Asian Business Dialogue on Corporate Governance 2001

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Conference Report

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Asian Corporate Governance Association

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- Anne Charron
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We wish to express sincere thanks to all our speakers, many of whom flew in from great distances to take part in the event, for giving generously of their time. Their names are included in the conference programme available within.

We are very grateful to the ACGA Board for providing valuable intellectual and personal support, and particularly want to thank those who were able to participate in the conference: Paul Hsu of Taiwan, In-Kie Hong of Korea, and Tak Wakasugi of Japan.

Finally, we wish to pay tribute to Dr. David Chiang, Honorary Chairman of ACGA and former Chairman and Managing Partner, Lombard Asian Private Investment Company (LAPIC). David had the vision and energy to found ACGA, for which we remain in his debt.

Ambassador Linda Tsao Yang, Acting Chair, ACGA
Jamie Allen, Secretary General, ACGA

Contents

1 Conference programme

9.00 am: **Introductory remarks:**
Ambassador Linda Tsao Yang
Acting Chair, Asian Corporate Governance Association

9.10-9.30: **Keynote speech:**
"Corporate Governance as a Competitive Necessity: A Market Regulator's Perspective"

Mr. Andrew Sheng
Chairman, Hong Kong Securities and Futures Commission

9.30-10.50: **Session 1:** **Improving Corporate Governance and Gaining Competitive Advantage in a Global Economy**

Moderator:
Mr. Douglas C. Henck
Executive Vice President, Asian Operations
Sun Life Financial Services of Canada, Inc.

Panelists:
Mr. Harvey Chang
Senior Vice President and Chief Financial Officer
Taiwan Semiconductor Manufacturing Company

Mr. Andrew Sheng
Chairman, Hong Kong Securities and Futures Commission.

11.20-12.40 pm: **Session 2:** **Challenges, Strategies and Progress in Implementing Corporate Governance in Asia**

Moderator:
Dr. Victor Fung
Chairman, Li & Fung
Chairman, Airport Authority of Hong Kong

Panelists:
Mr. Gary Coull
Executive Chairman, CLSA Emerging Markets

Mr. Kikwon Doh
President & CEO, Good Morning Securities, Korea

12.45-2.15: Luncheon speaker:
Mr. Robert F. Carlson
Vice President and Senior Board Member, Board of Administration
California Public Employees' Retirement System (CalPERS)

2.30-3.45: Session 3: The Role of Institutional Investors

Moderator:
Dr. Teh Kok Peng
President, GIC Special Investments, Singapore

Panelists:
Mr. Ian Faragher
CEO, Chubb Insurance, Hong Kong

Ms. Nawaaporn Ryanskul
Former and first Secretary General
Thai Government Pension Fund

4.15-5.30: Session 4: Regulatory Trends

Moderator:
Mr. Barry Metzger
Senior Partner, Coudert Brothers, New York

Panelists:
Mrs. Laura M. Cha
Vice Chairman, China Securities Regulatory Commission

Mr. Frederick Hu
Managing Director and Head, Greater China Economics and Strategy
Goldman Sachs (Asia)

Mrs. Lee Suet-Fern
Partner/Co-Head, Shearman & Sterling Stamford
Singapore

5.30-5.45: Conclusion
Mr. Peter Sullivan
Chairman & CEO, Lombard Investments, Inc.
San Francisco

6.00-7.30: Cocktails: Sponsored by FTSE and held jointly with the Association for Sustainable and Responsible Investment in Asia (ASRIA)

$\boxed{2}$ Quotable quotes:

"As recently as five years ago, corporate governance was not a topic for polite conversation among business leaders. Today, not only is it a legitimate and respectable subject for serious discourse, but there is a gathering consensus that it is a topic that needs to be pursued with a deep sense of urgency."

Linda Tsao Yang
Acting Chair, Asian Corporate Governance Association

"Global competition is a different ball game, and Asia needs to meet global standards. Good companies that meet this standard are being priced globally, and companies that don't are being priced locally."

Andrew Sheng
Chairman, Hong Kong Securities and Futures Commission

"I do not see a conflict between the pluralist approach of board responsibility (the stakeholder view) and a shareholder-only view. A broad-based, inclusive approach to running business is in the best interests of all stakeholders, including shareholders."

Douglas Henck
Executive Vice President, Asian Operations, Sun Life Financial

"Another challenge — and one perhaps unique to TSMC — is the adverse effect of trying to be transparent in a less than transparent market. What you end up with is your competitor quoting some of the numbers you have disclosed and misusing them by talking to your customers and saying, "this is what they're doing and this is what we're doing". But if you go back and look at what they are disclosing, they are not disclosing anything, so you don't know how to reconcile that. We have had to modify, and to a certain extent reduce, the level of information that we give out. But we try other means to help investors understand how we operate."

Harvey Chang
Senior Vice President and Chief Financial Officer
Taiwan Semiconductor Manufacturing Company

"Reform in Asia will hinge on issues such as the composition of the board, how board members are appointed, how many truly independent board members there are, and how the board functions. These issues are particularly critical in Asia because of the domination of many boards by strong owner-managers."

Dr. Victor Fung
Chairman, Li & Fung
Chairman, Airport Authority of Hong Kong

"The CLSA study (on corporate governance in companies) was the first of its kind. We felt it was important to produce because of the very inconsistent nature of corporate governance in the region. But it has also been rather expensive for us. I don't want to make a big deal about this, but the reaction to the rankings was quite violent... We lost quite a bit of corporate finance business — mandates that were signed were overturned or left to expire through various means. So it's a dangerous exercise and one that I'm quite keen that we don't stand alone on down the road."

Gary Coull
Executive Chairman, CLSA Emerging Markets

"The company's efforts to reform its corporate governance have paid off in various ways. Management has become more disciplined. We are delivering a clear message and image to our staff. And hiring has become significantly easier: we recently received 7,500 applicants from top universities for 15 new positions without having to advertise!... But the main payback is the trust of employees. If you ask me what is the major benefit of our corporate governance review, I can say the confidence from my employees."

Kikwon Doh
President & CEO, Good Morning Securities, Korea

"I believe that we have much in common with Asia. We both want companies to perform well, we believe that long-term strategies, not short-term shifts in stock price, will make a company profitable. We both understand that all companies, whether governed under a structure of full accountability and transparency or not, will inevitably experience both good and bad times along the path to profitability. And finally, we embrace a notion that accountable governance means the difference between wallowing for long periods in the depths of a down-phase in the performance cycle and being able to respond to correct the corporate course."

Robert F. Carlson
Vice President and Senior Board Member, Board of Administration
California Public Employees' Retirement System (CalPERS)

"The question we need to ask ourselves is: in a globalised world, with global investment opportunities, how do you ask people to invest in Asia when corporate governance standards in general are not so good? And the returns are not as good as you can get in the US, which has better governance and lower risk. We continue to invest in Asia because we think that there's scope for diversification. We also think there is an interesting story to tell about Asia. All of us hope that Asia will continue to reform, although the pace has been quite disappointing so far."

Dr. Teh Kok Peng
President, GIC Special Investments, Singapore

"Why, you may ask, are people in the insurance industry concerned about corporate governance? It is, in fact, our business. It's the insurance industry that provides the coverage for directors and officers who are exposed to risk. The policies we write kick in when something goes wrong and liability raises its ugly head. When directors and officers drop the ball out of incompetence, ignorance, lack of judgment — it's a long list — negligence, dishonesty, bending the rules or just good old-fashioned greed, it's the insurers that have to deal with it. This is no exaggeration."

Ian Faragher*

CEO, Chubb Insurance, Hong Kong

"Political factors play a very large role in Thailand, so we cannot bring about corporate governance reform without trying to make politicians aware of the situation as well their duties. I will give you an interesting example involving the Minister of Interior. He created a big uproar when he tried to enforce the law. Everyone thought he was doing something very drastic, but he said simply that if you don't follow the law, then you might as well abolish the law. As long as the legislature had passed a law, it was his duty to try to enforce it."

Nawaaporn Ryanskul

Former and first Secretary General, Thai Government Pension Fund

"At the firm level, the record of achievement four years after the onset of the Asian financial crisis in my view is unimpressive and disappointing. There are too few market leaders, that is, companies whose standards of corporate governance practice are not measured by the minimum standards prescribed by law but are an embodiment of best-practice standards that serve as a model for other players within the market place. There are too few institutional investors who are being seen to aggressively demand reforms in corporate governance at particular companies... And there are too few examples of the government as a model shareholder."

Barry Metzger

Senior Partner, Coudert Brothers, New York

"When the basic corporate culture itself is not clear (in China), and you add to that these murky and overlapping responsibilities and ownership rights and management responsibilities, it becomes even more egregious. Some recent cases in China show that some controlling shareholders have all along used their listed companies as their own little ATM machines. When this is discovered, they say they cannot repay, so it is the listed company that suffers."

Laura Cha

Vice Chairman, China Securities Regulatory Commission

"The poor standards of disclosure and investor protection in many emerging market economies have significantly increased the risk premium, the cost of capital, and hence reduced capital inflows that otherwise would have contributed to economic growth and raising living standards."

Frederick Hu

Managing Director and Head, Greater China Economics and Strategy

Goldman Sachs (Asia)

* Now head of Chubb's Greater China operations and based in Shanghai

"The situation at Asia Pulp & Paper (APP), with its opaque corporate structure and very weak governance, is probably a textbook illustration of what not to do. Yet international investors, seduced by the fact that there was a NASDAQ listing and maybe that major investment banks had underwritten the offerings of its securities, did not pay attention to APP's inadequate corporate governance. Many of these investors are not flippers, they were long-term players. Yet none of them appeared to have paid any attention..."

Lee Suet-Fern
Partner/Co-Head, Shearman & Sterling Stamford, Singapore

"In our investments (in Asia) we have observed a wide diversity in standards of corporate governance. We learned quickly through investment in one company, where the board did not have sufficient independence, that cost accounting and auditing standards were not up to international standards, and we had to play an extremely active role...to protect our interests. A much happier example was one made shortly after the Asian crisis in Korea's fifth largest securities firm. We helped to change the shape of the board and implement international best practices. We sold a minor portion of our investment for a 352% gain."

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

3 Key themes and suggestions

Accountability

- Corporate governance rests on three basic disciplines: self-discipline, regulatory discipline and market discipline. **(Andrew Sheng)**

- Companies have a duty to all stakeholders, including shareholders, and will benefit from taking account of their wider social responsibilities. **(Douglas Henck)**

- Independent directors in Hong Kong bear a high degree of individual responsibility. They need to be paid a lot more for what they do. **(Gary Coull)**

- Institutional investors could employ "virtual directors" to act as intermediaries between the investment community and Asian companies, monitor performance and, possibly, mentor management. They could even sit on boards as direct proxies representing institutional investors. **(Gary Coull)**

- Tapping the public markets and having public shareholders is a privilege. Is it inconsistent with that privilege for families to have public and private companies operating in the same area of business? **(Gary Coull)**

- The goal of any D&O programme is to sensitise the company's executives to the fact that virtually everything they do creates the potential for second-guessing and, perhaps claims, by persons adversely affected by their actions. From our point of view, directors and officers need not be flawless in their decision-making, but they must fulfil three essential duties. These are the duty of diligence, the duty of loyalty and the duty of obedience. **(Ian Faragher)**

- In China, the interests of the state, the majority shareholder, are not properly represented in many listed companies. Most managers are former government officials that look at listed companies as windfalls for themselves. They often do not have the right experience to run such companies and still consider them to be part of government. **(Laura Cha)**

- We always stress corporate governance in listed companies. But from a regulator's perspective, the governance of intermediaries is also extremely important. By this I mean investment funds and brokerage houses in China and elsewhere in the region. **(Laura Cha)**

Disclosure

- Companies sometimes fail to realise that they, as much as their investors, need timely, reliable and accurate information to run their businesses efficiently. **(Andrew Sheng)**

- It is important to run companies in an open and transparent manner. Unless management meets the standards expected by the investment community, a company will not achieve the P/E and value due to shareholders. **(Victor Fung)**

- Whether we have good news or bad, we have made an effort to disclose it to our auditors, employees and investors. We once reported a huge loss not just to our board, but to all our employees. I still remember their surprise when I told them that these numbers were the same as I had presented the day before to the board. But in the process we gained their trust. **(Kikwon Doh)**

Catalysts for change: corporations

- Asian corporations will change and compete, not because they are told to do so by the state or the market, but because they themselves want to change in order to remain in business. **(Andrew Sheng)**

- In the context of the new challenges facing companies — notably globalisation, increasing competition and technological change — building deeper and more strategic relationships with customers, suppliers, employees, communities and other stakeholders has become central to competitiveness. **(Douglas Henck)**

- TSMC was formed in 1987 with the ambitious goal of becoming a world-class company. We wanted to start as we meant to go on, and not to become entangled in common Asian corporate practices such as cross-shareholdings and diversification for the sake of it. **(Harvey Chang)**

- For continuous improvement (in corporate governance) I think you have to have good board members. While the chairman obviously has a responsibility to think about corporate governance as a whole, I must say a lot of my drive and impetus comes from some pretty active and independent board members. They are constantly pushing the frontiers, so to speak. I see my job as selecting the right people, then the company can take a continuous improvement route. **(Victor Fung)**

- What I can say is that there is a big difference between what people say and what they do....Every CEO will tell you that corporate governance is very important, but not all of them are actually changing their behaviour. Only one or two may be doing it today, but as time goes by the numbers will get larger. **(Kikwon Doh)**

- Long-term strategic vision is certainly an element that's necessary for good corporate governance. **(Peter Sullivan)**

Catalysts for change: investors

- Pressure brought by shareowner activists is being magnified by the growth of pension funds and mutual funds. Plan sponsors of these funds have a fiduciary responsibility to their constituents, who depend on the financial growth of wise and prudent investments. The result is a louder voice for shareowner rights. **(Bob Carlson)**

- One of the ways we can add value to long-term returns of our portfolio is through corporate governance. If we are committed to a platform that means we don't actively buy and sell (ie, passive indexing), then we must use our influence to help improve company performance. **(Bob Carlson)**

- Good corporate governance embodies both performance and conformance. How can we have more of it in Asia? There are some things that institutional investors can do, including working more closely with regulators and helping to inform the market about company practices. **(Teh Kok Peng)**

- The Government Pension Fund of Thailand was set up in 1997. When it started investing, it decided that whatever standards it wanted other people to adhere to, it would have to follow itself first. So corporate governance starts at home. We have to practice what we preach. **(Nawaaporn Ryanskul)**

- Shareowner activism in Asia is in the ascendant. Investor associations have been created and shareholders have been increasingly prepared to attend meetings, be more vocal, and organise the minority vote. Asians are far from being timid or disinterested. **(Lee Suet-Fern)**

Catalysts for change: rules and regulators

- Reform in Asia has converged around a set of basic principles, including reliance upon the importance of independent directors, the role of disclosure, enhanced accounting rules and auditing principles, and reliance on director and managerial accountability to shareholders. **(Barry Metzger)**

- Asia faces a growing need for convergence in regulatory standards. The rationale for this is clear: in today's global economy, investors come from all corners of the globe so the divergence in regulatory systems has imposed a barrier to the efficient allocation of capital globally. **(Frederick Hu)**

- Two groups are on the front line of reform: market regulators and investors. Sometimes they fight alongside, but often they are not adequately aware of their strong inter-relationship. **(Lee Suet-Fern)**

Risk management

- Business today is facing risks of greater complexity and diversity, complicating their responsibilities and the personal liabilities of directors and officers. New laws, recent court decisions, shareholder activism, the activities of groups such as non-governmental organisations and environmental lobbies are all raising the ante by defining more broadly the responsibilities of directors and officers. **(Ian Faragher)**

Company assessments

- There needs to be more than just talk about corporate governance. There needs to be more concrete appraisals of companies. **(Gary Coull)**

- Investors are often criticised for voting with their feet, but it can be a powerful indicator of poor corporate governance. **(Teh Kok Peng)**

- We need to evaluate progress in corporate governance at the firm level and create a scorecard of successes and failures. Many of the changes that matter most require only a matter of months to implement. **(Barry Metzger)**

Education

- We have had to educate our directors to understand that decisions must be made for the benefit of all shareholders. This is a continuing process and it's a challenge. **(Harvey Chang)**

- In Silicon Valley, there is a culture of venture capital investors exchanging ideas. In Asia, this is less likely because people are afraid of giving away secrets. Is economic life really a zero-sum game, or is it also win-win? Perhaps we can learn from the VCs in Silicon Valley. **(Teh Kok Peng)**

- There is a willingness to change in Thailand as long as you let people understand the essence of the thing first. If people don't understand the essence of the word, and there is only the promotion of the form, you will end up having the proper form but nothing in it. **(Nawaaporn Ryanskul)**

- At Lombard we believe so strongly in good corporate governance that we have a lengthy checklist on it. We talk through the concept of corporate governance with each investee company and we incorporate into the contract agreement any improvements that will be necessary. **(Peter Sullivan)**

Regulatory systems

- In a well-functioning market, regulators prevent harm to investors without being overly prescriptive to companies. But in China, market incentives do not have their normal value. We need to prescribe stronger medicine. **(Laura Cha)**

- This region must foster an "enforcement culture". Regulatory authorities in Asia should form a pan-regional consultative body, perhaps under the umbrella of APEC. This body should meet regularly, identify critical regulatory differences and loopholes, and set higher standards. **(Frederick Hu)**

- One of the key shifts in Singapore has been the move to a disclosure-based philosophy of regulation. This is a major departure from the previous prescriptive-disclosure regime. **(Lee Suet-Fern)**

4 Introduction

LINDA TSAO YANG

Acting Chair, Asian Corporate Governance Association (ACGA)

The emphasis of this conference, as its title suggests, is on dialogue. As recently as five years ago, corporate governance was not a topic for polite conversation among business leaders. Today, not only is it a legitimate and respectable subject for serious discourse, but there is a gathering consensus that it is a topic that needs to be pursued with a deep sense of urgency.

Let me give you an example. Over the last few days we have had the World Economic Forum's "East Asian Economic Summit" here in Hong Kong. Yesterday I had the good fortune of sitting in on a session titled, "Can Asia's financial system sustain the next recovery?" I want to quote — I should say paraphrase — what Mr Liu Ming Kang, President, Bank of China, said. He said that China's accession to the WTO would further intensify competition in China's banking sector. How does the Bank of China position itself to compete in this more intense competitive environment? And not only to compete, but also to seize the opportunities that change will offer? Mr Liu answered: "The most important thing we are doing is to improve our corporate governance at home. We must keep our own house in good order to meet the challenge. In fact, we will use corporate governance as a platform to further reform the Bank so that we can reposition ourselves for the next recovery in Asia."

What a difference five years have made! I'm so delighted that all of you share the same sense of urgency about the need to improve corporate governance.

Let me introduce our first speaker, our keynote speaker, Mr Andrew Sheng. Andrew is my professional colleague and personal friend. He is the Chairman of the Hong Kong Securities and Futures Commission and, prior to this, he was the Deputy Chief Executive of the Hong Kong Monetary Authority for a number of years. Previously, he was seconded to the World Bank and, following the Asian financial crisis, was appointed Chairman of the Task Force on Implementation of Standards by the Financial Stability Forum in 1998. He has also co-chaired the Working Party on Transparency and Accountability, which is one of the three working parties formed under the G22 Finance Ministers and Central Bank Governors. Mr. Andrew Sheng...

5 Keynote speech

"Corporate Governance as a Competitive Necessity: A Market Regulator's Perspective"

ANDREW SHENG

Chairman, Hong Kong Securities and Futures Commission

Andrew Sheng challenged the accepted wisdom on corporate governance with three questions and ended with a challenge.

I basically always ask three major questions. Why is Asian corporate governance so controversial? Secondly, how can it be improved? And thirdly, who can provide the best solution — the regulator or the market?

I am very encouraged this morning because I believe we have the answers right here in this room. The Asian Corporate Governance Association (ACGA) has been established with the support of corporate leaders throughout Asia-Pacific. You formed ACGA because you believe that corporate governance standards can and should be improved. And so do I. Moreover, like me, you are all tired of the mantra that we are so far behind the major markets in our corporate governance. We need to identify why we are behind and what we can do to catch up. It's as simple as that.

Why is corporate governance controversial?

For a start, let me say that corporate governance cannot be divorced from the culture or the environment in which companies operate. Before the Asian crisis we were admired for our entrepreneurship, dynamic growth, and family values of hard work and corporate loyalty. After the crisis, we were all tarred with the labels of crony capitalism, nepotism and reluctance to change. But it can't be all that bad. In ACGA's words last year, Asian corporate governance issues are, I quote, "Opaque management, parochial mindsets, unethical practices as well as timid or disinterested minority shareholders, and independent directors who are less than independent."

I think it would be helpful if we were to temper this image with a more balanced perspective, and I want to be as objective as possible about this. First, unlike American or European corporate history, which has at least 100 years head start (and even longer in Europe), modern Asian corporate growth is more recent in origin. Other than a few Japanese multinationals, most Asian companies emerged after the Second World War with state ownership or some form of state help. Many were founded by dynamic risk takers with support only from friends and family, and often competing against state-owned enterprises, which were usually supported by the state. Asian countries were trying to level the playing field between themselves and foreign competition, but the concept of a level playing field between state and family/private enterprises was not high on the policy agenda. In fact, it was not there.

Some Asian families were very successful and became world leaders. If we look at the structure of the more prominent family companies recently, from the conglomerates in Indonesia to the chaebols in Korea, we see that the grip of these families has become looser in the wake of the Asian crisis. To understand why, we need to delve into the origins of their success as well as their problems.

In the post-war rebuilding era, many Asian entrepreneurs built market share through a combination of internal savings, hard work and assistance from an export policy that encouraged manufacturing. Growth was the primary objective and profit margins were secondary. Both the government and the banking system were supportive of such growth and, in trying to maintain growth as well as a majority state or family ownership, many corporations become over-leveraged. You simply leverage in order to maintain your control. They engaged in short-term borrowing to finance long-term projects, especially in property and large-scale manufacturing capacity. Add to this an exposure to foreign currency borrowing without export earnings and many corporations became vulnerable to the shock of the Asian crisis.

Throughout Asia, we are still going through a phase of debt and corporate restructuring that has cost some economies as much as one third of their GDP (from bailing out non-performing loans in the banking system).

Now, this euphoria over growth and market share is not unique to Asian companies. It is also illustrated in the worldwide bubble in dotcoms, when many issuers, investors and analysts were valuing companies on price-revenue, not profit, projections. We're now returning to basics.

We realise now that it is no longer return to growth that matters — it is returns to equity. It is not returns to the family or the majority shareholder, but returns to all shareholders. It is not returns to management, but returns to people, all workers and stakeholders. In essence, the heart of corporate governance is returns to society — the mission of all good corporate citizens — with accountability to all stakeholders.

Globalisation is here to stay despite the tragic events of September 11th. Globalisation has brought about global competition, and the struggle between the large and the small grows keener than ever. With global investing and global choice, companies and markets will be benchmarked against global standards, whether they like it or not, including standards of corporate governance.

Now more than ever, discipline, transparency and accountability are regarded as the hallmarks of quality in capital markets. Globalisation also means that in conditions of greater market volatility, there will be a flight to quality. Once investors fail to trust a particular market, liquidity will dry up as capital flows to other markets of better quality. My good friend, Arthur Levitt, former chairman of the US Securities and Exchange Commission, considers that higher levels of corporate governance are fundamental in today's global environment, not only to compete but to survive.

How can corporate governance be improved?

Corporate governance, in my simplistic view, is like a three-legged stool resting on certain basic disciplines: self-discipline, regulatory discipline and market discipline.

• Self-discipline

I am convinced that corporations are built by entrepreneurs and destroyed by inefficient bureaucracies, private or official. Many of the best studies of companies around the world indicate that they are led by people who have passion, vision and commitment, and have a corporate culture that appeals to higher values than just the pay packet. The best corporations in Asia share these same attributes and, in terms of entrepreneurship, I believe Asian corporations are second to none.

But how many leading Asian corporations, struggling with the difficulties of modern management, are tied down by the need to employ friends and relatives who are less competent than the best in the market, or by conflicts within families? The same is true of many state enterprises, dragged down by outmoded controls and salary structures. How can such family networks or state bureaucracies compete against modern institution-led companies that not only hire the best talent, but are able to use global networks and brands to out-think, out-flank and out-sell our best companies? That's the real competitive imperative that all Asian companies face, irrespective of whether they are privately owned, state-owned or institution-led.

I am a great believer that Asian corporations will change and compete, not because they are told to do so by the state or the market, but because they themselves want to change in order to remain in business. Corporate captains who complain that quarterly reporting costs too much fail to realise that they, as much as their investors, need timely, reliable and accurate information to run their business efficiently. Certain Asian markets are beginning to set examples in this area: the China Securities Regulatory Commission, for example, has already mandated that quarterly reporting will take effect in all Chinese listed companies from the beginning of 2002.

But Asian corporations have one distinctive feature that is different from non-Asian companies. Almost all corporate governance mechanisms, Western or Eastern, seek to align the interests of managers with those of the company (ie, all the shareholders). In Asia the interests of the company are already aligned with those of the majority shareholder (either the family or the state), because they already control it. They are both shareholder and management. The major corporate governance concern in the West is that a self-selective group of managers owning less than 10-20% of a company's shares can entrench their self-interest at the expense of dispersed, public shareholders. Consequently, irrespective of whether you are in Asia or outside, if the managers believe that their self-interest comes first, all the trappings of OECD corporate governance guidelines, and requirements for audit committees and so on, will not necessarily prevent a company from suffering managerial abuse. This is true of all markets, developed or emerging.

But it's also clear that Asian companies have been preoccupied with their own internal succession and restructuring problems, and have only shared information with minority shareholders when it is required by law, rather than seeing it as a calling of ownership. This is a level-playing field issue between the majority shareholder and the minority shareholder. A report from CLSA in October 2000 concludes that while Hong Kong and Singapore have good corporate governance standards, it states that, "Surprisingly few companies in these markets have outstanding governance with most only meeting mandatory requirements." So even the so-called leading markets in Asia have some way to go. Merely meeting minimal regulatory standards is clearly not good enough for institutional and international investors. Tardiness in embracing the higher standards of good corporate governance could be costly, since corporate captains are not paying enough attention to the core values that drive global competitiveness.

Another characteristic of Asian corporations is that many are dominated by a highly successful, but paternalistic, head whose views often prevail over those of the board, including independent non-executive directors. This is a problem rooted in a society that avoids confrontation and disagreement. Over-reliance on the self-discipline of the corporate founder and dominant leader to sustain success over the long haul is at best hopeful and, at worst, unrealistic.

The best corporations today nurture a culture that encourages both expression of views and a willingness to listen, so that contending policies and strategies can be debated. Increasingly there are Asian companies, especially in the high-tech area, where contending views and innovation are encouraged (which is why I remain confident that Asian corporate captains will adapt and absorb the good lessons from the West). I know, for example, one successful Hong Kong venture capital fund that ensures the firms it invests in are all Asian, but whose management are trained and educated in the West. Hence, the Asian companies it backs have global corporate values in addition to legendary Asian entrepreneurship and hard work.

• Regulatory discipline

While corporate leaders are builders, self-discipline is never enough on its own. The importance of corporate governance lies in its contribution to both business prosperity and accountability. How one achieves business prosperity cannot be easily encapsulated into rigid rules and regulations. Hence the conventional wisdom that the regulator cannot, and should not, replace the judgement of the businessman in commercial matters.

Where does regulatory discipline come in? Even Adam Smith acknowledged the need for law and regulation to rap the fingers of the invisible hand when it gets into a little bit of mischief. It is totally understandable that in the early days of Asian development, bureaucrats were better educated and informed than many private sector businessmen, as was the case during Japan's Meiji reform. And so state business initiatives to develop banking and export sectors were spectacularly successful in the heady days of the Asian miracle.

Having said that, policy makers have also had to provide the institutional framework and the policies to attract investors. Regulators must drive reforms where necessary to meet international standards. Regulators must set the rules of the game in consultation with the private sector and enforce these agreed rules fairly and transparently. They must also protect investors through greater public education and disclosure rules. When cheating and fraud occurs there must be regulatory discipline. You can't replace that. But regulators, being the good bureaucrats that they are, tend to over-regulate. I admit this as much as anybody else. As my good Taiwan lawyer friend, Lawrence Liu, has said: "Asian regulators over-regulate and under-enforce." But that is another subject that I do not have time to dwell on today.

For the market to function properly, we need to appreciate that each party must do what each is good at. The strength of the private sector is to develop business, but it cannot regulate itself well because of conflicts of interest. The public sector handles infrastructure well, and has a unique position in setting standards, maintaining a level playing field and minimising market misconduct. Life gets very confused when the public sector is owner, regulator and competitor to the private sector.

But the question still remains, is self-discipline and regulatory discipline enough? The answer is that both are necessary, but not sufficient. Put it this way. Why have banks failed in both emerging and developed markets despite good bankers and strong regulators? To answer this, we need to come to the third discipline that I wish to talk about — market discipline.

• Market discipline

One reason some markets are more efficient than others is because market discipline is allowed to work in those markets. Protecting some parts of a market from competition is clearly bad for an economy as a whole. In the corporate governance area, market discipline is exercised most frequently through the share price and the incentive system.

In the US, large pension funds and institutional shareholders such as CalPERS have found that over time their responsibilities to their beneficiaries have been made more explicit by regulators and investors. Hence, they have become much more active and vocal in corporate governance, such as through formulating ethical investment criteria or acting to change problematic management. Their market power has enabled them to be an effective force. Unfortunately, institutional investors in Asia tend to vote only with their feet by selling out. We believe that they should support greater corporate governance activities, such as ACGA.

The other form of investor activism is to empower the investor through derivative suits. In the US, class-action suits are the most powerful tool and probably the most punitive for the company that strays in conduct. This is not necessarily the solution in the Asian legal tradition. The Common Law tradition in Hong Kong, for example, would have difficulty adopting class action and the contingency fee mechanism. So some Asian regulators have begun to encourage shareholder activism, such as in Taiwan where in the year 2000 there were 456 law suits against companies. Malaysia and Korea have also witnessed such activism. But Asian regulators are still debating the advantages and costs of allowing class versus derivative actions, and, I say this quite categorically, that we're not sure which is the right model to follow. In Hong Kong, for example, there is a private proposal for a Hong Kong Association of Minority Shareholders (HAMS) that would, among other things, carry out quasi class actions on behalf of its members.

But there is one market force that is emerging strongly — the arrival of rating agencies that offer corporate governance rating services in this region. By beginning to benchmark the quality of corporate governance, such quality will be priced more accurately. Companies will be judged by the market and how they behave. This is market discipline working at its best.

Conclusion

I believe the combination of self-discipline, regulatory discipline and market discipline will work together to push Asian corporations to behave more efficiently and to compete on a global level. Corporate governance cannot be divorced from corporate culture. Whatever the debate about Asian values across a diversity of Asian nations, Asian societies have always been pragmatic. I am convinced and optimistic that there is already awareness in Asia of the need to change in order to compete. We are all to blame for our faults and we all have to gain in making it work better.

6 Session 1

"Improving Corporate Governance and Gaining Competitive Advantage in a Global Economy"

Moderator:

DOUGLAS C. HENCK
Executive Vice President, Asian Operations, Sun Life Financial

Douglas Henck spoke in favour of a broad-based, inclusive approach to corporate governance.

Companies have a duty to all stakeholders, including shareholders, and will benefit from taking account of their wider social responsibilities. In the context of the new challenges facing companies — notably globalisation, increasing competition and technological change — building deeper and more strategic relationships with customers, suppliers, employees, communities and other stakeholders has become central to competitiveness.

This stakeholder model of corporate governance has its critics, with many companies resisting the notion of responsibility to all stakeholders. In 1998, the Toronto Stock Exchange President, Roland Fleming, criticised the stakeholder model for lacking a standard of clarity and a clear measure of accountability. In fairness, this lack of measurement is a shortcoming of the stakeholder system, but conversely a shareholder-only responsibility must demonstrate that it drives corporate behaviour that benefits all of society. The use of a "balanced scorecard" can help to advance management thinking and practice in this area, and encouragement would be a more effective tool than force in bringing about change.

I would like to make a case for that stakeholder model and look at the various stakeholders.

Customers

"Putting the customer first" is a tried and tested business strategy. As consumers today increasingly look at the ethical record of companies before buying ("ethical consumerism"), companies ignore these trends at their peril. With the growth in Asia of the consumer base there are, and will be, a significantly greater number of people in this category.

Employees

Giving people a sense of being part of a greater cause is as important as higher pay in encouraging employee motivation. One study of 3,000 strategic business units found that, in stable economic environments, those with good human resource management outperformed the poor performers by an average of 3.5%. But when conditions became complex or turbulent, the difference was a staggering 16.7%.

A relevant case study is Infosys, a developer of customised business software based in India. It initially adopted world standards of corporate governance because it recognised that it was competing in a global marketplace for talent and business — good governance made it more attractive to potential employees and customers. This in turn led to exposure to the global capital markets a few years later.

Business partners

Long-term relationships with business partners are crucial to success, because they reduce complexity and costs and increase quality. Fair terms are offered. In a legendary example, a president of Hewlett Packard once countermanded a terrific 20% discount that his purchasing agent had extracted from a supplier and negotiated a fairer, but higher, price — on the grounds that the supplier could not make a profit at the lower price. Conversely, a large auto manufacturer in Europe once famously cut costs by making unreasonable demands on suppliers, only to discover that it was subsequently not given priority by its suppliers, the quality of its cars declined, and its market share fell.

The environment

A bad environmental track record is not only bad for business, because of the penalties that polluting firms face, but causes reputational harm.

Shareholders

It is becoming increasingly clear that positive governance pays premiums. A governance premium on the price of your shares is more likely to be found within emerging markets, because of the greater diversity of corporate behaviour, than in mature markets.

Evidence is also growing that social responsibility correlates positively with financial performance. As "socially responsible investing" (SRI) becomes more popular, and the size and number of specialist SRI funds expands, more capital is available for companies perceived as having good corporate behaviour. Various indices of these SRI funds clearly demonstrate a higher than average performance, suggesting that we can have a good conscience and good products too. Most will happily take this win-win solution.

I do not see a conflict between the pluralist approach of board responsibility (the stakeholder view) and a shareholder-only view. A broad-based, inclusive approach to running business is in the best interests of all stakeholders, including shareholders.

The future

Where are these developments heading? The vision we should have is not just one of companies operating ethically and regulators performing effectively. It is more broadly about the role of business in society. The days are gone when we can look at our society, our lives, our commitments and examine each separate part as though it were isolated from the rest. Economies and the fates of different peoples, the privileged and under-privileged, are interconnected. Yet what we often see today are companies and countries playing games of divide and conquer, of confrontation rather than coordination. With erosion in the influence of governments and religious organisations, there may seem little hope in overcoming the previously unimaginable and complex problems afflicting much of the world. Perhaps only business has the resources, the competence and the credibility to begin to tackle these predicaments.

Panelist:

HARVEY CHANG
Senior Vice President and Chief Financial Officer
Taiwan Semiconductor Manufacturing Company (TSMC)

Harvey Chang gave a frank account of the efforts that his company has made to inculcate corporate governance into its culture.

When TSMC was founded in 1987, we set an ambitious goal of growing ourselves into a world-class company. We wanted to begin on the right foot. We wanted to operate as a world-class company and tried not to become entangled in many of the very common Asian company practices.

TSMC's corporate philosophy is based upon the following principles:

• Integrity
Integrity is essential because in the semiconductor foundry business you are entrusted with the design secrets of competing companies. We must have the integrity to hold that information confidential and be accountable for it. Treating all customers fairly means we need to apply the same standards to all stakeholders, particularly shareholders.

• Board independence
We set up a fairly independent board of directors from the start: independent in the sense that individual shareholders could not manipulate the board behind the scenes. This means that the influence of our two major shareholders — the Taiwanese government and Philips — has been limited and they enjoy no special privileges. Philips was unable, even during boom times in the cyclical semiconductor business, to get extra allocation of production capacity from us. And in contrast to most companies set up with state assistance in Asia, government involvement in our company has been minimal. The government never gets its hands into our operation and that's one reason why we are able to grow so fast.

• Structural simplicity/Shareholder value
Unlike many large companies in Taiwan and Asia, we opted to remain as one company. We did not form into a business group or engage in cross-shareholdings, cross-guarantees, and so on. All the profits that we generate are for all the shareholders. There's no preferential treatment and there's no particular group of shareholders who will benefit from a certain subsidiary of our's.

We do not believe in diversifying for the sake of it. Basically, either we will hold cash, or we use that cash to expand the company. This is also a practice very different, I think, from most other companies in Taiwan.

• Financial transparency
We very much believe in financial transparency and TSMC was the first company in Taiwan to disclose its quarterly earnings. More than 400 people attend this briefing, and in the evening we host a conference call to answer questions from overseas investors.

• Low leverage
In order to grow, while weathering the ups and downs of the semiconductor cycle, we maintain a very low financial leverage profile. We always maintain a very strong balance sheet and try to hold quite a bit of cash on hand. This is similar to most leading semiconductor companies around the world, but in Taiwan terms it is unique.

Our cash reserves have even prompted questions from Taiwan's regulators, who ask why we are not doing anything with them. But our response is that the cost of building a new fab plant is extremely high — around US$3 billion — and that we are keeping the money for future investment.

Benefits

What are some of the benefits we gain from this? TSMC's price earnings (PE) and price-to-book (P/B) ratios have consistently outperformed Taiwan's high-tech sector over the period 1997-2000. During that time, we had an average PE of about 35, which was 22% higher than our nearest competitor and 59% above the high-tech sector as a whole. Our average P/B ratio was about seven times, which represented a 100% premium over both our nearest competitor and the high-tech sector. Whereas a few years ago our market capitalisation was only about 50% greater than our nearest competitor, today it is close to three times as high. I think that because of the difference in our corporate governance practices, the market has rewarded us with a very high premium.

High corporate governance standards, as well as plaudits for being "the best company in Taiwan" (as rated by *Commonwealth* magazine), have helped us to attract highly talented employees.

Challenges

In Taiwan, as in many other places, entrepreneurs and large investors who sit on boards believe that it is acceptable to influence a company's decision-making in their favour. We have had to educate our directors to understand that decisions must be made for the benefit of all shareholders. This is a continuing process, and even when dealing with some of our major shareholders, it's a challenge.

The appointment of directors is quite different in Taiwan, however, from other countries. Only shareholders can be elected as directors (which limits the pool of potential board members). Unlike the US, where the chairman has the ability to create an independent board, in Taiwan this is more challenging. We have one independent shareholder who holds a very small number of shares and was elected as a board member, giving us effectively one independent director on a board of seven people. Already this was very difficult to achieve.

Another challenge — and one perhaps unique to TSMC — is the adverse effect of trying to be transparent in a less than transparent market. What you end up with is your competitor quoting some of the numbers you have disclosed and misusing them by talking to your customers and saying, "this is what they're doing and this is what we're doing". But if you go back and look at what they are disclosing, they are not disclosing anything, so you don't know how to reconcile that. We have had to modify, and to a certain extent reduce, the level of information that we give out. But we try other means to help investors understand how we operate.

Although it is sometimes hard to predict the result of implementing good corporate governance, we are certainly happy that we began on the right foot. We will keep listening to our stakeholders, particularly investors, on how we can improve our corporate governance regime.

Panel discussion and Q&A: Douglas Henck, Harvey Chang, Andrew Sheng

Topics covered in the discussion included (in chronological order):

- The impact of culture and values on corporate governance.
- Class-action law suits/minority shareholder activism.
- Incentivising corporate leaders to practice good governance.
- Market ambivalence towards corporate governance.
- Corporate governance and society.

Culture and values

Douglas Henck initiated the discussion by asking Andrew Sheng to elaborate on his earlier comment that business could not be divorced from the culture in which it operated. Did this imply that countries in Asia needed to change their cultures in order to improve their corporate governance regimes?

Andrew Sheng: "Culture" is not something that we can easily pinpoint. It is determined by history, by institutions, by legal tradition and by business practices. Globalisation has meant that everybody is now being marked to market. In Asia we have some of the best and some of the worst in quality. When you have such wide variation you will have highly volatile prices. That is exactly what has happened. Good companies, and good markets, that deliver higher quality have lower volatility. Asia has been extremely successful. We had the Asian miracle, but why did we have the Asian crash? That's volatility. It demonstrated that when we met global competition there were parts of the system that were dysfunctional; hence volatility was high.

What we now need to do, if we want to reach global standards, is to improve on those areas where we are lacking, such as in the areas of education, safety standards, environmental standards and corporate governance standards. It's a whole package. You can't say, "Well, that's the old way I used to do it 20 years ago and I can still compete on this basis." If you want to play in the Olympics, you play by Olympic rules. It's as simple as that. You can't say, "I'm going to still play by Asian Games standards." Not that Asian Games standards are lower, but the issue is that the rules are now globalised and investors are now global. They have global choice and many will not invest where corporate governance standards are lacking.

Douglas Henck: Before July 1997 there were leaders in this region effectively saying that Asian values were the reason for the success of the Asian markets in the early 1990s. After the crash in July, that argument disappeared somewhat. Were they wrong? Was it wrong to say that Asian values provided an environment for greater corporate success than, let's say, the individual rights and freedoms that the West generally tends to move towards?

Andrew Sheng: A lot of these things are not black and white. What are Asian values? Hard work, entrepreneurism, determination to succeed, willingness to compete — these are universal values. If you talk about what you don't like, about cronyism and all that, that is also universally disliked. People don't like to be cheated. In Asia we are going through what I call the "second-generation growth pains". We had an easy ride earlier on as the world opened up with free trade. Asia adopted an open approach to global markets and succeeded through family values and a very mercantilist government approach. That worked very well, but now global competition is a different ball game, and Asia needs to meet global standards. Good companies that meet this (standard) are now being priced globally, and companies that don't are being priced locally.

Douglas Henck: Harvey, what's your view? You mentioned in your speech the lack of a level playing field in Taiwan, and that your competitors use the numbers you disclose against you. It's an interesting balancing act. What about the culture you're operating in? And what hope do you have of changing it? Can you go to the regulators and make them impose the same standards of financial transparency on your competitors?

Harvey Chang: I believe the most effective force is the market. A few quarters ago we stopped telling people what our actual average selling price was. We found our competitors were using that information to give our customers the impression we were overcharging. So we now tell the market, "If you can force our competitor to offer the same level of information, we will offer that information again. Otherwise, we can't do it." Also, many analysts were using the information we provided to better understand the financial status of our customers, whose shares the analysts were also covering. So there are always pros and cons. But culturally I don't think we can rely on the regulators. Can regulators really determine exactly what companies should disclose? I don't think so. Market forces are still the most powerful catalysts. The market continues to reward us with a premium compared to our competitors, and if you want to preserve your funding capability you better play according to international rules.

Class-action suits/minority shareholder activism

Question: I've got a question for Andrew Sheng. Do I note a softening in your personal stance on class action for minority shareholders in Hong Kong?

Andrew Sheng: No, I think you need to understand the legal traditions. We come from a British Common Law tradition that doesn't really have class action. The Common Law tradition is moving towards the idea of (strengthening) the derivative action. If minority shareholders sue, the law facilitates them. But, as you know, suing is very costly. I don't have a solution for this. The Standing Committee on Company Law Reform in Hong Kong has produced a consultation paper debating this issue and there are many different types of models. I may have some personal views on this, but it is really up to the market to decide.

Douglas Henck: Harvey, would you see the need for the minority shareholders of your company to be able to stand up and say, "We don't like what's happening"?

Harvey Chang: Right now, I think that opportunity is provided in shareholders' meetings. It doesn't happen to TSMC, but we do see a number of listed companies in Taiwan that have shareholder meetings lasting a whole day. I believe the best way to handle this is to make information available on a quarterly basis, and then to take questions on the side. We have four dedicated investor relations staff and their voicemail and email boxes are always full, mostly with questions from institutional investors.

Incentivising corporate leaders

Question: I have one comment and one question for all of you. The comment is short. When you referred to the "Asian values" that were promoted several years ago, I think the people involved had other purposes in mind. If you look at their countries, they still don't have effective democratic systems.

My question is: when you try to promote the idea of an independent board of directors, or outside members on the board, majority shareholders in Asia are usually very reluctant to consider it. They think those directors will not be working for them. So how do we come up with an incentive programme to convince business leaders that they should practice good corporate governance within their companies?

Andrew Sheng: I think the best incentive is still the market. I started off as a bank regulator and people used to ask me why Hong Kong has less non-performing loans than anywhere else in Asia. The answer was very simple. One of the leading banks in Hong Kong started requiring that all its borrowers had to go to a reputable accounting firm. It was as simple as that. The businessmen protested, but soon realised that this was good for them because they now had better information to base their decisions on. The banks had good information on which to make a credit judgement. The cost of doing this was accepted as a necessary part of good business.

It's really a question of checks and balances in the system. The market is the best check and balance. It's not that somebody's judgement is not good. But it has to be tested by the market.

You have to convince business leaders that if they want access to global capital, they have to play by global rules and this includes having independent directors who will tell them to their face that they may be wrong. If you appoint a friend who relies upon you for his salary, you're not going to get an independent view. Again, it's a cultural issue — the unwillingness to dissent.

Asia will have to find its own way because we are very paternalistic. None of us like to contradict our parents or our teachers. We don't like to contradict anyone senior to us. I believe very strongly that change will only come through ownership, not because somebody is coming up with a big stick and saying you've got to change.

Harvey Chang: I agree with Andrew. I think market discipline is certainly the major force. But I also think it takes a bit of education as well as regulatory or legal enforcement. A lot of directors do not understand their fiduciary responsibilities, or what the consequences will be if they fail. It is important to help them understand and also to see the benefits (of corporate governance). For example, an independent board is probably best able to establish a competitive compensation system for key employees. If the board is dominated by a single person, or one family, the chances of this happening are much lower. In today's environment, if you don't have good people, what is going to happen to you? Not only will you be unable to recruit top talent, but you'll lose the good people you have. I think that that is one benefit that majority shareholders should be able to see.

Douglas Henck: Let me respond to the comment about Asian values. I think the comments on Asian values a decade ago were just a façade for authoritarianism. On the question about incentivising majority shareholders, I agree with Harvey. I think it's a balance of market forces and pressure from above. Sometimes it can be pretty subtle. You can have a regulation that says audit committees should comprise only independent directors, but if this is not the case then highlight that in your annual report. Sometimes, relatively small regulations can have a big impact.

Market ambivalence

Question: Andrew Sheng quoted someone as saying that we're over-regulated and under-enforced. I'd like to pick up on that point. Why is there so little enforcement and why do we still have so much self-regulation? You keep coming back to saying, "Well, let's trust the market". But I think the market is deeply ambivalent. If it's a choice between great governance and lousy performance, or great performance and lousy governance, the market will take performance every time. I'm interested in your comments on that.

Andrew Sheng: Again, it comes back to the legal tradition: the philosophy under the old British legal tradition was one of self-regulation. But the UK's new Financial Services Act has changed all that by moving away from self-regulation and towards a mega-regulator approach. Those of us who are still operating under the older Common Law tradition have basically left a lot to the market. In Hong Kong, for example, accounting, listing rules, insurance and so on, are still self-regulatory in approach and the government has tried to stay away as much as possible. But the times are a-changing.

The US model starts with the premise that information — reliable, accurate information — is a market fundamental and everybody must file their accounts with the SEC. If you have mistakes you will be fined and you may go to jail. Then you have this very strong class of intermediaries (investment banks, brokers, lawyers), plus a class-action system that keeps everybody honest. It's very powerful and very expensive.

The British legal tradition doesn't have that. The Registrar of Companies accepts returns, but doesn't actually check whether the information is right or wrong. That's left to the accountant, and disclosure issues have been very much left to the market.

We're all in a transition mode. Because we are now global, everybody says we should follow the US model. It's not that some of us don't want to do it, but we can't change the law and market practices so quickly. And there are quite a lot of different views as to whether the American model fits the rest of Asia. It's a very difficult legal and philosophical issue. In Hong Kong we are having a very healthy debate over this. Our culture and legal framework is constantly evolving, but we can't change all this overnight.

7 Session 2

"Challenges, Strategies and Progress in Implementing Corporate Governance in Asia"

Moderator:

DR VICTOR FUNG
Chairman, Li & Fung/Airport Authority of Hong Kong

Speaking as both a company chairman and a director on several boards, Victor Fung emphasised the importance of thinking through board composition.

It is very important in this day and age that we run companies in a totally open and transparent manner. Not only because it is the right thing to do, but a well-run company of that sort translates into better value for shareholders. Unless management meets the standards expected by the investment community, a company will not achieve the P/E and the value that is due to shareholders.

I think the focus today on corporate governance is going to be on how the board really works. Reform in Asia will hinge on issues such as the composition of the board, how board members are appointed, how many truly independent board members there are, and how the board functions. These issues are particularly critical in Asia because of the domination of many boards by strong owner-managers. It's sometimes not that easy, when you're an outside board member, to talk to the guy who owns 70% of the shares (and has run the company for 30 years) and he says something needs to be done and maybe you don't agree.

Making sure companies adopt nomination committees would be a good first step in getting the composition of the board right. If the board really functions as it should, then I think we will have made a big stride forward in terms of corporate governance and transparency.

Panelist:

GARY COULL
Executive Chairman, CLSA Emerging Markets

Gary Coull gave a wide-ranging and provocative presentation on the state of corporate governance in Asia.

I have four subjects that I want to talk about this morning. First, CLSA's experience in publishing corporate governance rankings in Asia. Second, my experience as an independent director on two public companies in Hong Kong, one small and one fairly large, both of which our company floated on the stock exchange. Third, a proposal for "virtual directors", which institutional investors could use to monitor their interests in companies. And fourth, a question rather than a suggestion — because I am not sure it is in my company's interest or the market's interest — but I am very troubled by the inherent conflicts of interest in the public versus private family ownership of companies in Asia. I think there's a lot of abuse still going on, and I think that underlies many of the corporate governance abuses that we see.

CLSA's governance survey

We first published the CLSA report on corporate governance last year (October 2000)*. We surveyed about 495 companies in 25 emerging markets across 18 sectors, and we did a very detailed survey of mostly publicly disclosed information and included some queries of companies. I wouldn't call it subjective, but it was somewhere between subjective and objective. The end result was a ranking of companies by their corporate governance compliance.

Looking down the list, you'd actually be very surprised — I'm not going to go into the details — but you'd be very surprised at the appalling performance of some of the largest and best-known companies in the region, many of which you may hold in your portfolios. And you may want to think about that.

The survey found a high correlation between good corporate governance and superior financial ratios, high valuations, and good medium-term rather than short-term share price performance. We found this was true across all markets and all sectors, so that's testimony to the universal applicability of corporate governance issues. There's also a strong correlation between corporate governance and economic value-added.

The study was the first of its kind. We felt it was important to produce because of the very inconsistent nature of corporate governance in the region. But it has also been rather expensive for us. I don't want to make a big deal about this, but the reaction to the rankings was quite violent. Companies that scored well typically asked for 30 to 40 copies of the survey. Those in the bottom quartile, or even the bottom third, reacted extremely badly to it. We lost quite a bit of corporate finance business — mandates that were signed were overturned or left to expire through various means. So it's a dangerous exercise and one that I'm quite keen that we don't stand alone on down the road.

My first point is that there needs to be more than just talk about corporate governance. There needs to be more concrete appraisals of companies. Perhaps in future these could be done by industry associations, rather than individual firms, so as to protect the innocent.

Independent directors in Hong Kong

In the last ten years, I have been an independent director for two companies in Hong Kong: Sa Sa, a small cosmetics firm, and New World Infrastructure (NWI), which is one of the big infrastructure arms of the New World Group. We took both of these companies to the market and I felt it was appropriate that after we got paid our fees we try and stay helpful in the process.

In both cases the system of independents on the board has worked well because they have been respected by management and they are pretty strong and pretty feisty. Generally, it is a lot easier to have influence on the management of a smaller company like Sa Sa than a large entity such as New World. Nevertheless, in the latter company the independent directors form the audit committee and have found management to be forthcoming about the volatile operating environment in China, where NWI is active.

One problem facing independent directors in Hong Kong is the high degree of individual responsibility that they are expected to bear. For example, they are supposed to validate connected party transactions, which is way beyond the time or skill set of most of them. I don't think it's very practical... But it's important.

* It was published for a second time in April 2001.

A second major point is that independent directors need to be paid a lot more for what they do. The average in the US is around US$40,000 per annum. That's probably a minimum to ensure that you're buying the time of good people to manage these issues.*

Virtual directors

Given that there is a surfeit of smart, un- or under-employed management consultants in Asia at present, institutional investors could make use of their communication and analytical skills by hiring them as "virtual directors". This is an original idea from a friend of mine called Ian Buchanan, who works as a consultant with Booz Allen in Singapore. In essence, virtual directors would act as intermediaries between the investment community and Asian companies. They could help to validate the strategic direction of a company, monitor its performance in more detail than investors are capable of, and possibly mentor management. They could even sit on boards as direct proxies representing institutional investors. Ian's idea was to try to close what he calls the "trust gap" that exists between minority investors and emerging-market owners of businesses.

Such directors could assess the CEO and senior managers on a regular and subjective basis. In Asia there's really very little ability to assess and re-assess CEOs and chairmen of boards, because families tend to own the majority of the company and control the board. That sort of issue just doesn't come up. But there has been a huge under-performance by many Asian companies in the current economic environment. Management change and board change is needed, but there's no mechanism to deal with it.

A virtual-director scheme would also make institutional investors more active at the board level, which would be a good thing. People who own 4.95% of a business should be asking for representation. Most don't. I think groups of institutional investors should work more closely together and pool their holdings and resources to effect change, which they generally don't do. And they can be very effective publicly in challenging companies on their operations.

Lastly, a "virtual director force" could undertake assessments of companies and publish these for the benefit of the marketplace.

Public vs private companies

Tapping the public markets, enjoying their liquidity and having public shareholders is a privilege. I think it's time to consider whether it's inconsistent with that privilege to have active and competing businesses in one family where part of it is public and part of it is private. Despite the legal safeguards against such things as connected party transactions, if you want to find a consistent theme of abuse through the region, often it comes back to public versus private.

Abuse may take the form of a sweetheart deal offered to the chairman of a big property company who chooses to write it into the family trust rather than his public vehicle. In the 1970s and 80s, there were many examples of assets going back and forth like ping pong balls between public and private shipping companies in Hong Kong. The property sector around Asia, and more recently the technology business in North Asia, also exhibit quite a bit of abuse.

This is a big subject and it's not often debated. I'm not even sure myself I'd like to see what I'm recommending fully implemented. But I really think the issue is important, and that business people are aware that this is one of the many things in corporate governance that concerns investment professionals.

* Independent directors in Hong Kong typically receive only around US$11,000 per year.

Panelist:

KIKWON DOH
President & CEO, Good Morning Securities, Korea

Kikwon Doh described how Good Morning Securities learned the hard way why corporate governance mattered.

Good Morning Securities was formerly called Ssangyong Investment & Securities Company. It started life 17 years ago and belonged to Korea's sixth largest conglomerate, the Ssangyong Group.

Ssangyong Investment & Securities had been very famous. Before the Asian crisis, it was cited by *Asiamoney* as one of the best securities firms in Korea. But it failed because of a few major overseas investment decisions made by the top management. The main structural problem was that the management and the board were not separated and thus there was no "check" system that could fairly evaluate those investments. We had great people, we had a great infrastructure for retail business. (But) I can say that this company was simply a failure of corporate governance. Even such a big company didn't really have the internal systems to protect against a wrong decision by a single person. Then the government, in the form of the Financial Supervisory Commission, stepped in and gave the company "management-improvement orders", meaning that within a limited time it had to meet certain financial goals or face closure.

In late 1998, Ssangyong Securities was acquired by a consortium of foreign investors* and relaunched with a new name, new management (including myself) and a new mission. With guidance from one of our new investors, Lombard Asian Private Investment Company, and an outside consultant from the US, we began carving out a reputation for ourselves as a model of good corporate governance in Korea. We did this by:

1. Building an independent board

The board of directors was separated from management to ensure that directors could monitor management effectively. This was pretty new, and also the first time this was tried in Korea.

2. Strengthening financial controls

When I joined Good Morning, I was surprised to find such a big company managed by only two junior financial controllers. They were rarely able to produce a reliable assessment of the firm's financial performance, so the company didn't know how much money it was making from one month to the next and never had a business forecast. To rectify this, we strengthened the capability of our internal financial analysts and the role of the statutory auditor.

3. Improving disclosure

A more active disclosure policy came next. Whether it was good news or bad, we made an effort to disclose the information to our auditors, employees and investors. During the first year I joined the company, we needed to take a huge write-off related to Ssangyong's legacy. It was really bad news, but we didn't just stop after reporting it to the board. We also talked to all our employees, including the junior staff. I still remember the surprise shown by employees when I told them that the numbers I was

* H&Q Asia-Pacific, Lombard Asian Private Investment Company, the Government of Singapore Investment Corporation and the International Finance Corporation.

presenting to them were the same ones that I had presented to the board the day before.

Payback

The company's efforts to reform its corporate governance have paid off in various ways. Management has become more disciplined. We are delivering a clear message and image to our staff. And hiring has become significantly easier: we recently received 7,500 applicants from top universities for 15 new positions without having to advertise! Good Morning also enjoys good relations with regulators and the press since they appreciate the fact that the company delivers information without trying to hide bad news.

But the main payback is the trust of employees. If you ask me what is the major benefit of our corporate governance review, I can say the confidence from my employees.

What do we want to do in future? We are considering increasing the pay of independent directors to attract more talented people to that role. And we intend to continue our corporate governance reforms.

Panel discussion and Q&A:
Dr Victor Fung, Gary Coull, Kikwon Doh

Topics covered in the discussion included (in chronological order):

- Structuring a board of directors/compensating independent directors.
- Progress in Korea.
- Achieving continuous improvement in corporate governance.
- Ensuring independents provide value.
- Ranking private companies/social responsibility.
- Qualifications for directors?
- Implementing the "virtual director" concept.

Structuring the board/compensating independent directors

Victor Fung initiated the discussion by asking the panelists for their view on the pros and cons of management participation at board level. How much of a board should be composed of executive directors versus those who are independent outside directors? Should one person be both chairman and CEO?

In the UK, boards usually comprised quite a few inside directors and a fairly minimal number of outside directors. Following the Cadbury Report (1992), this has been increasing. On the other hand, the US seems to have shifted towards a model where almost the entire board is from outside, except for the CEO and maybe one other executive. Which is a better model? The UK board probably enjoys an efficiency in terms of internal workings; while the US version obviously has better corporate governance in terms of outside balance and control.

But there is a contradiction: in the US there is more prevalence of one person being both chairman and CEO (which seems to conflict with its "outsider" board structure). In the UK the functions are normally split (despite its stronger "insider" structure).

What are your views about the proper balance? What would work best in the Asian context?

Gary Coull: It depends on the nature of the ownership of the company. A family that owns a controlling stake in a business is very unlikely to hand over control of the board to outsiders, whereas a company with a widely dispersed shareholder base should be run by a board representing all investors.

On the issue of chairman versus CEO, I think that the British approach has a lot of merit. The chairman considers strategy and liaises with the board, and the CEO is responsible for running the business. The CEO's performance should be constantly evaluated by an independent board, so I think separation is broadly a good idea.

In the case of Li & Fung (Victor Fung's own company), the chairman is well out of the business. You divide up the duties quite well, and that could be a model for other Asian family controlled businesses. That is, having one respected family member being chairman and another running the business.

But your question raises another issue: how does a relatively small place like Hong Kong make available a large number of good independent board members for all our publicly listed companies? The same suspects tend to show up everywhere. How do you train and generate a pool of very good, active and independent board members? And since 1997, in particular, I think there's been a reluctance in Hong Kong to put non-ethnic Chinese into positions of influence and power. That's starting to change a bit, but for the first couple of years after 1997 a lot of the prime boards were recruiting only Hong Kong people or ethnic Chinese. There's nothing wrong with that (in principle). I think the majority should always be. But there are long-serving non-Chinese in Hong Kong who have something to offer. I don't think society should be afraid to include other races.

Victor Fung: I don't really quite see that trend. I certainly hope not. Maybe we have to do a study on that.

Kikwon Doh: In Korea most of the new directors are coming from colleges and law schools, not from other industries. This trend has been changing recently, but I think it is a big issue. Sometimes you have the right person (on paper), but they are not devoted. That is why we have to make the package much more attractive to attract the right people.

Victor Fung: I totally agree with that. But then there is the danger that increasing board remuneration — because you want to do things properly — suddenly leads to accusations that you've increased board pay too much. But I do agree that it's almost a token fee right now for serving on Hong Kong boards. It's usually an honorific thing, so only certain types of people are willing to serve.

Progress in Korea

Question: My question to you, Mr Doh, is on the progress being made in Korea. Given recent government pressure on banks to buy distressed assets from large Korean conglomerates, is there genuine progress?

Kikwon Doh: That matter is highly sensitive and I don't think I am the right person to explain it. But what I can say is that there is a big difference between what people say and what they do. If you ask any restaurant owner, he will tell you that customer service is really important. But if you go to his restaurants, not all of them will serve you properly. I think the same thing is happening in corporate Korea. Every CEO will tell you that corporate governance is very important, but not all of them are actually changing their behaviour. Only one or two may be doing it today, but as time goes by the numbers will get larger.

Continuous improvement

Question: I have a comment and a question. The comment is to commend CLSA for putting out its study on corporate governance. I think one of the major issues is benchmarking. In this audience we're talking to the believers, but we need to have a benchmark out there so people can quantify their improvements. My question relates to the issue of continuous improvement in corporate governance. Perhaps I should direct it to Victor Fung, given his responsibilities as chairman of the Airport Authority of Hong Kong. How do you see the issue of continuous improvement each year?

Victor Fung: For continuous improvement I think you have to have good board members. While the chairman obviously has a responsibility to think about corporate governance as a whole, I must say a lot of my drive and impetus comes from some pretty active and independent board members. They are constantly pushing the frontiers, so to speak. I see my job as selecting the right people, then the company can take a continuous improvement route.

Gary Coull: One thing that our corporate governance study discovered was that sometimes it is the macro-level governance environment that brings companies down. In Korea, for example, companies generally are forced to comply only with Korean GAAP, rather than international GAAP. So there's a whole bunch of non-disclosure issues that aren't the fault of the companies, but of the system that doesn't require them. Governments need to set the hurdle a little higher.

Ensuring independents provide value

Question: I have a question for Gary Coull. I think there is no disagreement about the need for independent non-executive directors to be properly paid. But I also hear a lot of executives saying that they don't want to pay money — and I have to be careful with this one — to a bunch of "nod heads", basically people who don't add a tremendous amount of value to a board. They even want independent directors to have some stake in the day-to-day functioning of the organisation, maybe through share options or stock, rather than being paid US$45,000 a year for attending two board meetings, joining three compensation committee meetings (over conference calls), reading board papers on flights, and basically coming but not providing any value. I want to hear your view on this other perspective.

Gary Coull: Firstly, the executives complaining are the people who would have recruited those independent directors in the first place. The choice of the quality is in their hands. Secondly, publicly quoted companies obviously have a legal or statutory requirement to add independent directors. If they don't understand the role of these people, they shouldn't be public companies in the first place. Thirdly, the number of people that can really add value may be a relatively small pool. So I would challenge companies to look at themselves and question their rationale for being a public company and, secondly, to improve their selection process by employing a headhunting firm.

If you run your own business and only ever listen to your own people, you will create a hierarchical structure and people will be afraid to object. You want people to argue with you. You want people to give you new perspectives. It is important that owners of companies understand these benefits.

Ranking private companies/ social responsibility

Question: Should we extend the kind of corporate governance ranking CLSA has been doing to private companies? And should we extend the criteria for what constitutes good corporate governance into the area of social responsibility?

Victor Fung: We're intimately involved, because not only do we want to be good corporate citizens, but in our business the whole concept of ethical sourcing and working with suppliers that bear up to certain standards in terms of their employment practices, and so on, are very important parts of what we do.

Gary Coull: I think it's a good idea that any large component of an economy is monitored for its contribution, social or economic, but I don't know if it's our business to be ranking companies that public investors don't invest in. There should be other watchdogs, such as the press, playing an active role in holding companies accountable. Maybe there should be some stronger consumer element here, to benchmark the large private companies. On the issue of social responsibility, I think that might be more difficult to nail down.

These rankings could be dangerous the more subjective they get. Hong Kong is not a particularly litigious place, but you're taking a stab at people and they don't like that. At least in the public sphere it can be more objective and you'd probably win most court cases. But start getting into private companies, whether they're government sponsored or not, and you're on a bit of a slippery slope.

Qualifications for directors?

Question: Victor, you mentioned that in Hong Kong there's a very small pool of directors. We have the same situation in Singapore. What I have noticed as an adviser to many boards is that while we have many prestigious people as directors, they often have a very low level of knowledge about what constitutes good corporate governance. Sometimes their financial literacy is below rudimentary, and they don't know what is required of them. Would it be appropriate to impose qualification standards? Or would that further narrow the pool of directors? Is this something that might be addressed by training?

Victor Fung: Yes, it's a very big question. I would say that over time all of these issues would be automatically improved if we moved to a system of proper compensation. You'd then get more professionals who were well trained and have less of that honorific thing.

I think it's hard for any economy to legislate minimum standards for directors. You know that they already have the right character, otherwise you wouldn't have approached them, but to say you must have at least "accounting 101", that's very difficult to tell somebody.

Gary Coull: Another thing is that the “luminaries” probably should be going more into advisory boards, because advisory boards are for people with political connections. There's actually a need for younger, less known people who are there for their competence to be coming into the ranks.

Victor Fung: That's an excellent suggestion. Advisory boards are really treated honorifically and give a lot of prestige to a company.

Virtual directors

Question: I have only one issue and one question. The issue is that if you raise the standards expected of independent directors, the best quality ones will want to go to the better known firms and you may have a sort of tiering and an unintended discrimination against smaller firms. Also, in terms of the governance systems being imposed on firms, there are costs involved. If you're a small firm, this can have a big impact.

My question is for Gary Coull. I'm just curious to see how you could implement the virtual director idea in a situation where you have a portfolio of investors, some of whom move around in relation to changes in the industry and company prospects? How would you nominate such directors?

Gary Coull: The idea of the virtual director is mainly applicable to investors who take a very long-term view. There would be an unofficial agreement between the institution that nominates the virtual director and the investee company. Templeton, for example, which might own 5-10% of a reasonable sized company, would go to the CEO and say, "I own a lot of your company, I'm gonna be here for a while, here's my friend Bob who's an unemployed consultant, he's asking questions for me, and here's what I'd like him to do. Do you agree?"

There's not enough cooperation between investment institutions at the moment. If you actually add up the holdings of Templeton, Merrill and a few others in a particular company, you might find that they have 30% of the shares, but they're not exercising their 30% influence. What there really should be is an inter-linking around the world by company holding rather than by institution. Where investors have a commonality of interests, then they need to plan in each case how they are going to manage this. If some real action needs to be taken in an investee company, and maybe four or five investment institutions are involved, then these investors could take on a virtual director to represent them.

8 Luncheon keynote

Introduction:

LINDA TSAO YANG, Acting Chair, ACGA

It is my personal privilege and a great pleasure to introduce our luncheon speaker, Bob Carlson. Bob has been my mentor for more than two decades. When I first joined CalPERS, I always looked to Bob for guidance.

I remember when we first started corporate governance at CalPERS in the late 1970s. Those were the days of greenmail. As trustees on behalf of the pensioners and active employees, we decided that we could not tolerate such abusive practices. We decided to act. There was a proxy vote at a company in the Mid-west. Its propositions were so outrageous that the CalPERS investment committee said no to all of them (and voted accordingly on the proxy form). Three days later, our chief investment officer called me. He said, “Linda, we got a call from XYZ company. They asked if we checked the wrong box?” That was the state of corporate arrogance in those days! The attitude of most companies was, “if you don't want to be in bed with us, take a walk”. CalPERS decided that it was not going to take a walk. So began the active involvement of institutional investors in corporate governance in the US.

Bob has had a long list of achievements, as you can see from his bio. Bob has served on the CalPERS board for 29 years. He was President for 10 of those years, and he is now Vice President. He still chairs the finance committee and the compensation committee and, importantly, the investment policy and procedures committee. Proper policies and procedures are extremely important in the management of a fund, especially a fund with more than US$150 billion.

Bob is a lawyer and was a former General Counsel of the California Department of Transportation. Given the extensive highways and bridges criss-crossing California, the construction of any structure would have to come to his department for guidance. Bob's long experience not only covers the pension system, but also includes every aspect of infrastructure built in the state for many years.

"The Advent of Corporate Governance: A Vehicle for Ensuring the Long-Term Growth of Asian Companies"

ROBERT F. CARLSON
Vice President and Senior Board Member
California Public Employees' Retirement System (CalPERS)

Bob Carlson began by noting that sceptics believed corporate governance was a phenomenon that could not work in Asia, because Asian companies were so different from those in the US. But while the specific techniques of US corporate governance may not all be applicable to Asia, the principles of corporate governance could still work in this region.

CalPERS prefers to invest through all economic cycles and holds positions for as long as a decade. It invests for generations of income streams, because its liabilities (its obligation to pay pensions to the scheme's one million participants) stretch out for generations. It has to invest for the length of its liabilities.

I hope to provide empirical evidence that corporate governance is in our financial best interests, and to suggest ways we may move forward to help make it a reality at our companies and in our countries.

Background

Corporate governance is no longer a US phenomenon. In many countries, companies have tended to be controlled by insider ownership or through other companies. This reduced the available shares and limited the power of outside shareowners.

The landscape has changed. Heavy fund flows from US and other international institutional investors have helped propagate standards for corporate governance and the way minority shareowners expect to be treated. According to a recent news report in the American trade press, US pension funds invested about 11% of their assets — about US$790 billion — in the international markets in 2000.

The pressure brought by shareowner activists is being magnified by the fact that pension funds and mutual funds are becoming a growing vehicle for savings in the US. Plan sponsors of these funds have a fiduciary responsibility to a large number of constituents who depend on the financial growth of wise and prudent investments. The result of this pressure has created a louder voice for shareowner rights. Please note that I use the word "shareowner", not shareholder. In my opinion, we are long-term owners of these companies — the patient capital — not simply passive holders of shares.

Why corporate governance?

CalPERS is the largest public pension fund in the US and the world. Our assets under management are valued, as Linda said, at about US$150 billion. We hold stock in over 1,600 American companies and over 750 companies abroad.

The majority of our equity assets are invested using a passive indexing strategy. Today, 23% of the fund is targeted for international investing (with 19% targeted for equities, and 4% for fixed income). We currently have about $35 billion invested internationally. Approximately $6.5 billion of that is invested in the Pacific Rim.

One of the ways we can add value to long-term returns of our portfolio is through corporate governance. If we are committed to a platform that means we don't actively buy and sell (ie, passive indexing), then we must use our influence to help improve company performance.

The CalPERS approach

In the late 1980s, we began working closely with the US Securities and Exchange Commission (SEC). We sought two rule changes — one that would bring consistency to the way in which companies reported executive compensation, and the other which would free up rules to allow shareowner communications to occur without fear of violating an antiquated rule governing such communications. We were successful in convincing the SEC to change the rules. Pretty soon we were able to evaluate company performance and compare notes with other institutional investors.

As our corporate governance programme evolved, we moved away from a specific issues approach and began to focus on specific company performance. Today, we review the performance of US companies in our portfolio in a systematic way. We compare the performance of those companies against their industry peers. That review results in a long list of companies that may be publicly identified as a CalPERS' "focus" company. Our officials then meet with the directors and chief executive officers of each of these companies to discuss performance and governance issues. The Focus List contains those firms that, at the end of the process, continue to merit public and market attention.

How do we pick those companies? We look at three factors: market performance, corporate governance practices and economic performance.

We systematically select companies that suffer poor market performance relative to their industry peers, have corporate governance policies that are less than favourable to shareowners and have suffered poor economic performance. Those companies that perform poorly in all screens are then individually analysed to determine whether governance discussions with the company's board and management could be of value and improve performance.

Our track record using this approach is very good. We have seen improved performance with such corporate giants as General Motors, American Express, Sears and Kmart, to name a few.

Adding value

You may ask what empirical evidence do we have to assert that corporate governance activism has added value to companies and increased dividends or share prices? One of the most prominent studies on this subject was published by our pension consultant, Wilshire Associates. The study was published in the Journal of Applied Corporate Finance in 1994 and was updated in 1996. It's a very important study for us, because I had questioned whether or not corporate governance activism was just going to cost us money and allow every other shareowner to ride on our shirt-tails. But we proved that we did add value.

The study looked at the stock performance of 62 companies that we targeted between 1987 and 1995. During the five-year period immediately before our first contact with these companies, they under-performed the Standard & Poor's index by an average of 89%. Five years later, after we had influenced them, the same 62 companies outperformed the index by an average of 23%. The Wilshire study suggests that we added about US$150 million each year in additional returns, against the cost of running the programme of less than $500,000 per year.

Our focus list has influenced the behaviour of many other companies that have voluntarily taken steps to improve their corporate governance rather than become the subject of CalPERS scrutiny. Simply put, the American corporate culture of today is far different than it was in the early 1980s. Good governance is something that has been institutionalised by US corporations and is very widely valued.

We have taken our years of experience and translated what we believe works into a set of corporate governance principles and guidelines. These represent the evolution and ongoing development of our corporate governance programme. They also represent the foundation for accountability between a firm's management and its shareowners.

Going abroad

You may ask yourself, why did CalPERS extend this corporate governance programme abroad? How does it differ from our US programme?

CalPERS entered the international securities market in the late 1980s not only to seek good returns, but also to diversify our investment portfolio. We decided to increase our allocation to international investments from 12% to 20% of our total portfolio.

As the size of our international holdings began to grow, we asked ourselves why shouldn't we extend our corporate governance efforts to investments outside the US? Given our fiduciary responsibility, the answer was yes. We were not free to ignore international corporate governance.

We recognised that globalisation was causing other countries and companies to reassess and adopt corporate governance to compete. With barriers to globalisation breaking down so rapidly, it presented an opportunity for us to introduce the topic and share our experience and philosophy. We started by conducting our own study on international corporate governance and, based on this, we adopted a formal international corporate governance programme in 1996. It focussed on four countries where our international exposure was highest: Japan, France, Germany and the UK. We established a set of principles for each country.

In formulating these principles, we took into account the legal, economic and cultural traditions in each country. These principles include, and I think you have heard them all today:

- Director accountability to shareowners;
- Transparent markets;
- Equitable treatment for all shareowners;
- Easy and efficient proxy voting methods;
- Codes of best practice that define the director/shareowner relationship;
- Long-term corporate vision that emphasises sustained shareowner value.

These principles are designed to complement the governance work already initiated by investors within the four countries.

Recently, the International Corporate Governance Network (ICGN) and the OECD both adopted similar principles. And I was also pleased to learn that there are efforts to advance corporate governance in Hong Kong. There is a private proposal to institute a statutory corporate governance oversight body called the Hong Kong Association of Minority Shareholders (HAMS). If it wins government support and becomes operational, HAMS would promote and lobby for legislative and regulatory reform, rate the governance practices of companies, and even possibly have the power to target serious abuse. I compliment this effort.

Governance in Asia

Another question you might ask is what role can corporate governance play in Asian investments? This is the key to this whole conference. A recent annual report issued by the Asian Development Bank (ADB) stated: "Regardless of economic orientation, strategic priorities or policy choices, Asia's recovery will depend on the four pillars of governance: accountability, transparency, predictability and participation." The ADB cites these pillars to help restore investor confidence and bring an end to the current turmoil, corporate bankruptcies and declining stock prices.

I cite here the comments of the ADB because its corporate governance philosophy is the most important, in my mind, to all of Asia. A while back we formed a partnership with the ADB and committed US$225 million for long-term private equity investments in the emerging markets of the Asia-Pacific region. The alliance was an international first both for CalPERS and for the bank. The investments have been designed to finance a variety of ventures, including industry and financial services in this region.

What makes this partnership so unique is its investment criteria. One of them is a requirement that they won't invest in companies that don't have good corporate governance. Other private equity partners doing business in Asia for us, including Lombard, Carlyle and Newbridge, also have a keen understanding of what we expect in terms of corporate governance. They seek to ensure that investments of their funds have adequate transparency, alignment of interests and that they use our principles as they make these investments.

In June 2000, McKinsey conducted a survey on the role that corporate governance plays in international private equity investments by large US investors. More than 70% of those surveyed indicated that corporate governance was as important as financial issues when investing in Asia. Some 82% said they would be willing to pay a premium for companies with good corporate governance in Japan; and a total of 89% were willing to pay a premium for companies with good governance in Taiwan. Finally, 90% were willing to pay a premium for companies with good governance in Korea.

How much of a premium, you may be wondering?

In Japan and Taiwan, they were willing to pay a 20% premium, and they would pay an even higher premium of 24% in Korea. So there is statistical data that proves that corporate governance does work.

A wish list

I would like to talk about my wish list for Asian countries and companies. I began my talk today by saying that you need not worry about CalPERS applying its US techniques abroad. I hope that you will, however, see us as your partners on the journey of improving corporate governance.

I believe that we have much in common with Asia. We both want companies to perform well, we believe that long-term strategies, not short-term shifts in stock price, will make a company profitable. We both understand that all companies, whether governed under a structure of full accountability and transparency or not, will inevitably experience both good and bad times along the path to profitability. And finally, we embrace a notion that accountable governance means the difference between wallowing for long periods in the depths of a down-phase in the performance cycle and being able to respond to correct the corporate course.

So I will close with this wish list. This is going from "talking the talk", which has been going on in Asia a long time, to "walking the walk".

First, start by examining your current practices. See where improvements can be made that would enhance efficiency and long-term business interests. Next, work with the stock exchanges to develop corporate governance standards and rules that will be in the best interest of both listed companies and those who invest in these companies. If you want to be attractive to local, as well as global money markets, upgrade your corporate governance standards. Experience tells us that those who are willing to adopt and change will be rewarded.

You will be successful if you have a well thought-out process in place to address corporate governance issues. Keep abreast of the philosophies and strategies of shareowners. In this way, you will be prepared when shareowners come knocking at your door.

Lastly, develop procedures for transparency. You don't need to change your present relationships, but you can put in place guidelines governing these relationships and disclose these guidelines to your shareowners. You can demand that those with whom you work adhere to good standards and then disclose those standards. That will help to ensure good performance, and your transparency will enhance shareowner confidence that you are doing the right thing for your company.

In conclusion, I believe corporations around the world will need to adopt good corporate governance practices to attract and retain long-term capital, both domestic and foreign, and to attract and retain professional talent, and compete effectively in the global marketplace. These companies will become more attractive to investors who value corporate governance standards.

Asia has an excellent promise for the future. I believe that the recent financial crisis offers an opportunity to install good corporate governance practices that will make tomorrow's Asian market a better one. My hope is that the confidence of CalPERS in the Asian economy and our international corporate governance programme will help.

This is my final wish: that our principles and guidelines will stimulate your thinking, even to the extent that they evoke disagreement. These disagreements can be used to formulate greater clarity of thought and, ultimately, greater consensus.

And here's my last remark. Leaders of global capital around the world will be watching and waiting to see how this will work in Asia, how you implement and carry it out, and walk the walk of corporate governance. Thank you very much.

Q&A session

Question: After the events of September 11, has CalPERS changed its view on equity investments?

Robert Carlson: Our investment committee met a couple of days after September 11 and our decision was to stay the course. We made no changes and no big asset allocation changes at all. What we did was decide that maybe this is the time to buy. Our asset allocation changed because the stock market was going down, and so our percentage of investments in equities had to be increased. So we decided to take some money out of our fixed income investments and our cash equivalents and put it into the equity market. We did that in 1987 and we came out a winner. So we stay the course and we also take advantage when the market is down to be able to buy.

Question: I understand that CalPERS incorporates a social and ethical screen when making investments. To what extent are you developing this for use in emerging markets?

Robert Carlson: Yes, we are evaluating emerging markets country by country, and we are looking at all the things that you have mentioned, from the environment to human rights, so we can have a better idea of what these countries look like.

My personal opinion is that emerging markets means changing markets. They are changing for the better and we want to find out how well they are doing in all of these areas. I hope there are not hurdles or anything that keeps us from investing there. But we need an idea of what is the risk, so you get the return for this risk. A study is underway now, but it has not been approved yet by our board. We hope some good will come out of this, so we can have entry into the emerging markets.

Another aspect of this is that it will give us an entrée into doing private equity investments in the emerging markets, because then when we pick the companies we can do our due diligence on how well they are incorporating good governance practices. So I look forward to us moving ahead faster than we do in the public markets by investing in the private markets.

Question: Can mutual funds be as proactive in corporate governance like a pension fund such as CalPERS?

Robert Carlson: Well, mutual funds are in a little different position than pension funds. They have a problem of money moving in and out of their funds, and they have to be able to sell and buy shares because the owners of mutual fund units move their money around. So they have more of a problem in being long-term investors. They will probably sell companies that are not performing (instead of holding for long periods), so they are in a different position.

Question: You mentioned that you had developed corporate governance principles for four foreign countries, including Japan. Have your principles had any impact in Japan?

Robert Carlson: No! That's a very good question. I was hoping that Japan would change quicker and move towards better corporate governance. I think I went there in 1983 right at the beginning when we started our international portfolio, and I had all the confidence in the world from then on that they would come through. Then I gave a speech in Japan a few years later and again I spoke on corporate governance. I thought that they would, again, be moving and they are not. Recently, I was at a Pension 2000 conference in Tokyo and Beijing, and I thought that Japan would have moved and done something. They haven't and so our decision now is that our portfolio for Asia-Pacific is ex-Japan. We handle Japan separately to the rest of Asia and we are under-weighted there, as you might expect. But until things turn around — and maybe with their new leader they might be changing — we will stay this course. But we have to see it first, because we haven't seen it before.

9 Session 3

"The Role of Institutional Investors"

Moderator:

DR TEH KOK PENG
President, GIC Special Investments, Singapore

Teh Kok Peng spoke about the ways in which institutional investors could move corporate governance forward in Asia.

Let me start by trying to give a definition of corporate governance. I know there are many definitions, but one that I particularly like as an investor is: corporate governance is the "enhancement of corporate performance through supervision, monitoring of management performance and ensuring the accountability of management to shareholders and other stakeholders". The key is that good corporate governance embodies both performance and conformance. How can we have more of it in Asia? There are some things that institutional investors, for their part, can do:

• Work more closely with regulators

Institutional investors often possess valuable information — based on their experience of developed capital markets like the US — about the way regulations work in practice, and what rules do and do not work. This is one area where they could work more closely with regulators; in particular, playing a role in building the broader legal, financial and regulatory institutions that Asia needs.

They could also work more closely with the international financial institutions, like the Asian Development Bank and the World Bank, to improve the effectiveness of the technical assistance that these banks provide for "capacity building" (ie, the development of a regulatory infrastructure).

• Inform the market

The better quality institutional investors could provide a "public good" to retail investors in Asia. Their skill and size enables them to do more research, and demand more financial and business disclosure. They could then publish these analyses of corporate governance in different companies.

While investors are often criticised for voting with their feet rather than being activist, voting with your feet can have a salutary effect. If you have both a carrot and a stick, then voting with your feet can be a powerful indicator of poor corporate governance.

The necessity for governance

While the jury is still out on whether corporate governance really improves performance, an analogy could be made between democracy and corporate governance. To paraphrase Winston Churchill: “It's not a perfect system. But the alternatives are worse.” Good governance, like democracy, may not produce fantastically high rates of growth, but it will produce sustainable growth. And it should ensure that a system of checks and balances is in place so that nothing goes disastrously wrong.

A private equity perspective

Private equity investors such as GIC generally don't vote with their feet because they can't. When they invest in a company, they stay for a while. How do they respond to poor corporate governance in Asia? In the following ways:

- **Taking controlling stakes:** In such cases, the issue of bad governance is less likely to occur. The new investors are in charge and they try to put in place all the right structures. The managers are conducive to good corporate governance because they are owner-managers, or they are fully accountable to the new owners.
- **Aligning executive compensation and improving the board:** Private equity investors typically implement compensation structures that are performance- and compliance-based. They also put in place structures that improve financial reporting and controls, risk management and legal compliance. And they appoint directors who have the expertise to take companies to the next stage in their business and oversee the structures required.
- **Enhancing performance and conformance:** A private equity investor seeks to enhance the value of the firm in a sustained way so that they can exit the investment and return the money to their investors. To achieve this, they need to put in place good corporate governance.

GIC's experience

GIC Special Investments started investing in private equity in the US, and later Europe. Although based in Singapore, we have only invested in Asia since the beginning of the 1990s. To a certain extent we got caught up in the Asian miracle and learned the importance of transparency the hard way. There was a lot of money sloshing around, and yet, no matter how you worked the numbers, the returns just didn't pan out. We have done investing in Asia before the financial crisis and, of course, we have paid for it. But fortunately, the bulk of our investments, because of the way we started, were in the US and Europe and these have done well.

The question we need to ask ourselves is: in a globalised world, with global investment opportunities, how do you ask people to invest in Asia when corporate governance standards in general are not so good? And the returns are not as good as you can get in the US, which has better governance and lower risk. We continue to invest in Asia because we think that there's scope for diversification. We also think there is an interesting story to tell about Asia. All of us hope that Asia will continue to reform, although the pace has been quite disappointing so far.

We are also grappling with the concept of transparency. I am not sure to what extent we see economic life and competition as a zero sum game, or whether it's also a win-win activity? Before coming to Hong Kong for this conference, I asked to meet some of the venture capital funds that GIC invests in, or would like to have a relationship with. I was struck by the fact that none of them wanted to see me as a group. I wanted to see all of them together, because I didn't have much time. I wasn't interested in hearing all the intricate details of their deals, I just wanted a broad market perspective. My staff told me that they were happy to see me one-on-one, but not as a group because there were sensitive trade secrets or intellectual property rights that they did not want to reveal. This reminded me of an incident in Silicon Valley a few years ago when I got a similar group of top venture capital funds together. While they were competitors, that didn't stop them from being friends or exchanging ideas. If you look at Silicon Valley in detail, despite the crash and so on, there's a culture of working very closely together. Maybe that's one lesson we can learn from there.

Panelist:

IAN FARAGHER*
CEO, Chubb Insurance, Hong Kong

Ian Faragher explained in pointed terms why good corporate governance was of critical importance to insurers, and what insurers expected of directors and companies.

Why, you may ask, are people in the insurance industry concerned about corporate governance? It is, in fact, our business. It's the insurance industry that provides the coverage for directors and officers who are exposed to risk. The policies we write kick in when something goes wrong and liability raises its ugly head. When directors and officers drop the ball out of incompetence, ignorance, lack of judgment — it's a long list — negligence, dishonesty, bending the rules or just good old-fashioned greed, it's the insurers that have to deal with it. This is no exaggeration.

Banking on the wrong guy

We recently had a situation in Hong Kong with a bank that had provided substantial mortgage loans to a lawyer for three of his clients. The lawyer was approved by the bank and retained by it. The bank released the mortgage funds to the lawyer in early 1997; the total sum was in excess of HK$25 million. The bank's loans department believed that the loans were fully secured by property. But as late as May 1998 — that is, 18 months after releasing the funds — the bank continued to ignore its own internal control procedures by failing to insist on title deeds for the loans. Finally, in May 1998, the bank undertook a land search on the three properties for which it had loaned money. The search revealed existing encumbrances. It also showed that the assignment of the mortgage deeds in favour of the bank had never been submitted by the lawyer. In other words, the bank had been taken for a jolly good ride as there was simply no collateral for the loans. In fact, the whole scheme was bogus.

There are several issues that relate to governance in this case:

- **Laxity:** The bank's loan department had been lax about making sure that the properties being mortgaged to it were free of any lien and that the bank's interest was registered. This was unpardonable.
- **Poor appointment process:** The process and value judgment relating to the appointment of lawyers to handle mortgage business with the bank appeared to be most casual.
- **Opacity:** The bank knew it had problems with this lawyer from as early as January 1998, but deliberately withheld this knowledge from us (which contravened its policy with us). It hoped that the lawyer would trade his way out and repay the money. But he didn't and the bank did not inform Chubb of the situation until February 1999, two years after the loans were first released and 13 months after it first became aware of the problem. Needless to say, we were not particularly impressed and its claim was withdrawn.

The moral here is that sound corporate governance would have prevented this situation, both by minimising the loss and setting the scene for an insurance recovery.

But, more importantly, business today is facing risks of greater complexity and diversity, complicating their responsibilities and the personal liabilities of directors and officers. New laws, recent court decisions, shareholder activism, the activities of groups such as

* Mr Faragher is now head of Chubb's Greater China operations and is based in Shanghai.

non-governmental organisations and environmental lobbies are all raising the ante by defining more broadly the responsibilities of directors and officers. Because we write the policies that cover these risks, we have a vested interest in knowing who runs companies and how well they are run. We are very partial to good corporate governance at the board and senior management levels.

Proactive self-protection

In my role I meet with a number of boards throughout Asia and have noted a significant increase in awareness of corporate governance over the past four years. As their insurance covers the personal liabilities of the directors, it is vitally important for these individuals to understand both governance and its inter-play with directors and officers (D&O) liability insurance.

Risk management or loss control is a concept well known to modern corporate management. Over the past decade the benefits of a well-designed executive protection risk management programme has also become increasingly apparent. In addition to the clear risk reduction benefits, proactive management of director and officer exposures can improve a company's ability to recruit talented management and directors. Importantly, however, it enhances the quality of corporate decision-making.

The sophistication of D&O markets throughout Asia varies considerably. There are still many in which this is not a common component of the risk management corporate strategy, whereas in other markets it would be rare for a public company not to carry a D&O programme. We also see a significant demand from corporations that intend raising capital overseas or which have foreign independent directors and employees. In my own case, when asked to sit on a board, a personal concern is both the level and, perhaps more importantly, the quality of the D&O liability insurance.

The fundamental goal of any D&O programme is to sensitise the company's executives to the fact that virtually everything they do creates the potential for second-guessing and, perhaps claims, by persons adversely affected by their actions and decisions. From our point of view, directors and officers need not be flawless in their decision-making, but they must fulfil three essential duties. These are the duty of diligence, the duty of loyalty and the duty of obedience. They are, if you like, our three commandments. What do they mean?

The three duties

First, diligence requires executives to act in good faith and be consistent with what a reasonably prudent person in a comparable position would do under similar circumstances. Prior to making a business decision, executives need to obtain and consider all material information reasonably available to them.

Second, loyalty implies that a company's executives must not engage in personal conduct that would be prejudicial to the corporation or take advantage of the corporation. We would suggest that they should even avoid any appearance that they may have misused their position of trust for their private benefit.

Third, obedience means that the directors and officers must perform their duties in accordance with applicable laws and statutes and, importantly, within the company's articles of incorporation.

The way we at Chubb see it, superior corporate governance occurs only if a company-wide commitment to excellence and discipline exists. Board members and senior officers must remember that their job is to serve the interests of both the corporation and, importantly, its various constituencies. Executive decisions should be thoughtful, informed, made by disinterested parties and fully documented. We believe that good corporate governance is simply good business and we work with and support those companies that are honestly and decently governed.

Panelist:

NAWAAPORN RYANSKUL
Former and first Secretary General
Thai Government Pension Fund

Nawaaporn Ryanskul spoke candidly about the role of pension funds in Thailand's emerging corporate governance system, and touched upon some new developments in political and commercial awareness of governance.

The Thai Government Pension Fund was set up in 1997 with a big endowment. When it started investing, it decided that whatever standards it wanted other people to adhere to, it would have to follow itself first. So corporate governance starts at home. We have to practice what we preach.

As an investor, the Fund insists on counterparties, including issuers of securities, its fund managers and everybody that deals with it, having a structured governance programme. We don't wait for the shareholders' meetings to raise our concerns. We have analysts' meetings and we talk to companies themselves. We speak out loud, not in the press, but directly to companies that we are interested in. With fund managers, we do the same thing. Even with our private equity investment managers, we will raise these concerns during contract negotiations and then review their work.

There are three public pension funds in Thailand: the Government Pension Fund; the Social Security Office; and the State Enterprise Provident Funds. They have a public duty to set high standards, not because they should be crusaders, but because they can use their size to good effect. In fact, only the Government Pension Fund has been particularly active in corporate governance to date. The others have yet to invest significantly in the capital markets. But once they start investing, I think they will have to raise the same concerns as we have been doing.

The pension fund industry in Thailand is very fragmented. Each company has its own fund and these are usually too small to pay a lot of attention to corporate governance. Their directors are not well equipped to do their jobs, and most companies are more concerned with business operations than their staff funds.

They think that by hiring fund managers, they can forget about the issue. Fund managers just manage, they don't look at how to improve the environment so that they get a better return. State enterprises fall into the same category as private pension funds in this regard, but they have started to do something. They know that by banding together, and exchanging ideas, they can have some say in the market. I think, in the future, you will see more activity in this field.

As for the government's effort to improve corporate governance, there has been a lot of promotion and a lot of concern, but we yet have to see things put into practice.

New developments

Political factors play a very large role in Thailand, so we cannot bring about corporate governance reform without trying to make politicians aware of the situation as well their duties. I will give you three interesting examples involving the Minister of Interior. In the first case, he created a big uproar when he tried to enforce the law. Everyone thought he was doing something very drastic, but he said simply that if you don't follow the law, then you may as well abolish the law. As long as the legislature had passed a law, it was his duty to try to enforce it.

The Minister has also tried to be very transparent and accountable in certain administrative matters. In recent months there was a change in the appointment of district governors, so he set up clear rules as to who could qualify, what the qualifications for promotion were, and so on. I think this is something very foreign to Thailand, because people are so used to other criteria. It is a good start from my point of view.

The third example again involves accountability. In Thailand, especially in the public sector, accountability is linked to the budget. As long as you stay within your expenses, you are safe. But the Minister is trying to make people more accountable than that, and has set up a test programme. He has made three or four district governors the chief executive officers of their provinces and is benchmarking them against different systems: certain districts are defined as "old systems" and others as "new systems", and he will evaluate them at year-end to see which system works best. Even though he didn't use the words "corporate governance", I think these reforms are moving in the right direction and I am very encouraged by that.

On the economic front, the Security Exchange Commission and the Stock Exchange of Thailand have been trying to promote corporate governance. Among other things, they set up the Thai Institute of Directors, which has trained several hundred directors already. I was the first fellow of the institute and was in the first batch of about five or six people who dared to take the examination!

Other activities have included disseminating international best practice to local listed companies, and allowing some self-regulation within pension funds (as in the Government Pension Fund) rather than only relying on prescriptive investment limits. There is a willingness to change in Thailand as long as you let people understand the essence of the thing first. If people don't understand the essence of the word, and there is only the promotion of the form, you will end up having the proper form but nothing in it.

Panel discussion and Q&A:
Dr Teh Kok Peng, Ian Faragher, Nawaaporn Ryanskul

Topics covered in the discussion included (in chronological order):

- Assessing corporate governance in investee companies.
- Articulating your governance criteria (as an investor).
- Proactive investment protection in China and Asia.
- Corporate ties with government — upsides and downsides.
- Assessing bribery.

Corporate governance in investee companies

Question: I would like to return to the question of the role of private equity investors raised in Teh Kok Peng's speech. I agree with what was said, but I think that during the due diligence process investors must make an assessment of the willingness and ability of an investee company's management to understand and implement better corporate governance and to accept that it is a fundamental part of their objectives. If you don't have this understanding, whatever is written down will not really do any good.

Teh Kok Peng: Absolutely, I agree. I think you're operating in an environment where the awareness of corporate governance is still low, so you wouldn't apply the exact same standards as you would in the West. In our investing, if we don't think the senior management or the majority owner is responding satisfactorily to the corporate governance issues we pose, then we try to get to know the middle management a few layers down. If we are not satisfied, we don't invest and try to improve them, even if we like the business, because there are certain battles you just can't win.

Articulating your governance criteria

Question: I really have a comment rather than a question. Some studies show that institutional investors will pay a premium for companies with good corporate governance. But why should we be willing to pay a premium when there are no clear corporate governance dividends that we can cash at the bank? Institutional investors need to make it more explicit that what they're really talking about is risk: that good governance reduces risk and bad governance increases it. What institutional investors should be looking for are risk-adjusted rates of return. I think you see this no more clearly than in the US market right now with the case of Enron. Despite winning awards from *Fortune* magazine, it has just seen billions of dollars wiped off its market capitalisation due mainly to bad transparency and accounting. So I think there has to be a little more articulation from institutional investors as to precisely how corporate governance makes a difference to their investment criteria.

Teh Kok Peng: Yes, I agree with that. In fact, I have a little story to tell. Some years ago, Enron approached us to invest in a certain fund with them. But the terms of the fund involved such conflicts of interest that we decided not to do it.

Ian Faragher: What we see when evaluating companies is that things can change very rapidly. You can have a company where things are going very nicely, they have a relatively simple system of corporate governance, then things change and the system is inadequate. As the saying goes, you never know “who's swimming naked until the tide goes out”! That's really the case with a lot of these companies. We find that corporate governance takes an enormous amount of work on our part to continually re-evaluate the situation.

Proactive investment protection in China and Asia

Question: China is trying to improve its corporate governance and also bring in more institutional investors to stabilise the market. But there really isn't corporate governance in China right now. And now, of course, we've had the recent suspension of the sale of state-owned shares because the market's falling which is a blow to corporate governance. This is a chicken and egg situation. How can it be resolved?

Teh Kok Peng: I think that at the regulatory level there is a tremendous desire and determination to improve things. One piece of evidence is the fact that a former deputy chairman of the Hong Kong Securities and Futures Commission, Laura Cha, has been persuaded to go to China to be a vice chairman of the China Securities Regulatory Commission. It's quite something to appoint somebody who was not a Chinese citizen previously to a position equivalent to a vice-minister, and she had to relocate from Hong Kong to Beijing.

Another piece of evidence is that China is in the process of opening up its mutual fund industry to foreign-invested joint ventures. The government has made it very clear that they want these foreign funds to introduce international best practices — although a lot of institutional investors do not see the Chinese public equities market as ready for them.

But if you are a private equity investor, you can take controlling stakes and protect yourself. Or, if you only have a minority stake, you can still get people on the board (and certain decisions have to be made by the board). I think you can substitute these other kinds of control mechanisms in situations where market opportunities are good yet regulatory regimes are still immature.

Nawaaporn Ryanskul: When you look at a market and see nothing to invest in, because no one has good corporate governance, perhaps you need to talk to the companies that do appear to have some future. We sometimes find that companies do not do what we think is good governance simply because they don't understand it. If you ask them to do certain things, often they will. It's what I call our developmental role. We go in early, try to explain and see the result. Most of the time they'll listen — especially in big companies where people expect them to know all these things.

Ian Faragher: I would like to echo Nawaaporn's comments. What we have found is that a lot of the risk management that goes with a proper corporate governance programme is not always expensive to do. They are just very good internal procedures that should be implemented. I think both Dr Teh and Nawaaporn are saying that you've got to take an active role. If you get in there, explain why it's really good business practice, we've found a number of corporations to be very receptive. Those that don't, don't get the investment.

Corporate ties with government

Question: A lot of companies in Asia have close ties with government and so are protected or subsidised to some extent. So, in a sense, poor governance helps corporate sustainability. As an investment fund, would you rather invest in companies that have the backing of government (despite their poor governance) or in companies that are independent but have good corporate governance? And what is the role of investment funds in Asia in general, because this doesn't just apply to China with state-owned enterprises, but also to companies in Asia that are controlled by tycoons who have very close ties with governments?

Teh Kok Peng: I'm not sure I can give a broad answer, but I would say that we would look for sustainable performance. When you invest in a company you are looking forward as to what will happen, and many things can happen. The government can change and therefore the relationship changes. In the case of Malaysia, for example, there were some companies that were closely associated with Anwar Ibrahim, and when he had to leave government I think quite a lot of companies associated with him suffered. If I can just give an example from GIC. Years ago, when Indonesia was under Suharto and was booming, a lot of people felt that you had to deal with his children or you couldn't do anything in Indonesia. We declined to do so, not because we foresaw exactly what was going to happen during the Asian financial crisis, but we thought that it was not something that was sustainable. We didn't want to take advantage of the patronage that his children had and get a rent-seeking advantage. Any advantage that is given by the government can also be taken away. It's not a genuine competitive advantage.

Ian Faragher: What you're talking about is looking at long-term fundamentals and I think good corporate governance establishes such fundamentals. The whole idea of corporate governance is to balance the competing, but often similar, interests of the various stakeholders and that gives long-term sustainable advantage. But a political advantage is rarely long-term.

Nawaaporn Ryanskul: Sometimes people never learn, do they?! During the heyday before the Asian crisis, bankers would go and lend to countries and companies that financially were not sound, thinking that they will be the first ones to get out. And when there is a financial crisis, they blame the companies and they blame a lot of other people, except themselves for being too greedy.

We have to find a balance when we are working with other people's money. We want a profit, but we cannot be greedy by going and gambling. We have to make sure that the external environment does not have too many surprises, because there are enough surprises to manage already. Because of politics some funds shy away from certain countries altogether, even though there are some good companies there. But there are other funds that are willing to bet on certain sectors in a country, because they think that that sector will survive all the political uncertainties.

Assessing bribery

Question: What specifically do you look at when examining a company to make sure it is not offering bribes to public officials? With the OECD's Convention Against Bribery, most overseas countries have passed laws to make this practice illegal (although it wasn't until as recently as a year ago in some places). The US has had the Foreign Corrupt Practices Act for a long time, but there's only been about 30 convictions. So the presumption is that there is still some bribery happening. That presumably is not within the realm of good corporate governance. What are some of the red flags you would look for to make sure bribery is not occurring?

Teh Kok Peng: I'm not sure that in every company we go into we would have the antenna and ability to detect whether they have given bribes in the past. What we try to do is assess the whole tenor of their governance. It seems to me that a company that makes bribe-giving a customary practice would reveal itself when you probe its senior and middle management. It will show instances of bad corporate governance in other areas as well. Obviously, if you ask them whether they give bribes, they will say no. So you try to get a measure of the air quality, so to speak, within the company and then avoid them if the level is not high.

Ian Faragher: From an insurance point of view, one of the things that you look at is the structure of the committees set up within a company to review its decisions. If a company is highly centralised, with no accountability of people and little transparency, then obviously it's going to be more prone to bribery. It's very difficult to detect, but I think you would be more suspicious in a company where decisions are not reviewed by any outside people.

10 Session 4

"Regulatory Trends"

Moderator:

BARRY METZGER
Senior Partner, Coudert Brothers, New York

Barry Metzger presented a critical assessment of the slow progress in corporate governance reform at the firm level in Asia.

I like to think of corporate governance as a mosaic composed of four mosaic tiles.

The first mosaic tile is composed of laws and regulations: company laws, securities laws and regulations and, of somewhat less direct relevance but nonetheless important, bankruptcy laws, competition laws and certain provisions of the criminal law.

The second mosaic tile is enforcement: it is enforcement by regulators and also by corporate stakeholders, who can go to court when they believe their rights have been infringed. It is also the exercise by shareholders of their rights within the corporation, such as by proposing resolutions at the general meeting of shareholders.

The third mosaic tile is non-binding standards: corporate governance codes of best practice, which have received a great deal of attention within the region in recent years, are good examples of such standards.

The fourth mosaic tile is market practice: ultimately, the objective of corporate governance is to have a market that incentivises good corporate governance behaviour and sanctions bad behaviour. Market practices are in part a reflection of market infrastructure, which includes the very important role that can be played by analysts at financial intermediaries and by financial journalists.

The four years since the onset of the Asian financial crisis has been a period of remarkable legislative and regulatory activity affecting corporate governance. How far have these changes taken us and where are they going? I would like to address two subjects. One is convergence: the extent to which we see across a variety of countries similar approaches to corporate governance reform. The other is creating a scorecard to evaluate progress-to-date.

Convergence

When we look across the region at changes in corporate governance laws and regulations, I am particularly struck by something I read about a year ago — an article entitled "The End of History for Company Law" by two American law professors. If you'll indulge me for a moment, I'd like to read from an abstract of that article:

> "Despite the apparent divergence in institutions of governance, share ownership, capital markets and business culture across many different economies, the basic law of the corporate form has already achieved a very high degree of uniformity and continued convergence is likely.
>
> "The principal reason for convergence is the widespread consensus that corporate managers should act exclusively in the economic interests of shareholders, including non-controlling shareholders. This consensus on a shareholder-

oriented model of the corporation results in part from the failure of alternative models, including the manager-oriented model that evolved in the United States in the 1950s and 1960s, the labour-oriented model that reached its apogee in German co-determination, and state-oriented models that until recently were dominant in France and much of Asia.

"Other reasons for the new consensus include the competitive success of contemporary British and American firms, the growing influence worldwide of the academic disciplines of economics and finance, the diffusion of share ownership and the emergence of active shareholder representatives and interest groups in many jurisdictions.

"Since the dominant corporate ideology of shareholder primacy is unlikely to be undone, its success represents the end of history for corporate law. The ideology of shareholder primacy is likely to press all major jurisdictions forward towards similar rules of corporate law and practice. Although some differences may persist as a result of institutional or historical contingencies, the bulk of legal development worldwide will lead towards a standard legal model of the corporation. For the most part, this development will enhance the efficiency of corporate laws and practices."

I think that may be a bit simplistic in downplaying continuing differences in corporate law rules between different countries. But when we look across Asia over the course of the last four years, it's quite striking how many countries have chosen from the same smorgasbord of alternatives in corporate governance reform, with a very strong emphasis and reliance upon the importance of independent directors on boards, the role of disclosure, enhanced accounting rules and auditing principles, and reliance on director and managerial accountability to shareholders.

The scorecard

As we look at corporate governance reform in the region, we often say that we are only four years on, that we remain in the very early days of the process and that there is much to be done. But I think we need to evaluate progress to date, particularly at the firm level, to do a scoring and to create a scorecard of successes and failures. It may take years to develop a comprehensive regulatory system and to mobilise market forces across the entire market of publicly listed companies. But, at the firm level, the changes in corporate governance practice that matter often require only a matter of months to implement; though there are some elements (such as changes in internal accounting and information standards) that may take somewhat longer to implement.

At the firm level, four years on the record of achievements in my view is unimpressive and disappointing. There are too few market leaders, that is, companies whose standards of corporate governance practice are not measured by the minimum standards prescribed by law but are an embodiment of best-practice standards that serve as a model for other players within the market place. There are too few institutional investors who are being seen to aggressively demand reforms in corporate governance at particular companies. There are too few examples of shareholder activism in internal corporate forums and in the courts. And there are too few examples of the government as a model shareholder because, in a number of countries around the region, the government remains a significant shareholder in firms listed on the stock exchanges.

Where are the market leaders? Why aren't there more of them? And what is necessary to develop them further? These are among the questions that we have been grappling with in our discussions today and we will further address in our panel. In this regard, I think it is particularly important that we are beginning to see benchmarking —

individual-firm ratings in the corporate governance area — whereby we go from simply looking at a set of market standards set out in regulations or best-practice codes to a company-by-company evaluation of their corporate governance practices and record.

Panelist:

LAURA CHA
Vice Chairman, China Securities Regulatory Commission, Beijing

Laura Cha gave a concise and frank overview of some of the challenges facing corporate governance reform in China, and how the regulator is responding.

The responsibility of the regulator is to maintain market discipline and integrity so as to ensure confidence in the market. Without investor confidence, a market will lose its capital-raising function. Investor confidence comes from certainty in the rules and the knowledge that they are being treated fairly and equally. Therefore, from the regulator's point of view, the most important reason for ensuring good corporate governance is to enhance investor protection and foster investor confidence. The key consideration is how much should we prescribe before regulations become a burden on companies and interfere with their efficiency?

It is generally accepted that regulations should aim at preventing, or discouraging, conduct that would cause harm to the investors. Regulations should not impede the ability of the management to make commercial judgments, or interfere with the operation of a company. While creating sufficient deterrent effect, the benefit of regulations should always be balanced with the cost on those regulated. Regulators cannot foresee all possibilities of malfeasance or misconduct and, therefore, should not aim to prevent all. Nor should regulators attempt to regulate every aspect of corporate behaviour and become a nanny for the corporate world. In the area of corporate governance, it is believed that the regulator should set down core principles and minimum standards and leave the companies to determine the extent to which they practise these to ensure shareholder value.

Differences in China

We believe that incentives for good corporate governance will come from the market (as reflected in the value of a company's shares). However, in a market such as China, where a lot of the fundamentals are really not considered by investors, market incentives do not have their normal value. In an emerging market like China, we need to take a somewhat different approach. Or rather prescribe stronger medicine.

Let us look at some of the key elements of corporate governance. It is often said that the clear segregation of ownership rights and management responsibilities is important. There is timely and full disclosure of information to the public, there is proper internal control to ensure accountability of board and management, there is the avoidance of conflicts of interest, and equal and fair treatment to all shareholders.

• The "three separations"

I would like to say a few words on what we are doing in China. First, the separation of personnel, assets and finance between a controlling shareholder and a listed company. This is what in China we call the "three separations". This relates to the clear segregation of ownership rights and management responsibility, as well as the clear and separate identity of the listed company. Some of these principles are fairly straightforward and may not seem that unusual or particularly important in the Western world. But for China, where most of our listed companies are restructured state-owned enterprises, these are very real issues.

In some ways the situation in China is not that different from the rest of Asia, where most of the owners of listed companies are the founding families and control one big block, whereas in China that controlling shareholder is the state. But the difference between those families and the Chinese state is that the interests of the former is usually aligned with their management (as they themselves manage the company). These family interests in many cases are not that divergent from the minority shareholders, because it is in their interest to run their listed company well and reap the benefit.

But in China's case it is somewhat different. The interests of the state, although it is the controlling shareholder in many listed companies, are not clearly reflected in the management or properly represented. The management is appointed by the controlling shareholder, but because most managers are former government officials they tend to look at a listed company as a windfall for them. On one hand they may not have the right experience to run a listed company and, on the other hand, they still see the listed company as part of government. And so we have some very murky situations where the controlling shareholder has been misusing the funds of the listed company. There is no clear separation of personnel. The same person may serve as an officer or as a board member of the controlling shareholder and at the same time serve on the listed company.

When the basic corporate culture itself is not clear, and you add to that these murky and overlapping responsibilities and ownership rights and management responsibilities, it becomes even more egregious. Some recent cases in China show that some controlling shareholders have all along used their listed companies as their own little ATM machines. When this is discovered, they say they cannot repay, so it is the listed company that suffers. Examples like this are quite egregious and we try to deal with them over the short term by enforcement, but in the longer term there really needs to be an emphasis on good corporate governance.

As you know, assets in China are often spun off from controlling shareholders into new entities so that they may become listed vehicles. After listing, the assets and titles are sometimes not clear, the transfer is not complete and minority shareholder interests have been impeded. Examples like this are quite abundant. So for us in China, the importance of giving a listed company a separate and independent identity cannot be stressed enough.

• Over-regulation

It has often been said that to avoid allowing a controlling shareholder to take advantage of a company through connected transactions, you need rules that require disclosure and, in some cases, approval of such transactions by independent board members or minority shareholders. But we also realise that we cannot impose this type of requirement too often or make it too onerous, otherwise companies might miss business opportunities. One tends to go overboard and I know that the CSRC sometimes tends to over-prescribe to compensate for the misconduct that may have occurred. Which leads to another problem for the regulator: do you try to stamp out a few instances of misconduct and then punish the other 98% who are largely complying with the law? It is a tough case and it is very difficult to strike a balance, but in an emerging market like China one tends to over-prescribe.

• The value of independent directors

Some of you may have heard that China has recently issued directives requiring listed companies to have two independent directors by June 2002 and three (or up to one third of the board) by June 2003. As we have more than 1,100 listed companies, that would mean we will require more than 3,000 independent directors over the next 18 months. So a very logical question has been asked: "Where are we going to find all these directors?"

I emphasise time and again, and I will do it here, that we do not believe that independent directors are a panacea for internal controls and good corporate governance, but we must take the first steps. There are a lot of people who are keenly interested in the running of listed companies. There are investors. There are all kinds of books on the stock market. There are academics who write articles and critiques of various issues on corporate governance. We believe that by requiring a certain number of independent directors, we will begin a culture of awareness about the importance of corporate governance.

We fully recognise that independent directors may not be as effective as we would like them to be over the next three years or so. We are offering training courses that give a basic understanding of the fiduciary duty of directors, but it is a big task in China. We realise that if we put too onerous an obligation on independent directors we may discourage people from becoming independent directors. And we also know that true independence is not easy to come by. Even in Hong Kong and other parts of Asia, it is quite common to appoint people friendly to the board to this role.

We are also using training courses for investor education. We hope that by publicising the role of independent directors and the importance of corporate governance, there will be an increase in the awareness of what is required of company officers and board members. And we hope that the media, or rather public scrutiny, will help us create pressure for change. Pressure coming from the market is, I believe, much healthier than from the regulator.

Intermediaries need governance too

Finally, let me say just one more thing. We always stress corporate governance in listed companies. But from a regulator's perspective, the governance of intermediaries is also extremely important. By this I mean investment funds and brokerage houses in China and elsewhere in the region. We have found, particularly in times of market downfall, that there are issues in some of the smaller firms that find themselves in financial trouble. If you trace the problem, you find it is often because they did not have good risk management or internal control, or a good corporate governance structure. Perhaps the good governance of intermediaries is even more important than that of listed companies? We are hoping that awareness of corporate governance among listed companies will extend to intermediaries, and we are also trying to require our intermediaries to have independent directors.

Panelist:

FREDERICK HU
Managing Director and Head, Greater China Economics and Strategy
Goldman Sachs (Asia), Hong Kong

Frederick Hu argued persuasively for greater convergence in regulatory standards in Asia and for the creation of an "enforcement culture".

I have three observations that I would like to present. One, Asia faces a growing need for convergence in regulatory standards. Two, it is really important for this region to foster an enforcement culture. Three, it is critical to involve and empower all market participants, especially investors, for the sake of achieving better corporate governance.

Wanted: A regulatory umbrella for Asia

The rationale for convergence in regulatory standards is very clear. In today's global economy, capital moves across borders and companies and governments seek to raise it. Investors come from all corners of the globe so the divergence in regulatory systems — the lack of harmony in national laws, regulations and rules affecting financial markets — has imposed a barrier to the efficient allocation of capital globally.

In particular, the poor standards of disclosure and investor protection in many emerging market economies have significantly increased the risk premium, the cost of capital, and hence reduced capital inflows that otherwise would have contributed to economic growth and raising living standards.

My proposal at this conference is that regulatory authorities in Asia should form a pan-regional consultative body, perhaps under the umbrella of the Asia-Pacific Economic Cooperation (APEC) forum. This body should meet regularly. It should identify critical regulatory differences, loopholes and deficiencies between its members and set sufficiently stringent, yet achievable, regulatory standards. And it should formulate appropriate guidelines and action plans for members so that they reach these standards.

Such regulatory cooperation has already taken place among members of the Bank for International Settlements (BIS), culminating in the Basle Accords. I believe there is a strong case for Asian regulatory authorities to move in that same direction. The Hong Kong Securities and Futures Commission and the China Securities Regulatory Commission (CSRC) should take the lead in this process. There are already active informal contacts and cooperation between these two agencies. But I believe there is scope for this kind of interaction to become more formalised and better structured, with a systematic review of their respective regulatory systems and the steps that could be taken to harmonise them.

There are already a significant number of mainland companies listed in Hong Kong as red chips and "H" shares. In fact, these Chinese companies now account for about one third of Hong Kong's market capitalisation. As China deepens its state-enterprise privatisation and restructuring, this list will grow. The potential adoption of schemes such as CDR ("Chinese Depositary Receipts") would add to the need for regulatory consistency between Hong Kong and China. The growing financial integration of the Hong Kong and Chinese markets would clearly be an important catalyst for achieving regulatory harmony throughout the region. Effort must be made to embrace cutting-edge regulatory models and best practices, which I would refer to as the Anglo-Saxon system. This is perhaps controversial, but when I talk to investors globally they seem to accept this view.

A common excuse is that the bar should be lowered because markets are less developed in emerging economies. But I would take an opposite view. As a latecomer, there are so many mistakes and lessons to be learned, so much experience to be borrowed, and so much knowledge and skill to be leveraged from the developed markets. There is a real possibility to close the regulatory gap quickly and even leapfrog in some areas. Laura's comments about the CSRC's new guidelines on corporate governance show that if these initiatives were fully implemented they would actually place China ahead of many Asian and emerging market peers.

Foster an enforcement culture

There is really a lot for Asia to do: introduce new laws and regulations; amend and update existing ones; and build a sound regulatory infrastructure. But at the end of the day, capital markets cannot develop and corporate governance cannot improve as quickly as reformers would wish if the enforcement is not there. There remains a large gap between what the law says and how the market behaves. Regulatory bodies in the region face credibility problems. In this regard, I am impressed with what the CSRC has been doing to step up enforcement, whether it is about investigating and disciplining listed companies for misleading financial accounts, or cracking down on market manipulation by investment and securities firms. All these actions have sent a strong message to the market that the CSRC is serious about enforcing securities laws and regulations.

Empower investors

While I cannot emphasise enough the importance of regulatory authorities in capital markets, I would caution against having unrealistic expectations about what they can accomplish. A sound regulatory infrastructure and enforcement are necessary, but not sufficient, conditions for bringing about transparent, fair and efficient capital markets and good corporate governance. We need the cooperation of all market participants: listed companies, securities firms, investment banks, accounting and law firms and, above all, investors. These stakeholders should be provided the incentives to protect their own reputations and interests. They should understand that following the law and having good corporate governance makes good business sense. It enhances shareholder value and strengthens competitive positions.

Unfortunately, too often we observe so-called regulatory capture: where market participants collude and violate laws, and regulators hesitate to take action against them for fear of causing a stock market collapse or corporate bankruptcies. There is a moral hazard here. This can be seen in China where securities firms and investment banks are all state-owned. They take excessive risks and disregard their reputations. There is a total lack of compliance culture in many of these firms. The solution, of course, is to introduce private and international firms into the industry, and ensure they are fully accountable and have good incentives for compliance.

Finally, I would highlight the critical role of investors in monitoring investment companies and intermediaries. A regulatory agency is an indispensable watchdog for protecting investors. But it would be far more effective if investors were empowered and mobilised to protect themselves, perhaps through associations, clubs and class-action suits. Regulatory authorities ought to be encouraging and facilitating shareholder activism across Asia.

Stringent regulatory standards, enforcement and self-compliance by companies, and investor activism will together promote the development of well-functioning, transparent and efficient capital markets, and spread good governance practices throughout the Asia-Pacific region.

Panelist:

LEE SUET-FERN
Partner/Co-Head, Shearman & Sterling Stamford, Singapore

Lee Suet-Fern spoke about the shift towards disclosure-based regulation in Singapore, the rise of "shareowner" activism, and certain contradictions that she sees in investment practice in Asia.

Asian economies are now in recession. It's time to properly deal with structural issues. Corporate governance is one of them. It is increasingly recognised as a major driver of a nation's economic competitiveness. There is renewed recognition in Asia that to attract investors from around the world the norms of corporate governance need to be observed. These norms give comfort and transparency to those not totally familiar with the local business milieu and are closely interlinked with a war to strengthen the financial sector. Who is at the front line? Two groups: market regulators and investors themselves, sometimes fighting alongside, often perhaps not adequately aware of their strong inter-relationship and partnership to achieve a shared vision. Both have, in the last few years, enhanced and expanded their roles.

New regulatory trends

Let me first deal with market regulators. In Singapore, key first steps were taken during the last financial crisis with the formation of a Corporate Finance Committee in 1997. Some of its recommendations were translated into law at the beginning of 2001. One of the key shifts was the movement to a disclosure-based philosophy of regulation and the introduction of a reasonable-investor test to determine disclosure requirements of all public offering documents in Singapore. This was by far the most important reform introduced and a major departure from the previous prescriptive-disclosure regime. It is very much the approach that we have seen here in Hong Kong and I won't venture to comment who's copying whom!

Since then three further committees have been formed in Singapore. We always do things by committee! The Corporate Governance Committee, the Disclosure and Accounting Standards Committee, and the Company Legislation and Regulatory Framework Committee. Interestingly, in Hong Kong the Standing Committee on Company Law Reform has also set up three sub-committees.

The Corporate Governance Committee has issued a Code of Corporate Governance drawing from experiences in the United States, the United Kingdom and Australia. The code sets the model and benchmark for corporate governance best practices that Singapore companies should strive for. Our stock exchange has endorsed the code and now requires listed companies to disclose and explain in their annual reports any deviations from the code. We very much have a patchwork of regulations, some of which is self-regulation, and there is a shift towards the US model.

The Disclosure and Accounting Standards Committee has recommended that primary legislation should contain a general obligation for listed companies to make such continuous disclosures as are necessary to enable investors to arrive at informed decisions. The committee has also recommended that compliance with prescribed accounting standards should be legislated. The success, however, of a disclosure-based regime depends not only on legislation, but on the willingness of local regulators to enforce it.

We heard this morning that Asian regulators "over-regulate and under-enforce". I was interested to note when I flew up yesterday that the South China Morning Post carried a slightly damning criticism of uneven-handedness. The suggestion was that the Hong Kong SFC pursues small fry whilst ignoring the big fish. Now in Singapore we can't have that sort of criticism, so the Singapore Exchange definitely has gone for big ships — they recently suspended the stock of Neptune Orient Lines. Its chief executive, Fleming Jacobs, was very upset, the reason being that apparently information relating to Neptune Orient Lines' business outlook was given to the press and deemed as not having been made generally available. The Exchange took a very serious view on corporate disclosure grounds and was applying rigorous standards similar to the US SEC's "fair disclosure" rules, which require that if there is disclosure of material non-public information then it must be given to the public, and if there is unintentional disclosure then that disclosure must be made promptly.

There is also other evidence that the Singapore regulator is inclined to take prosecution increasingly seriously. A few weeks ago, the chief executive of Freight Link was prosecuted under the Companies Act because he authorised the use of what we might consider a commonly used statement: "Barring any severe dislocations of regional economies [this was at the beginning of the year, pre-September 11] directors are of the view that prospects of the Group's operations should remain satisfactory." Soon after the company recorded a loss of S$27 million (about US$15 million). He was fined S$10,000, although he was not detained at the President's pleasure! Notwithstanding our reputation for being quite a draconian state, I am pleased to tell you that we have not yet mandated caning for corporate governance offences!

Shareowners arise

As a lawyer whose work involves crafting words, I like the distinction you made at lunch, Bob, between a "shareholder" and a "shareowner". Certainly, shareowner activism has really been ascendant. Investor associations have been created in Asia and shareholders have been increasingly prepared to attend meetings, be more vocal, and organise the minority vote, notwithstanding issues of concentrated ownership in many companies in Asia. We can see that Asians are far from being timid or disinterested. In Singapore, there is the Securities Investors Association and in Malaysia there is the Securities Industry Development Centre. Both have been very active. Although wider shareholder activism is unlikely to lead to the instigation of class-action suits in Singapore — mainly due to the nature of our legislation and the heritage we have from the UK — Singapore investors seem to have utilised their votes in many ways, and without any particular encouragement from the government or the regulator. At general meetings they have been seen to nominate directors and influence management. So you see we can think on our own sometimes!

Recently, at Fraser & Neave's EGM, there was a special resolution to provide retirement payments for directors, but minority shareholders voted successfully against it. Another recent instance was at Pacific Holdings in Singapore, where again the minorities were able, by just getting themselves more organised, to call for a meeting under the Companies Act and remove three incumbent directors. These investors are very much coming together and not voting with their feet, but acting as shareowners and registering their views.

Contradictions

In order to save time for discussion, I am going to close with just a few remarks on two completely different companies or sets of companies. One is Asia Pulp & Paper (APP) and the other is Singapore's government-linked companies. We have been told today that to access global capital markets there is a need to play by global standards. Curiously enough though, the situation at APP, with its opaque corporate structure and very weak governance, is probably a textbook illustration of what not to do. Yet international investors, seduced by the fact that there was a NASDAQ listing and maybe that major investment banks, including Goldman Sachs, had underwritten the offerings of its securities, did not pay attention to APP's inadequate corporate governance. Many of these investors are not flippers, they were long-term players. Yet none of them appeared to have paid any attention and they managed collectively to pour some US$13 billion into this company. Interesting too is the role of the investment banks in sponsoring its fundraising issues, even until very recently when it was quite evident that the company was in trouble. Maybe what Nawaaporn says is true, that everybody was too greedy.

Let me touch on the other point. Gary Coull this morning talked about the abuses in family companies that arise because of the ambiguity between what is privately held and what is publicly held, and how the shareholders behave vis-à-vis what is publicly held and privately held.

In Singapore there are many large companies. Many of them display excellent corporate governance and I have been privileged to witness that many of them really do comply with what I would regard as close to global standards. Most of these companies are government-owned. Many are also publicly listed, and when they are publicly listed they do have different constituencies of minority shareholders.

Now Laura mentioned earlier that when you have government-owned companies, sometimes you have a situation where the state shareholders have interests that may not necessarily be aligned with those of the company, so that adds another layer of complication. Right now I need to choose my words very carefully. It must therefore in Singapore be particularly challenging for the government and its investment holding company, Temasek, to manage their stable of companies for the perceived good of Singapore as a whole, without compromising commercial good sense for each company and good corporate governance in each of their companies. One does wonder how much the sense of undue government shareholder involvement has influenced the overseas expansion plans of Singapore's excellent corporates. Banner deals that come to mind are Singapore Telecom's unsuccessful bid here for Hong Kong Telecom and its successful bid for Optus in Australia, and Singapore Airline's bid for Ansett. Now ladies and gentlemen, as I do need to go home to Singapore tomorrow I am going to end my comments here.

Panel discussion and Q&A:
Barry Metzger, Laura Cha, Frederick Hu, Lee Suet-Fern

Topics covered in the discussion included (in chronological order):

- How important are codes of best practice?
- Legal barriers to shareholder action in China.
- Should investment banks take the lead in forming a "council of institutional investors" in Asia?
- Corporate groups

Codes of best practice

Barry Metzger opened the discussion by noting that codes of best practice had played a role in promoting corporate governance reform in Asia, despite being non-binding in many cases (though with some mandatory elements). How important were these codes? And what impact would they have in places like China and Singapore? Laura?

Laura Cha: In China's case, we haven't completely issued a code yet. What we call the "Code of Core Principles and Minimum Standards" was issued for consultation earlier this year. We have had two seminars on the subject, so I would say we have widely consulted the markets. It will probably be published towards the end of 2001. We know what we want to do and we are keeping to core principles and minimum best practices. As to how much people will comply, that remains to be seen.

Listed companies will have to include in their annual reports an explanation of any deviation from good corporate governance practice, why they are not following it and how they will address those issues. Although many best practices are not mandatory, we are hoping that by requiring disclosure it will at least bring these things to the attention of investors. An aspect not yet in the code, but could be introduced later if people are not following it, is to make some of the provisions mandatory.

In the annual report we will also require listed companies to indicate the number of times they have been reprimanded by the regulator over the past year. We are considering this because, in many cases, we do not have proper sanctions under current Chinese law. What we can do at the moment is issue a public censure or reprimand, but if you do it a lot then people get numb and get used to it. But if we require companies to put this in their annual report, then again it will bring it to the attention of investors. So there are various things we can do with disclosure to give listed companies an incentive to follow the code.

Lee Suet-Fern: As I mentioned, Singapore has introduced a code, it has been adopted by the Exchange, and companies are required to indicate deviations from the code in their annual report. I think this has been very good. It has clarified issues and raised the bar. Boards can look at the specifics of the code and see where they are non-compliant; and I think they do move to it. So the code has been extremely helpful in raising awareness of good corporate practice.

Legal barriers in China

Question: Mrs Cha, I know that corporate governance is a big issue for the CSRC and you have been encouraging minority shareowners to take companies to court. But recently when minority shareholders tried to take Guangxia to court, although a local court agreed to take the case, China's highest court ruled that they couldn't. You said in an interview that this was frustrating and that even if the court found the company guilty, yet another agency, the Public Security Bureau, would have to enforce that decision. When do you see these contradictions or barriers being overcome? And, my second question, how big of a setback to your drive to improve corporate governance is the recent suspension of the sale of state-owned shares?

Laura Cha: With regard to your first question, it is very disappointing to us that the court refused jurisdiction on the case, which we believed could be properly resolved in the judicial system. The law will have to be amended in China, there is no question about it. We will continue to encourage shareholders to bring pressure on the system so that the law will be amended and the courts hopefully will be more enlightened in that regard. We share the frustration of the shareholders, but from the CSRC's point of view there is not a whole lot that we can do to help them.

With regard to your second question, first of all, even though the announcement was made by the CSRC, one has to remember that the policy to sell or not to sell, or the price at which the state shares will be sold, is a matter not for the CSRC. The CSRC is an implementing organisation. The owner of the state shares is the Ministry of Finance, so that obviously there are considerations behind the suspension. But I don't believe that the suspension itself will dent our efforts or slow down our work in promoting corporate governance.

Frederick Hu: If you look around the region, many of the legislative changes in terms of corporate governance in recent years have not had the best reception in the courts. Shareholders have attempted to exercise their rights, but they've had difficulty in translating those rights into effective court actions. This is a reflection of the weakness of the judicial system in some countries, and the fact that the judiciary and the legal establishment really needs to be educated. Even in countries with far longer traditions of court systems and of resolving commercial disputes within the courts, this has been a problem. It's been a problem in Korea, Japan, and a number of other places.

Investment banks and leadership

Question: I have a question for Fred Hu. I would like to invite him to address some of the comments made by Lee Suet-Fern about the role, or apparent lack of a role, of financial institutions in promoting corporate governance. This morning Gary Coull noted the loss of business after CLSA published its report on corporate governance. And a suggestion was made for a Council of Institutional Investors in Asia that would possibly require someone like Goldman Sachs to take the lead in setting it up (and putting aside its sense of competition with other financial institutions). Goldmans would drive the common good here. Would you make some comments on that?

Frederick Hu: I would acknowledge that a full-service investment bank like Goldman Sachs may not always be the best equipped to address specific corporate governance issues concerning investors, because these firms have a large corporate advisory group whose primary objective is to look after issuers. For this job we retain law firms and accounting firms to make sure that the paperwork is consistent with the regulatory requirements and investors are satisfied with the level of disclosure and the quality of information about issuing companies.

In developed markets like the US and the UK, the hope is that adequate legal protections are in place and investors are sophisticated enough to read prospectuses, talk to management, make their own judgement, and so on. The ultimate responsibility, of course, is with investors. They have a direct stake, whereas investment banks only serve an intermediate function.

Nonetheless I do think it is important for investment banks to play a more proactive role going forward, and to work with investors to enhance the practice of corporate governance. There is certainly scope for financial institutions to join force to work towards better corporate governance, which, after all, is vital for the healthy development of capital markets.

Goldman Sachs's own experience shows investment banks can play a positive catalyst role in fostering better corporate governance. For example, during the privatisation and stock market listing of PetroChina, there were lots of thoughts about how to transform a stodgy state-owned enterprise into a shareholder friendly new company. The challenge was monumental. Prior to the restructuring, this company or almost every other Chinese company for that matter, never thought about corporate governance issues. Everything was so new, so alien to them. Goldman Sachs worked closely with government regulators and the company to make sure PetroChina could successfully adopt international accounting standards, establish a board with well-respected independent directors, and introduce an executive compensation scheme that ties management pay closely with company financial performance, etc. These initial efforts by PetroChina, with assistance from Goldman Sachs, have laid some of the critical foundations for sounder corporate governance going forward.

Corporate groups

Question: I hear the Chinese government is promoting corporate groups, and earlier on today we heard Harvey Chang and also Gary Coull talking about corporate groups in Asia. In their experience, such groups can be harmful to corporate governance. I want to hear your view on the formation of corporate groups in China and whether it will be harmful to corporate governance?

You also talked about parent companies seeing their listed subsidiaries as ATM machines, and that when a subsidiary is in trouble they sometimes inject assets to help them. As an investor, we often find these controlling parent companies as black boxes. We know that in China there are accounting standards for related-party transactions, but often we don't have enough disclosure to understand these transactions. Should listed companies disclose more about their parent companies which are not listed, so that investors will know more about these transactions?

Laura Cha: Well, it's hard to draw the line. How far you want to go upstream is always a problem. Let's look at Hong Kong as an example. Most Hong Kong listed companies are a vehicle for a corporate group and in-between the parent company and the listed company there is a middle layer.

As to whether disclosure should be made on the parent company, how far upstream do you go? If you extend it one layer, people are always going to go to the next layer. To the extent possible, we have required disclosure on connected transactions, especially where there is conflict of interest, but to have full disclosure on the parent company, which is not a listed company, I think that that might be going a little too far.

Barry Metzger: I think that generally corporate government reforms in the region and internationally have been focused on individual listed companies rather than on groups, though the presentation of consolidated accounts and the handling of related-party transactions have sought to address group issues. The reforms to date dealing with relationships within corporate groups have been inadequate.

11 Conclusion

PETER SULLIVAN
Chairman & CEO, Lombard Investments, Inc., San Francisco

We've heard many wonderful presentations and interchanges today between experts representing Asian and multinational corporations, institutional investors, financial and professional intermediaries, market regulators, and from our audience of educators, journalists and others. Their thoughts have been provocative, stimulating, enlightening.

If you allow me, I will try to do two things. First, give a quick summary of my own views on corporate governance. And then try to paint a broad overview of what we've heard today. Obviously that painting will be very impressionistic, if not abstract.

Let me start at the outset by saying I have worn two hats. One in the public sector for 25 years at the Asian Development Bank (ADB), and more recently in the private sector at Lombard, so I've had a chance to look at corporate governance from two very different perspectives. Bob Carlson mentioned at lunch that the ADB had adopted a set of principles on good governance. We were very proud of those at ADB because we had to get that passed by 57 different member countries of the bank, and the politics in getting 57 countries to agree on good governance was challenging.

But we did come up with the four themes that Bob mentioned at lunch: accountability, predictability, participation and transparency. And I think they apply very well to corporate governance. Accountability, meaning the accountability of management to a board and board to shareholders. Predictability, which means rules and regulations and codes of best practice, under which you can predict what should be done by the management and boards. Participation, which is the role of the shareholders, the shareowners and the corporation. And transparency, which I think speaks for itself.

In my new role at Lombard Investments, which is a private equity firm focusing on investments in Asia, I've moved perhaps from theory to practice. I've seen the results of both good and bad corporate practice, and how it impacts on the bottom-line — and believe me, it does.

Lombard has participated in private equity investments from Korea to Taiwan, and from Hong Kong to the Philippines and Thailand. Our major partner in these activities has been the California Public Employees' Retirement System (CalPERS) and we know how much they stress good corporate governance.

In our investments we have observed a wide diversity in the standards of corporate governance in Asia and, unfortunately, diversity is not always a good thing. We learned quickly through investment in one company, where it turned out, despite due diligence, that the board did not have sufficient independence, where cost accounting and auditing standards were not up to international standards, and where we had to play an extremely active role, although we were only a minority shareholder, to protect our interests. We had to build a coalition among other shareholders to replace management and part of the board in order to try to develop good corporate governance.

A much happier example was one made shortly after the Asian currency crisis in Korea's fifth largest securities firm. We helped there to change the shape of the board and, working with new management, we helped to implement international best practice. You heard the results of that this morning from KK Doh, because that was Good Morning Securities.

And does good corporate governance pay off? Well, we sold a minor portion of our investment earlier this year for a 352% gain.

At Lombard we believe so strongly in good corporate governance as a critical element for enhancing shareholder value that we have a lengthy checklist on corporate governance, which we use as the basis for evaluating every possible investment we make. We talk through the concept of corporate governance with each potential investee company and we incorporate into the contract agreement any improvements that will be necessary.

I would like to summarise the main ideas of today's conference under five categories.

- What is corporate governance?
- What are its essential elements?
- What are the obstacles to good corporate governance?
- What is its real value?
- And what are the next steps for us?

What is corporate governance?

Nawaaporn noted that good governance could apply at all levels: international, national, political, and economic. But if we focus on corporate governance, we know that it's not really a new concept, as Andrew told us this morning: it's an issue that has existed since public limited companies were first developed in the 19th century, separating owners of firms from their managers. But the emphasis is new, as evidence mounts to show how important it is in enhancing shareholder and stakeholder value.

We've heard different definitions today. I like Dr Teh's definition and I like CalPER's definition, which are similar and stress the relationship among participants in determining the direction and performance of corporations. And here the key players are the shareowners, management and the board.

We heard other definitions as well today, broader definitions involving relationships among stakeholders, employees, customers, clients and society at large. Douglas, Andrew and Christine in the audience touched on these themes.

In any case, I think we can say that corporate governance involves the process of managing a corporation to ensure the ongoing vitality of the business and the long-term value for shareholders.

Essential elements

What are the essential elements of corporate good governance? Among other things, the accountability that I mentioned in ADB's definition. Accountability of managers to boards and boards to shareholders. Some of the common themes we heard during the course of the day were the independence of boards — Andrew Sheng gave examples of that. Transparency and disclosure — Harvey Chang and his description of TSMC's quarterly reports, or KK Doh's meetings with his employees are good examples.

We've heard about accounting and auditing standards, about the avoidance of conflicts of interest from Laura, and about equitable treatment of all shareholders, minority and foreign. And again Harvey told us about how in TSMC, one of its major shareholders, Philips, did not get preference in allocation.

We heard about social, community, and environmental enhancement issues.

Laura talked to us about the more complex issues in China, in the "three separations" that she addressed.

How are these ideas of good corporate governance regulated or enforced? We talked about laws and regulations (one of Barry's "four mosaics"), about stock exchange regulations, about codes of best practice, self-regulation and voluntary practice, compliance reporting, and fair voting methods. We didn't touch much on long-term strategic vision, but I think that is certainly an element that's necessary for good corporate governance.

Obstacles

Several speakers addressed obstacles to corporate governance. Legal and regulatory weaknesses were discussed. Barry Metzger talked about the convergence in legal and regulatory policies, at least a convergence on where we want to be going. Frederick Hu suggested there's a growing global consensus on this, and a consensus between China and Hong Kong.

Laura Cha discussed the difficult issue of how much regulators should prescribe and the risks of over-prescription.

We talked about the fact that there may be sufficient legal and regulatory instruments, but still enforcement problems. Andrew Sheng alluded to this, and Fred talked about the gap between law and practice in this region. Lee Suet-Fern also talked about the uneven-handedness of enforcement and the efforts that Singapore was making to avoid this and to take prosecution seriously.

We discussed another potential obstacle and its consequences: family ownership. The issue of the lack of independent directors and the problems of finding sufficient independent directors. We talked about the need for training directors and about auditing, accounting, reporting. The need to understand the duties and liabilities of directors, Ian Faragher touched upon that.

Real value

Is the struggle for corporate governance worth it? I've mentioned Lombard's experience. Ian gave us a dramatic example of what happens when good governance is not exercised. Bob Carlson mentioned that a mere expenditure of US$500,000 to supervise a portfolio of 62 investments earned a return of something like $150 million a year. That certainly is a very good bottom-line.

Bob also mentioned a study by McKinsey, which looked at six countries in Asia and showed that institutional investors were prepared to pay between 20% and 27% premium for good governance. In short, we learned that good corporate governance lowers the cost of capital.

Gary and KK reminded us of another benefit-that you could attract good talent with good corporate governance. Harvey Chang also touched on that. KK's description of 7,500 applicants for 15 jobs at Good Morning Securities was a stunning concept! "Corporate governance maximises shareholder value", from the words of Victor Fung.

Or, more simply, corporate governance matters.

Next steps

Well, to conclude. How do we get there? I think each of us has to start by looking at our own practices, to see what can be improved and how we can act as models for others. Nawaaporn said this clearly, namely that we had to practice what we preach. Or, in Bob Carlson's words, "We have to walk the walk". This applies, as Laura told us, to intermediaries as well as to the firms in which we invest.

Second, we need to work with legislators, regulators and stock exchanges to improve the rules and procedures.

Third, as Fred told us, shareowners have to insist on their rights and take the appropriate action vis-à-vis boards and management.

Fourth, I think we need to support other methods and other tools for market discipline. The work of CLSA is extremely impressive and very bold. Rating agencies are doing that too. Others of us have to show and follow objective ratings of corporate governance.

Finally, we need to work within our own communities to develop codes of best practice, stressing transparency, accounting and auditing standards, equitable treatment of shareholders, independent boards and board committees, and dialogue on best practice.

Many speakers — Douglas, Andrew, Gary — talked about the need for voluntary, or the benefits of voluntary, compliance.

Finally, I might add, as a plug for the Asian Corporate Governance Association (ACGA), that we need to support organisations like ACGA, which do this kind of good work.

12 About ACGA

The Asian Corporate Governance Association (ACGA) is a private, non-profit organisation incorporated under the laws of Hong Kong. It is dedicated to facilitating corporate and economic development in this region through improved corporate governance. Our principal objectives are:

- To be a leading provider of independent information and analysis on corporate governance developments across Asia.
- To promote constructive, practical and ongoing dialogue on corporate governance among and between key groups such as institutional investors, companies, financial and professional intermediaries, and market regulators.
- To advise and assist Asian companies on the implementation of good corporate governance practices.

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. We are pleased to welcome the following companies as new corporate sponsors: Chubb Insurance, CLSA Emerging Markets, and Sun Life Financial.

Activities 1999-2001

INFORMATION & ANALYSIS

- Published a report on corporate governance reform in 11 major Asian economies — "Building Stronger Boards and Companies in Asia". We have distributed more than 4,000 copies of this report worldwide.

- Tracked governance developments in these same economies, undertook original research, and contributed articles to both specialist legal, financial and shareholder journals and the mainstream media.

- Made presentations, based largely on original research, at more than 30 conferences, seminars, workshops and business meetings around Asia, the United States, and Australia.

GOVERNANCE DIALOGUES

- Organised the "Asian Business Dialogue on Corporate Governance 2001", held in Hong Kong in November 2001. This conference, an informal dialogue focussing on practical issues, brought together speakers from key groups involved in the implementation of corporate governance in Asia — institutional investors, corporations, financial and professional intermediaries, and regulators.

- Organised a seminar for Korean companies in Seoul in May 2000 — "Corporate Governance in Asia after the Crisis".

- Worked closely with national and international organisations on education-related events and conferences, including the OECD, Harvard Business School, Hong Kong Society of Accountants, Hong Kong Institute of Company Secretaries, and the Institute of Internal Auditors of Thailand.

- Participated in a workshop on Indonesia's new corporate governance code (at the invitation of the Jakarta Stock Exchange and World Bank).

TRAINING AND ADVISORY

- Conducted a customised training course for the legal and compliance department of a major investment bank in the region.

- Responded to several hundred requests for information on different aspects of corporate governance in Asia, or on corporate governance principles and codes from around the world.

- Appointed to a new advisory committee, the SFC Shareholders Group, formed to advise the Hong Kong Securities and Futures Commission on shareholder rights and investor protection issues.

- Participated in the judging of corporate governance awards schemes in Hong Kong and Thailand.

Contact person and details

For membership details and other information, contact:

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Asian Corporate Governance Association Ltd
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Speaker Biographies
Asian Business Dialogue on Corporate Governance 2001
November 1, 2001, Hong Kong

MR. ROBERT F. CARLSON
Vice President and Senior Board Member, Board of Administration
California Public Employees' Retirement System (CalPERS)

Robert F. Carlson has been an elected member of the Board since 1971 and served as Board President from 1976 to 1985. Mr. Carlson was elected by and from retired members. Prior to his retirement, he was elected by and from state active members. Mr. Carlson is the Chair of the Finance Committee and Vice Chair of the Performance and Compensation Committee. He also serves on the Benefits and Program Administration and the Investment committees. In addition, he serves on the ad hoc committees for Investment Policies, Procedures and Guidelines, and the R Street Project (subcommittees of the Investment Committee).

Mr. Carlson also serves as a member of the Boards of Directors/Trustee of nine investment companies in the Franklin-Templeton Group of Mutual Funds. He has also served as Adjunct Professor of Law at the University of the Pacific, McGeorge School of Law, from 1975 to 1989.

Mr. Carlson has been a member of the California State Bar Association since 1952 and was admitted to practice before all California state and federal courts in 1952. He was admitted to practice before the United States Supreme Court in 1966. He retired as Chief Counsel with the California Department of Transportation in 1985.

Mr. Carlson received his Bachelor of Arts from St. Mary's College and his Bachelor of Laws and Letter, Juris Doctor, from University of California, Hastings College of Law. He was named Hastings Law School Alumnus of the Year in 1997.

He resides in Carmichael with his wife Barbara.

MRS. LAURA M. CHA
Vice Chairman
China Securities Regulatory Commission

Mrs. Laura Cha is a Vice-Chairman of the China Securities Regulatory Commission (CSRC). She was appointed to the post by the State Council in January 2001 and became the first person outside the Mainland to join the Chinese Government at vice-ministerial rank. Premier Zhu Rongji indicated at a press conference in March 2001 that the appointment of Mrs. Cha was just a beginning and the Government was prepared to recruit professionals from overseas, particularly in the financial and securities fields. This was seen as an encouraging sign for overseas Chinese professionals and demonstrated the Government's commitment to economic reform.

Mrs. Cha was educated in the US, with a BA degree from the University of Wisconsin and a law degree from the University of Santa Clara. She practiced as an attorney in San Francisco and in Hong Kong and advised many multinational corporations in their investment in China in the 1980s. She joined the Securities and Futures Commission (SFC) of Hong Kong in 1991 as an Assistant Director of Corporate Finance. She became Executive Director in 1994 and headed the Corporate Finance Division for five years before being appointed as Deputy Chairman in 1998. In her 10 years with the SFC, Mrs. Cha participated in several major reforms of the Hong Kong securities market. She was a key player in establishing the regulatory framework for the listing of Chinese state-owned enterprises in Hong Kong in 1993 as well as the demutualization and merger of the stock and futures exchanges of Hong Kong in 1999.

At the CSRC Mrs. Cha is in charge of the Public Offerings Department and Listed Companies Department as well as the Training Center.

MR. HARVEY H.W. CHANG
Senior Vice President & Chief Financial Officer
Taiwan Semiconductor Manufacturing Company

Founded in 1987, TSMC is the world's largest pure integrated circuit foundry with annual turnover exceeding US$5 billion. The company is based in Taiwan's "Silicon Valley", the Hsin-Chu Science-Based Industrial Park, and is dedicated to providing manufacturing services for advanced ICs. Among all Taiwan Stock Exchange listed companies, TSMC enjoys the highest market capitalization and is the first Taiwanese company traded on the New York Stock Exchange.

Career Steps

January 1998 - Present: Senior Vice President & CFO, Taiwan Semiconductor Manufacturing Company Ltd.
June 1997 - May 1998: Vice Chairman, KG Telecommunications Co., Ltd.
October 1993 - December 1997: Chairman, China Securities Investment Trust Corp.
August 1992 - September 1993: President, China Development Corporation
February 1989 - July 1992: President, Grand Cathay Securities Corporation
November 1984 - January 1989: Senior Vice President & General Manager Trust Department, Chiao Tung Bank

Honors and Accomplishments

- Recipient of 2002 Eisenhower Exchange Fellowship Award
- Recipient of Achievement in Best Practices Award 2001 by CFO Asia Magazine
- Winner of Best Investors Relations Officer Asia 2001 Award
- Recognized as one of Asia's Best CFOs 2001 by Finance Asia
- Recipient of 1998 Distinguished Alumni Service Award from Wharton School

Social Services

- Chairman, Felix S.Y. Chang Foundation
- Chairman, Taipei Ching Yin Cultural & Educational Foundation
- Member, Asian Executive Board, Wharton School

Education

M.B.A. Wharton School, University of Pennsylvania, 1977

B.S. National Taiwan University, 1973

MR. GARY COULL
Executive Chairman
CLSA Emerging Markets

Gary Coull is Executive Chairman of CLSA Ltd., a widely recognised leader in brokerage, investment banking and direct investment services in the emerging markets of Asia, Latin America, Emerging Europe, the Middle East and Africa.

Mr. Coull was born and raised in Vancouver, Canada and graduated in 1976 from the University of British Columbia with a Bachelor's degree in Arts. He came to Hong Kong by chance in 1977 and became captivated with the region after his first visit to China the following year. Having adopted Hong Kong as his home, Mr. Coull spent his first six years working as a business journalist for the South China Morning Post before joining the Far Eastern Economic Review.

In 1983, Mr. Coull left journalism and started a China investment and trading company, which he ran until he joined Hong Kong brokerage Winfull Laing & Cruickshank in 1987. French bank Credit Lyonnais subsequently bought Winfull Laing & Cruikshank, which subsequently led to the creation of CLSA.

Headquartered in Hong Kong, CLSA is 35% management owned and operated with over 1,000 staff and a presence in 29 markets. In 1999, CLSA established CLSA/e, a global electronic broking arm that provides tailored execution services to both institutional and retail clients around the world. CLSA/e is comprised of three entities including G-Trade, a wholesale execution services joint venture with Bloomberg Tradebook; G-Port, a global agency broker; and Equity Access, a cross border retail trading services provider.

Mr. Coull is also Executive Chairman of a direct investment joint venture, CLSA's Private Equity Group, whose investors include General Electric, Verizon Communications and Allianz; a director of Sa Sa International Holdings Limited; a director of New World Infrastructure and a Governor of the Canadian Chamber of Commerce.

Mr. Coull is an avid golfer and a keen racehorse owner.

MR. KIKWON DOH
President & CEO
Good Moning Securities, Korea

Mr. Kikwon Doh is the President & CEO of Good Morning Securities.

Prior to taking his current position, Mr. Doh was Business Manager, Global Consumer Banking Group, Citibank, N.A., Thailand. His functional responsibilities included marketing, sales, distribution, operations and product areas.

Mr. Doh started his career as a Management Associate for Citibank, Korea. He was the Branch Manager in charge of the Main Branch/Itaewon Branch, Sales Director, Marketing, Consumer Banking Director, and President & CEO, Citicorp Finance & Securities (Thailand) Ltd.

His education consists of an MBA from Duke University, NC, USA in 1985 and a BA in Sociology from Yonsei University, Seoul, Korea.

MR. IAN FARAGHER*
Chief Executive Officer, Hong Kong
Chubb Group of Insurance Companies

Ian Faragher, BE, is Chief Executive, Hong Kong, of the Chubb Group of Companies. He has held this position since 1998.

Mr. Faragher's primary goal in Hong Kong is to achieve profitability through controlled growth and sound expense management in what is a highly competitive insurance market.

By switching resources and focus away from commodity classes of business towards specialty business, Mr. Faragher has succeeded in tapping profitable lines of growth. He has also been able to reduce expenses by flattening the organisational structure and hands on support and involvement in the underwriting process.

Mr. Faragher was involved in the acquisition in Hong Kong of a large underwriting agency that has provided for both expanded distribution and an expanded customer base in service industries.

As Country Manager for Chubb in Taiwan from 1994 to 1998, Mr. Faragher made the Taiwan operations profitable in one of Asia's most regulated insurance markets.

In Taiwan, Mr. Faragher was responsible for the strengthening of relations with brokers, launching direct marketing initiatives and working with government regulators on specific legislation to improve the insurance industry environment.

Working with government regulators, Mr. Faragher succeeded in obtaining government approval for offshore placements and comprehensive all-risk, property and personal accident products not previously available in the market.

Mr. Faragher held two other key postings in the Chubb Group. From 1992 to 1993, he was President of Chubb Insurance Company (Thailand) Limited, and from 1989 to 1991, Country Manager, Chubb Singapore.

Prior to joining Chubb, Mr. Faragher was with the Kemper Group of Insurance Companies from 1977 to 1988.

* Now head of Chubb's Greater China operations and based in Shanghai

DR. VICTOR FUNG KWOK-KING
Chairman, Airport Authority of Hong Kong
Chairman, Li & Fung

Dr. Victor Fung is Chairman of the Airport Authority Hong Kong, a statutory corporation responsible for the operation of Hong Kong International Airport.

Dr. Fung is the Chairman of the Li & Fung Group, a leading Hong Kong-based regional trading company and Chairman of Prudential Asia, the Asian investment arm of Prudential Insurance Company of America. He is a Director of Pacific Century CyberWorks Company, Orient Overseas (International) Limited, Kerry Properties Limited and Sun Hung Kai Properties Ltd.

During the period from September 1991 to September 2000, Dr. Fung served as Chairman of the Hong Kong Trade Development Council, the statutory body responsible for the promotion of Hong Kong's external trade.

Dr. Fung is the Chairman of the Hong Kong/European Union Business Co-operation Committee, a high-level bilateral committee of business leaders from both regions. He is also a member of the Hong Kong Special Administrative Region Chief Executive's Commission on Strategic Development, the Judicial Officers Recommendation Commission and a Hong Kong Representative of the APEC Business Advisory Council (ABAC).

Born and raised in Hong Kong, Dr. Fung holds Bachelor and Master Degrees in Electrical Engineering from Massachusetts Institute of Technology, and a Doctorate in Business Economics from Harvard University.

Dr. Fung has received a number of honours. In 1995, he was voted Businessman of the Year under the Hong Kong Business Awards Scheme for his success as an entrepreneur and for his contribution to Hong Kong's economic development. Dr. Fung was made a Commander of the Order of the British Empire (CBE) in 1993 in recognition of his commitment to public service. In 1997, the University of Hong Kong conferred upon him an Honorary Doctorate Degree of Laws. In February 1999, Dr. Fung was awarded the 1998 Hong Kong Leader of the Year.

MR. DOUGLAS C. HENCK
Executive Vice President, Asian Operations
Sun Life Financial

Douglas Henck was appointed Executive Vice President, Asian Operations of Sun Life Financial on April 3, 2000. In this capacity, he has overall management responsibility for Sun Life's operations in Asia. 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-accumulation products.

Prior to joining Sun Life, 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. He was the lead negotiator for AIG's November 1999 purchase of 70% of Lippo Life, the number one life insurance company in Indonesia.

Prior to joining AIG, Mr. Henck was with the US-based Aetna Inc., which he first joined in 1974 after graduating with a B.S. Mathematics from Rensselaer Polytechnic Institute in New York. He qualified as a Fellow of the Society of Actuaries in 1978 and in 1981 moved to Aetna International where, in 1985, he became the then youngest employee at Aetna ever promoted to Vice President. Mr. Henck moved to Hong Kong in January 1987, establishing Aetna's Asia Regional office and remaining as the senior executive in the region for the next ten years.

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. While holding these positions, Mr. Henck led three delegations of American businessmen to Washington, D.C. to discuss trade and policy issues with members of the U.S. Congress and administration officials. He also hosted dozens of similar meetings in Asia, including individual meetings with, among others, the President of the United States, the U.S. Secretaries of State, Commerce and Treasury, the Prime Minister of Malaysia, the President and Premier of China, and countless meetings with Hong Kong Government officials including Governor Patten and Chief Executive Tung. 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 (including CNN and the ABC Evening News) as well as in print media (including the Asian Wall Street Journal, Washington Post, USA Today and all of the Hong Kong newspapers).

MR. FRED HU
Managing Director & Head, Greater China Economics and Strategy
Goldman Sachs (Asia), Hong Kong

Fred Hu is a Hong Kong-based managing director at Goldman Sachs Group. He studied at Tsinghua University in Beijing, where he received a Master's degree in Engineering Science. Later, he pursued advanced studies at Harvard University, where he obtained an M.A. and Ph.D. in Economics, and taught undergraduate and graduate courses in economics and statistics.

Mr. Hu was an associate at Harvard's Center for International Affairs, and served as a consultant to the World Bank. He worked for many years as a senior economist at the International Monetary Fund (IMF) in Washington D.C, where he was engaged in macroeconomic research and policy advisory work for a variety of member country governments, including China. Mr. Hu also served as head of research at the World Economic Forum in Geneva.

Mr. Hu sits on the boards of several institutions, including the Bank of China and China Huarong Asset Management Company, and is a member of the editorial boards of several leading Chinese academic journals. He is an advisor to the minister of Foreign Trade and Economic Cooperation (MOFTEC) and has advised the Chinese government on financial reform, pension reform, and international economic policies. He also serves as the co-director (non-resident) at the National Center for Economic Research (NCER) at Tsinghua University.

MRS. LEE SUET-FERN
Partner & Co-Head
Shearman & Sterling Stamford, Singapore

Mrs. Lee is the co-head of Shearman & Sterling Stamford, the Singapore joint law venture between Shearman & Sterling and Stamford LLC, a Singapore firm. She has had extensive work experience during the past two decades with a focus on equity and debt capital markets, mergers and acquisitions and corporate finance. She has been involved in many of Singapore's most significant corporate transactions and has been named as a leading practitioner in Singapore in Chambers Global Guide to the World's Leading Lawyers 2001 and Asia Law Leading Lawyers 2001.

Bar Admissions

- Barrister-at Law at Gray's Inn, London, 1981
- Advocate & Solicitor, Supreme Court of Singapore, 1982

Education

- Cambridge University, MA (Law), double first, 1980
- Senior Scholar, Girton College, Cambridge University
- Wright-Rogers Scholarship, Cambridge University
- Various University and College Prizes
- Post-Graduate Law Course, 1982
- AW Boon Haw & Aw Boon Par Memorial Prize for Best Student
- Justice Tan Ah Tah Prize for Professional Ethics

Mrs Lee is the author of numerous articles and papers covering topics such as mergers and acquisitions in Singapore, securitization, takeovers, recent developments in Singapore's financial services, cross-border listings, and a comparison between cooperative and equity joint ventures in China. She is actively involved in various professional bodies, including the Inter-Pacific Bar Association (as chairman of the financial institutions and transactions committee) and the International Bar Association (as vice-chairman of its banking committee). Mrs Lee also sits on the boards of several companies, including Sembcorp Logistics Ltd, FHTK Holdings Ltd, Chemical Industries (Far East) Ltd and ECS Holdings Ltd, and is a member of the audit committees of Sembcorp Logistics and ECS Holdings.

MR. BARRY METZGER
Senior Partner
Coudert Brothers International Attorneys, New York

Barry Metzger has recently returned to the international law practice of Coudert Brothers after serving as General Counsel of the Asian Development Bank.

Mr. Metzger studied at the Woodrow Wilson School of Public and International Affairs at Princeton University (A.B., magna cum laude, 1966) and at the Harvard Law School (J.D., cum laude, 1969) where he served as President of the Harvard Legal Aid Bureau and was a recipient of the Sheldon Memorial Fellowship.

As an Overseas Service Fellow of the Ford Foundation-funded International Legal Center, Mr. Metzger served as Assistant to the Principal of the Ceylon Law College in Colombo, Ceylon (Sri Lanka) from 1969-71 and then became Director of Asian Programs at the International Legal Center's head office in New York.

Mr. Metzger joined the international law firm of Coudert Brothers in New York in 1974 and became one of the founding members of the firm's Asian practices. He served as an associate in the firm's New York Office as part of its East Asian Group in 1974-76, served as an associate, partner and then managing partner of the firm's Hong Kong practice during 1976-84, established an office for the firm in Sydney, Australia and served as managing partner from 1984-89, and moved to London to become managing partner of the firm's London practice during 1989-95 until accepting the position as General Counsel of the Asian Development Bank in January 1995.

In his private practice, most of Mr. Metzger's professional work has focused on cross-border financial transactions and acquisitions in the emerging markets and, in particular, in the Asia-Pacific region.

At the Asian Development Bank, Mr. Metzger served as the principal legal advisor to the Board of Directors and Management, supervising a multinational team of 26 lawyers. As such, he was intimately involved in the Bank's emergency financial assistance to Thailand, Korea and Indonesia during the Asian financial crisis. He also led a significant expansion of the Bank's legal technical assistance activities which assist its developing member countries in effecting legal, regulatory and judicial reforms and in strengthening the professional capabilities of their legal, regulatory and judicial institutions.

Mr. Metzger has written extensively on the need for legal, regulatory and judicial reforms in emerging markets, including "Redefining Asia's Legal Framework" (14 International Financial Law Review 12-14, October 1995), "Infrastructure Finance in Asia" (Banking Law and Practice, 1996), "The Asian Financial Crisis, Corruption and Legal Reform" (presentation to the Association of the Bar of the City of New York, November 1998), "The Role of Law and Legal Institutions" in The Asia Competitiveness Report 1999 (World Economic Forum, Davos, 1999), "An Asian Perspective on Legal Modernization" in Making Development Work: Legislative Reform for Institutional Transformation and Good Governance, (Kluwer, 1999), "Fixing Asia's Multinationals" an op-ed piece in the January 15, 2001 edition of the Asian Wall Street Journal, "The Asian Financial Crisis, Corruption and Legal Reform" in Liber Amicorum Dr. Ibrahim F.H. Shihata (Kluwer, 2001) and "Korean Corporate Governance at the Millennium: The Challenge of International Competitiveness" in Journal of Corporation Law (Spring 2001).

Mr. Metzger headed an international team advising the Ministry of Justice of the Republic of Korea on corporate governance reforms during 1999 and 2000 and is currently the senior member of an international consortium assisting the Federal Commission for the Securities Market of the Russian Federation in the preparation of a Corporate Governance Code.

MS. NAWAAPORN RYANSKUL
Former and first Secretary General
Thai Government Pension Fund

Date of Birth : 1944
Nationality : Thai
Education : 1967 B.A. Goucher College, Maryland, U.S.A.
1969 M.A. (Economics), UCLA, U.S.A.

Work Experience:

- May 1997-June 2001:
  - Secretary General, Thai Government Pension Fund

- August 1987-February 1996: Thai Danu Bank
  - Strategic Advisor
  - Senior Executive Vice President
  - Senior Vice President

- October 1969-April 1987
  - Manager, Financial Institution Development Fund
  - Deputy Director, Department of Bank Supervision and Examination
  - Division Chief, Banking Analysis Division, Banking Department

Others:

- Fellow Member, Thai Institute of Directors
- June 1992 - June 1995 Member of the Board of Directors, Stock Exchange of Thailand

MR. ANDREW L.T. SHENG
Chairman
Hong Kong Securities and Futures Commission

Mr. Andrew L.T. Sheng was appointed the fourth Chairman of the Hong Kong Securities and Futures Commission in October 1998.

Prior to joining the Commission, Mr. Sheng was the Deputy Chief Executive of the Hong Kong Monetary Authority from 1993 to 1998. There, he managed the Authority's reserves and external departments. From 1989 to 1993, Mr. Sheng was seconded to the World Bank, Washington, D.C., where he was with the Financial Sector Development Department. From 1976 to 1989, Mr. Sheng held various positions at Bank Negara Malaysia (Central Bank of Malaysia) including Chief Economist and Assistant Governor in charge of Bank and Insurance Regulations.

In November 1999, he acted as the Chairman of the Task Force on Implementation of Standards, a task force formed by the Financial Stability Forum. In 1998, Mr. Sheng co-chaired the Working Party on Transparency and Accountability, one of the three Working Parties formed under the Group of Twenty-two Finance Ministers and Central Bank Governors.

Mr. Sheng was educated at the University of Bristol where he received a First Class Honours Degree in Economics.

MR. PETER SULLIVAN
Chairman & CEO
Lombard Investments, Inc., San Francisco

Peter Sullivan directs the overall international operations of Lombard and its various investment funds. Prior to joining Lombard, Peter was the Ranking Vice President of the Asian Development Bank (ADB) in Manila and senior American on the staff of the Bank.

During his 25-year career at the Bank, Peter held various management-level positions including Vice President (Region East), Vice President (Operations), and General Counsel. As Ranking Vice President and Vice President (East), Peter was responsible for supervising a lending program between US$3 billion - $7 billion per annum, and administering a loan portfolio of over $24 billion for the developing countries of East Asia, the Pacific, and Central Asia.

Peter was also responsible for the Bank's procurement and consulting contracts, and chaired the Investment Committee for the Bank's $600 million Staff Retirement Fund.

After serving in the United States Army, Peter began his business career as a lawyer with Sullivan & Cromwell. He earned a Bachelor of Arts degree from Princeton University and a Juris Doctor from Yale Law School.

DR. TEH KOK PENG
President
GIC Special Investments, Singapore

Dr. Teh Kok Peng is the President of GIC Special Investments Pte Ltd, a member of Government of Singapore Investment Corporation Private Limited (GIC). Before that, he was concurrently a Deputy Managing Director of the Monetary Authority of Singapore (MAS) and a Deputy Managing Director of GIC. Dr. Teh worked with the World Bank in Washington D.C. for six years, from 1975 to 1981.

Dr. Teh did his undergraduate studies in Australia and his graduate studies at Nuffield College, Oxford, England. He attended the Advanced Management Program at the Harvard Business School in 1989.

He was a member of the Board of Trustees of the Chinese Development Assistance Council, the Advisory Committee of the Institute of Policy Studies, and the Consultative Committees of the Department of Economics and Statistics, National University of Singapore and the Department of Applied Economics, Nanyang Technological University. He was on the Board of Trustees of the Institute of South East Asian Studies from 1984 to 1997. He was the President of the Economics Society of Singapore from 1991 to 1997. Finally, he is a board member of several companies and funds in which GIC Special Investments Pte Ltd has invested.

In 1993, Dr. Teh was conferred the Public Administration (Gold) Award by the President of Singapore.

AMBASSADOR LINDA TSAO YANG
Acting 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 female Executive Director appointed by the United States Government to the Board of a multilateral development bank 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 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 the then $80-billion 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 an advisor to Lombard Investments, a private equity investment firm in San Francisco. She serves on the board of The Pacific Pension Institute, The Center for Asia Pacific Policy, RAND Corporation and The California Asia Business Council.

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 Chiao-Tung University of Shanghai, she is the mother of two sons.

Asian Corporate Governance Association

The Asian Corporate Governance Association (ACGA) is a private, non-profit organization incorporated under the laws of Hong Kong. It is dedicated to facilitating corporate and economic development in this region through improved corporate governance. Our principal objectives are :

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Sponsors :

Lombard Asian
Private Investment Company

CHUBB

CLSA
EMERGING MARKETS

Sun Life Financial

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