
MANAGING DIRECTOR
PRIVATE EQUITY (THAILAND) CO LTD

Pote Videt is Managing Director of Private Equity (Thailand) Co., Ltd., an affiliate of Lombard Investments, which provides technical assistance to the US$245 million Thailand Equity Fund in certain private equity matters. Previously Mr. Videt was Managing Director of Credit Suisse First Boston responsible for Southeast Asia and Managing Director of Goldman Sachs in Hong Kong. His transactional experience has ranged from small entrepreneurial concerns to several Fortune Global 500 companies, government enterprises and international organizations. In its first worldwide survey, Global Finance magazine named Pote Videt as one of the best bankers in the emerging markets.

In 1997, Mr. Videt served briefly as Deputy Minister of Commerce in the Thai Government. From 1998-2001, he served as advisor to Deputy Prime Minister Dr. Supachai Panitchpakdi with regard to international economic policy. He is currently on the Council of Economic Advisors to the Prime Minister of Thailand.

Pote Videt serves on the Board of Trustees of the Asia Society and is also a member of the Board of Directors of three listed Thai companies: Loxley, Trinity Wattana and Vinythai.

He graduated summa cum laude, Phi Beta Kappa from Yale University with a B.A. degree in economics and holds an M.B.A. with distinction from Harvard Business School.

AMBASSADOR LINDA TSAO YANG
CHAIR
ASIAN CORPORATE GOVERNANCE ASSOCIATION

Ambassador Yang was the U.S. Executive Director on the Board of Directors of the Asian Development Bank in Manila from 1993 to 1999. She was the first woman appointed by the United States Government to the Board of a multilateral financial institution and the first Executive Director appointed by President Clinton and confirmed by the U.S. Senate.

Upon her retirement in December 1999, Ambassador Yang was presented the Distinguished Service Award by the then U.S. Secretary of the Treasury, Lawrence H. Summers. The award citation stated that, "Ambassador Yang has been one of the main forces behind the strengthening of the Bank's private sector operations and she has led the effort to put in place a Bank-wide approach to private sector development. Ambassador Yang played a key role in defining the Bank's participation in the international response to the Asian economic crisis, including pushing for early and expanded attention to social impacts and social development. She has provided strong fiduciary and operational oversight of Bank operations and has worked to make the Bank more transparent and accountable."

The first woman and the first minority appointed to serve as California's Savings and Loan Commissioner, she was responsible for the regulation and supervision of state-chartered savings and loan industry from 1980-82. She was the first Asian American appointed to the Board of Administration of the California Public Employees' Retirement System (CalPERS) and served as Vice President of the Board and Vice-chairman of its Investment Committee.

Ambassador Yang is Chair of the Asian Corporate Governance Association. She serves on the board of The Pacific Pension Institute, The Asia Foundation, The Center for Asia Pacific Policy, RAND Corporation, and The Committee of 100, a Chinese-American organization in the United States. She is an advisor to Lombard Investments, a private equity investment firm in San Francisco, and a member of The Trusteeship for the Betterment of Women in Los Angeles and The Council on Foreign Relations.

A graduate of St. John's University in Shanghai, Ambassador Yang earned her Master of Philosophy degree (Economics) from Columbia University of New York. Her areas of concentration were banking, finance and international economics. Married to Dr. An Tzu Yang, Professor of Mechanical Engineering (Emeritus) at the University of California, Davis campus and Honorary Professor at Jiao-Tong University of Shanghai, she is the mother of two sons.

V-NEE YEH
CHAIRMAN
HSIN CHONG CONSTRUCTION

V-Nee Yeh took over the chairmanship of Hsin Chong Construction, a publicly listed firm in Hong Kong, in 2002. It has the longest history of any active construction company in Hong Kong.

He is also a co-founder of Value Partners Limited and VP Private Equity Limited.

Mr. Yeh was a council member of The Stock Exchange of Hong Kong Limited (SEHK) until its merger into the Hong Kong Exchanges and Clearing Limited. He remains a member of the SEHK's Listing Committee and is a member of the Listing Committee of the China Securities Regulatory Commission.

He sits on the Takeovers & Mergers Panel and the Takeovers Appeals Committee of Securities and Futures Commission. He is also a director of Arnhold Holdings Limited, Guangdong Brewery Holdings Limited and Next Media Limited, listed companies in Hong Kong.

Mr Yeh began his career after graduating from the School of Law at Columbia University in 1984. He worked with the Lazard Houses (New York, Hong Kong and London) in corporate finance, capital markets and risk arbitrage from 1984 onwards, until his resignation from Lazard Brothers Capital Markets as a partner in 1990.

Aged 44, Mr Yeh was admitted a member of the California Bar Association in 1984. He has a B.A. and a J.D. degree.

Asian Corporate Governance Association

The Asian Corporate Governance Association (ACGA) is an independent, non-profit membership association dedicated to assisting in the implementation of effective corporate governance in Asia. Highlights of our work in recent years include:

- Tracking corporate-governance developments across 11 countries in Asia and carrying out independent research.
- Creating a website (www.acga-asia.org) that provides comprehensive and concise coverage of corporate governance reform in Asia.
- Forming the "ACGA Investor Discussion Group", a confidential quarterly forum where leading institutional investors can share ideas and concerns.
- Developing exclusive services for ACGA members, including: semi-annual Member Briefings in Hong Kong and Singapore; premium website content; and a monthly "Member Alert" bulletin.
- Speaking at more than 110 conferences, seminars and workshops around the region.
- Regularly speaking to the media about corporate governance issues.

ACGA was founded in 1999 by Lombard/APIC, a private equity fund management company, in cooperation with a board of senior executives and professionals from around Asia. Lombard continues to be a major sponsor. Other Founding Corporate Sponsors include: Chubb Insurance, CLSA Asia-Pacific Markets and Sun Life Financial Asia.

Founding Corporate Sponsors:

Lombard Asian Private Investment Company | CHUBB | CLSA ASIA-PACIFIC MARKETS | Sun Life Financial

ACGA Corporate Members

Our aim is to build an effective network of members who support ACGA's goal of advancing governance reform that is both disclosure-based and market-driven. Members include:

- Aberdeen Asia
- AIG Investment Corp (Asia)
- Aon Hong Kong
- British Columbia Investment Corp
- CalPERS
- CalSTRS
- Chubb Insurance
- Citigroup Asset Management - Asia
- CLSA Asia-Pacific Markets
- Coudert Brothers
- Credit Agricole Asset Management (HK)
- Dibb Lupton Alsop
- GIC Special Investments
- Hermes Pensions Management
- Hewitt Associates
- Hong Kong University of Science and Technology
- IMC Pan Asia Corporation
- Jardine Lloyd Thompson
- Kookmin Bank
- Li & Fung
- LIM Advisors
- Lloyd George Management
- Lombard/APIC
- Marsh Inc.
- Milbank, Tweed, Hadley & McCloy
- Mirant Asia-Pacific
- Neptune Orient Lines
- Oracle Corporation Asia-Pacific
- Prudential Asset Management
- Standard & Poor's
- Standard Life Investments
- State Street Global Advisors Asia
- Sun Life Financial Asia
- SUNDAY Communications
- Swire Pacific
- Templeton
- TSMC
- Value Partners
- Vtech Holdings
- Watson Wyatt

For details on membership benefits, contact Jamie Allen on (852) 2872 4048 or jamie@acga-asia.org