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Synthesis Note

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&

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**Ministry of Heavy Industry and Public Enterprises
Ministry of Corporate Affairs**

**NFCG
National Foundation for
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The transparency in SOE performance and in the way the state exercises its ownership function is a key recommendation of the OECD Guidelines on Corporate Governance of State Owned Enterprises. The Network on Corporate Governance of State-Owned Enterprises in Asia met in New Delhi, on 25-26 June 2008, to discuss this important topic in the Asian context. Under the chairmanship of Mr. John Lim, President of the Singapore Institute of Directors, this meeting was co-hosted by the Ministry of Heavy Industry and Public Enterprises, the Ministry of Corporate Affairs (MCA) and the National Foundation for Corporate Governance (NFCG), and the Standing Conference of Public Enterprises (SCOPE). It was supported by the Government of Japan and the Global Corporate Governance Forum.

Participants continued the work started in Singapore two years ago, focusing on how best to implement the OECD Guidelines in the specific economic, legal and political context of Asia. Most of the meeting focused on two chapters of the Guidelines, namely transparency and disclosure and the equitable treatment of shareholders. The first two sessions of the meeting focused on the Indian situation, with influential officials, business leaders and scholars discussing the reach and achievements of current reforms. Participants also engaged in an animated discussion about the current landscape for SOE governance reforms in Asia. A special address was made by KPMG, India to discuss challenges in converging towards IFRS for SOEs. Finally, a drafting session allowed discussion of a draft regional policy brief giving recommendations with regard to reforming SOE governance in the Asian context.

The level of participation and active exchange of experience confirmed the role that the Network plays as a platform for the policy dialogue on SOE governance in Asia. Policy makers, experts and practitioners from various governments, the ownership entities and SOEs themselves engaged in a very open and rich sharing of experience. It allowed the participants to be informed about the current reforms and main challenges in countries throughout the region and to discuss what could be the main recommendations to be developed in the regional policy brief.

Participants discussed the first four chapters of the regional policy brief and reached a broad agreement on the main content of the remaining two chapters. This Policy Brief will be finalised in the fall 2008 and presented and discussed in the OECD Working Group on Privatisation and Corporate Governance of SOEs in its November 2008 meeting. It will also be presented both in the Global Network and in the next meeting of the Asia Roundtable on Corporate Governance in the second quarter of 2009. This document will be the first of its kind, i.e. developing specific recommendations on priorities for implementing the OECD Guidelines in a regional context. It is expected as such to be also of relevance and use outside of Asia.

All participants also agreed that the finalisation of the policy paper should be considered only as a first step, while the future work of the Network should focus on implementation. The issue of enforcement and implementation was underlined as critical, as well as the one of professionalisation of SOE boards. Thailand volunteered to host the next meeting.

The key messages from this meeting are as follows:

- India has undertaken significant reforms to improve the corporate governance of its SOEs, including in the area of transparency and disclosure. The new Company Act will include new provisions strengthening transparency and disclosure requirements as well as protections of minority shareholders. The MOU system has proven effective in defining more clearly SOE objectives and allowing closer monitoring of results. The recently adopted Guidelines on corporate governance for CPSEs, developed by the Department of Public Enterprises (DPE), are to be commended and include interesting monitoring and compliance mechanisms. Various institutions such as the SCOPE are active in encouraging better compliance by SOEs. However, there is still a long way to go, especially in terms of effective compliance and at the state level, though some efforts are on, in Kerala for example. In terms of accountability, a number of measures have been

taken in order to enhance the operational autonomy of CPSEs, especially for the most important and profit making SOEs with the status of “Navratna” and “Miniratna”.

- A number of Asian countries have also undertaken **significant corporate governance reforms** and reviewed their legal and regulatory framework. These reforms often include the adoption or review of corporate governance codes and the professionalisation of SOE boards, reviewing their structure and functioning, such as in Indonesia, as well as their nomination processes, such as in Thailand. Some of these reforms have been broad in scope and ambitious in their implementation, such as in Malaysia, where positive results are beginning to be seen.
- Good practices and **interesting initiatives** could be sources of inspiration, for example the development of a directors’ pool in Thailand, or the corporate governance scorecard and the setting up of an Institute of Public Corporate Governance in the Philippines.
- A number of SOEs in Asia have still important **policy objectives**. Policy objectives should be transparent and related costs covered from the state budget, and not confused with CSR. CSR, in turn, should be embedded in corporate culture strategic and related actions sustainable.
- **MOU-type systems** have still to be developed in some countries, with a balanced set of objectives. They are critical in curbing interference in day-to-day management.
- It is necessary to improve the **monitoring of SOE performance** by ownership entities and develop more systematic benchmarking, including with foreign peers. An overall “eco system” needs to be put in place to be able to discipline the SOEs’ objective setting and performance monitoring system.
- SOEs are often submitted to a **multiplicity of audits** and efforts should be made to clarify their respective roles, encouraging complementarity rather than duplicity. It is critical for internal auditors to report to a truly independent audit committee, which would also be responsible for selecting competent and independent external auditors.
- Developing an **aggregate report** on SOEs remains a challenge for most countries in the region. To date, only India has a long experience in doing so and Singapore a more recent one. Such reports are instrumental in enhancing transparency and have proven to be useful communication devices.
- A number of countries are in the process of developing an **ownership policy**. This is considered important to enhance the overall transparency and predictability of the state as an owner.
- The protection of minority shareholders is a cornerstone for developing capital markets where SOEs are often the largest capitalisations. Legal and regulatory frameworks are in most cases appropriate, but **enforcement is weak**. Minority shareholders should also become better informed and more active.
- For many Asian economies the legal and regulatory framework for transparency and disclosure as well as for the equitable treatment of shareholders is considered as appropriate. The main challenge remains in **implementation**. Mechanisms to encourage compliance include regular monitoring by the ownership entity or others, such as regulators, awards, press coverage, etc. Courts can also play an important role by prompt and efficient resolution of issues involving minority shareholders.
- In carrying out reforms, **prioritisation** is of the utmost importance. Reforms should be progressive and sustainable. It is necessary to advance step by step and might be advisable to **focus** on a selected number of large SOEs.
- The role of **independent directors** on SOE boards is crucial and remains a key challenge in some countries. The **nomination process** for directors, and especially independent directors, should be based on merit and also be and perceived as free from political interference.

- To improve enforcement and compliance, it is important to generate **political support** for governance reforms.
- **Public awareness** and support is also necessary to press for reforms. The role of competent **media** is important in this regard, as well as the role of **non-government actors**.

More specific and detailed review of the different sessions' discussion is presented in the following pages.

In its welcoming remarks, **Dr. Dewan**, Director General of **SCOPE** welcomed all participants from foreign countries, international and Indian organisations and thanked the government of Japan for its financial support. He reminded participants that the Asia SOE Network was created just after the adoption of the OECD Guidelines on Corporate Governance of SOEs in 2005 and that it was the first regional network of its kind¹. He drew their attention to the objectives of the Network and the focus of this meeting, i.e. transparency and disclosure. He also expressed the view that the finalisation of the policy paper should be considered only as the first step, while future work should focus on implementation.

To set the stage for the discussion, Dr. Dewan underlined the significance of SOEs in the Indian economy² and described the important reforms undertaken by the government of India to improve the corporate governance and transparency of SOEs. The intent of the government is to make the PSUs (public sector undertakings) truly board governed. Important reforms included the development of the MOU system since 1987, the increased autonomy granted to PSEs' boards through the *navratna and miniratna*³ status, the report by the Gupta committee granting them even further autonomy and consolidating the accountability towards parliament, the BRPSE in 2004⁴, the recently adopted Guidelines on Corporate Governance developed by the DPE, dealing with the constitution of boards, audit committees, reporting systems, etc.. In May 2008, recommendations on remuneration of executives were also adopted, delinking it from the civil sector pay structure and introducing performance related pay, which constitutes a paradigm shift. Regarding transparency issues, in May 2008, 24 PSEs signed a MOU with Transparency International Belgium and adopted an Integrity Pact System related to transparency in procurement. He also reminded participants that listed PSEs were subject to high corporate governance standards through the SEBI listing agreements⁵. PSEs are also required to report on compliance with corporate governance requirements in their annual reports. The Institute of Chartered Accountants of India (ICAI) has also issued guidelines on certification of corporate governance to its members. Dr. Dewan underlined the active role played by the SCOPE to encourage the empowerment of SOE boards, the adoption of good corporate governance practices, the adoption of CSR standards, etc.. He also reminded participants that the Company Act is also undergoing amendments to improve, inter alia, its corporate governance related provisions.

Mr. Bandyopadhyay, Secretary of the Department of Public Enterprise in the Ministry of Heavy Industry and Public Enterprises, also welcomed participants on behalf of the Indian government. He expressed great interest in the recommendations that will come out of this Network in the form of the Policy Brief and gave his assurance that the Indian government will take these recommendations into account in fine-tuning the institutional and regulatory framework for SOEs. As had Dr. Dewan, he underlined the important reforms

¹ A similar network has been launched in Africa in the spring 2008 and a Task Force in MENA in the fall 2008.

² PSEs in India are responsible for 2-3 % of the GDP, 27% of the industrial production and employ directly 1.6 million persons. 45 PSEs are listed on stock exchanges and represent around 25% of the market capitalization: 25%.

³ Various powers are delegated to PSEs that have comparative advantages and capacity to become global giants, presently known as Navratnas. Full managerial and commercial autonomy is devolved to successful profit making companies operating in a competitive environment, i.e. Miniratnas.

⁴ Board for Reconstruction of Public Sector Enterprises (BRPSE) was established in December 2004 as a part time advisory body to advise the Government on the strategies, measures and schemes related to strengthening, modernizing, reviving and restructuring of public sector enterprises.

⁵ Clause 49 requires, inter alia, 50 % of independent directors on boards, the set up of audit committees, the adoption of high quality accounting standards and risk management systems, and the protection of minority shareholders.

that have been carried out in India regarding the governance of SOEs and acknowledged that there is still a long way to go. Improving the governance of SOEs should be done to allow them to survive and expand. Since the beginning of the 90's, PSEs have proven that they are able to survive in an open economy⁶. Along with corporate governance reforms, he also underlined the importance of CSR. However, the concept of corporate governance as well as the one of CSR still have to percolate down to the even more numerous state-level SOEs. After the long debate that preceded the adoption of the 2007 Guidelines, India is now ready to play an active role in spreading the message about the importance of good corporate governance for SOEs. This Network's meetings are very useful for learning about what is happening in other Asian countries and for having a meaningful dialogue on most important challenges regarding SOE governance.

Mr. Anurag Goel, Secretary of the MCA, also underlined the importance of this conference and his expectations for active and informal interaction among its participants. He focused his speech on the link between corporate governance and CSR and the importance of the latter, recognising that corporations don't function in a vacuum and that what is decided in the boardroom could affect all sorts of stakeholders. Mr. Goel underlined the importance of an appropriate public accountability framework for SOEs and noticed that good corporate governance practices still need to build in the SOE sector. He mentioned the great impact of the recent Right to Information Act to which SOEs are subject. He also briefly described the main actions taken by his recent Ministry (created in 2004), including: the foundation of the National Foundation for Corporate Governance; the establishment of the Indian Institute of Corporate Affairs; the modification of the competition law and the setting up a competition commission which should be in function before the end of 2008; the introduction of Limited Liability Partnerships and new partnership structures. Following the recommendations of the high level JJ Irani Committee, a new Company Law with better shareholder protections, stronger disclosure requirements and in general improved corporate governance provisions should be introduced this year. He finally described the revolutionary "E governance initiative 2021", whereby all correspondence between ministries and corporations are to be filed in an electronic form, giving an easy public access to all documents.

Mr. Rainer Geiger, Deputy Director in the Directorate for Financial and Enterprise Affairs at the OECD underlined the fact that India is a very appropriate venue for the Network meeting, given the importance of SOEs for its economy and the significance of recent and current policy reforms, as demonstrated by the 2007 Guidelines. He noted that corporate governance is high on the agenda of the Indian government and rightly so, as corporate governance is key to economic performance, access to finance and an efficient functioning of capital markets. Corporate governance is also an important ingredient for the business environment and for the reputation of India as home and host country for foreign investment. The recent OECD Economic Survey of India highlighted the role of sound corporate governance for the economic growth and reform process and recommended the reforms to be vigorously continued to further reduce poverty and spread benefits of it to large parts of society.

Mr. John Lim, Chair of the OECD Asia SOE Network, also thanked the Indian government for hosting the Network meeting and repeated that India is a very appropriate venue with regard to the numerous reforms and initiatives taken to improve SOE governance, with some noted success, most notably the recent Guidelines. He introduced the focus of this meeting, i.e. transparency and disclosure, by emphasising the difficulties in implementation and on the right and subtle balance to be found between disclosure and confidentiality. The unique feature of this Network is the sharing of experience and the dynamic learning environment. With this meeting, all chapters of the OECD Guidelines will have been covered and the Policy Brief completed. However this should constitute only the end of the first phase. The objective of the first phase was to convince all participants that SOE reform is very important. The next

⁶ 156 out of the 247 central PSEs are making quite substantial profits, in addition to providing the budget with large tax revenues. Their investment has also increased significantly since the beginning of the 80's.

phase will be even more important, focusing on how to implement the recommendations developed in the Policy Brief. Each country will have its priorities in terms of implementation, but this work should be continued until effective changes have been implemented.

India Focus 1

As an introduction, **Mr. Tripathi**, Joint-Secretary in the Department of Public Enterprises, presented the main features of the recently adopted Guidelines on the Corporate Governance of CPSEs. India is one of the few countries having adopted such Guidelines, applicable to listed as well as unlisted SOEs. They cover the composition of boards and audit committees and functioning of boards. Important features include the fact that risk management is clearly put under the board's responsibility. The Guidelines also include in an annex a model "Model Code of Business Conduct and ethics for Board Members and Senior Management". They include a whole chapter on disclosure, with the requirements to have a separate section in the Annual Report on corporate governance with details on compliance with these Guidelines. The SOEs should also get a certificate from either their auditors or the company secretary on compliance with these Guidelines. These Guidelines have been adopted after discussion with all relevant stakeholders and consideration of all relevant laws and regulations. The DPE also decided to grade CPSEs based on their implementation of these Guidelines.

Mr. Balakrishnan, Chairman and Managing Director of the Hindustan Petroleum Corporation Limited, introduced his speech by noticing that out of the five Indian companies listed in the Fortune 500, four were SOEs. After a privatisation and a liberalization phase, the focus is now shifting back to the improvement of SOEs and sector regulation. Since the beginning of this century, the regulatory context has changed significantly and there is now an increasing demand for transparency and disclosure to be aligned with practices in developed markets, in order to create an inflow of foreign institutional investors. Companies have realized that good corporate governance is a prerequisite for accessing funds. Good corporate governance boils down to honest and transparent dealings by owners and managers and requires a clear cut allocation of responsibility between board, senior management, shareholders and other stakeholders. Regarding the SOEs, the current policy rules out privatisation and promises full autonomy to PSE boards. Efforts are focusing on modernizing PSEs and closing loss-making ones. SOEs have contradictory objectives due to different roles and separating these roles is difficult. These dilemmas are extensively discussed in the newspaper. A number of measures have been taken to improve the accountability in SOEs over the years, including the MOU System and the implementation of various corporate governance norms, voluntary or mandatory ones, such as the Clause 49 of the SEBI listing agreement. Their implementation implies huge costs, and they should not infringe on the right and duty of management to manage. With the requirement to have half of independent board members (Clause 49), it becomes difficult to find independent and competent directors. The size of the boards should not be increased to accommodate requirements of independence. The DPE Guidelines are a good step in improving the corporate governance of CPSEs. However, challenges remain, particularly regarding "special obligations". Moreover, the plethora of controls⁷ existing on SOEs are onerous and time consuming. The CEOs end up spending their time managing the relations with various forms of the government, rather than managing the company. There is no real need in CPSEs to have more independent directors to ensure transparency as with all this scrutiny there is very little a CPSE can hide in India. CPSEs stand head and shoulder above the private sector in terms of quality of their corporate governance.

Dr. Dewan complimented the DPE for the quality of the Guidelines. These Guidelines will also help unlisted SOEs to prepare for listing. This is the implementation which is tricky. Compliance should not be too costly. He focused his comments on the role of the board. The success of implementation will depend on the competence and the conditions allowing independent directors to function independently and remain

⁷ Internal audit, external audit, DPE, state audit, Central Bureau of Investigation, Parliamentary Committees, etc.

independent. Having one third or one half of independent directors does not make a difference; all depends on what use is made of them. Board should not be too large to allow effective discussion. Dr. Dewan also underlined the multiplicity of reporting requirements and accountability mechanisms, as well as the multiple interferences faced by Indian SOEs, making their CEOs *de facto* boundary managers. The recommendations of the Gupta committee have still to be implemented. No directives should be directly given to the management, and SOEs should be reviewed by their supervisory ministries no more than twice a year. There should be a negative list of areas to be kept away from intervention and comments, except from the CAG. Finally, he warned against CSR loading SOEs to the extent that no more benefits are possible. SOE should not play the role that the state should play. CSR should be strategic to be sustainable.

Mr. B. K. Patnaik, Principal Secretary in the Department of Public Enterprises, reminded the hundreds of SOEs not listed at the state level and played the devil advocate. His main message was that, if transparency is very important, most SOEs suffer not from lack of transparency but from lack of freedom. Many of them are underperforming because they are not allowed to perform the way the private sector enterprises do. Insistence on transparency has resulted in bureaucratization and added costs, with multiple channels for scrutiny and accountability. Focus should be rather put on performance. The Guidelines have given a lot of protection to the shareholders. They have to be protected, but other stakeholders should not be forgotten. Similarly, the Guidelines include important provisions regarding independent directors. Audit committees are important but they should not have an excessive control over management. There is a lack of transparency in the appointment of CEOs and lack of succession plans. Finally, SOEs must perform their social role and do have some CSR. However, it is not the business of business to carry out government responsibilities. CSR norms are like all other norms, they have to be put in perspective.

Mr. M. Kallevig, Deputy Director General in the Ministry of Trade and Industry in Norway, commented on the DPE Guidelines. He found them very interesting, particularly the requirement to report on compliance, and thought they would create greater transparency. He noted however that one point was missing in the Guidelines, i.e. the nomination of the CEO by SOE boards. Without this, boards can not carry out their responsibilities. He also explained that in Norway there are no officials on SOE boards, to avoid the government to be held responsible for unpopular decisions and to avoid political considerations to overcome business ones in the board's deliberations. Other board members would also tend to listen too much to the government representatives and align with their positions. He also asked whether there was room for employees' representatives within SOE boards in India, given the positive experience in this regard in Norway. He finally mentioned the importance of encouraging diversity in boards.

Dr. Y.R.K. Reddy, of Yaga Consulting Group Pvt Ltd & Academy of Corporate Governance, India, complimented the DPE for being very quick in developing the Guidelines and for implementing them swiftly and even to non-listed SOEs. However, what matters at the end is the rate of conformance, and thus the mechanisms put in place to discipline and encourage SOEs to conform. In the SOE case, it cannot be the providers of finance. It might be to some extent the CAG (Controller and Auditor General) or the Parliament. He also questioned the conditions for the selection of independent directors. He advised to get away from nominee directors. The system still needs to be reformed to allow the nomination of truly independent, fit and proper directors. He also mentioned the issue of administrated prices, the costs of which should be born by the state budget. He finally called for an ownership policy to be developed in order to explain clearly how the state exercises its ownership responsibilities.

The discussion covered the issue of excessive accountability, notably with the impact of the recent Right to Information Act. Another discussion was on the nomination process of independent directors and how to ensure they don't become another form of political patronage. If they are not competent, no matter how independent they are. For the time being, in India, they are appointed by the Ministry in charge based on the recommendation of the Public Enterprise Selection Board, as for senior managers of CPSEs. The SOE originally gives a list of ten names to the government, which then sets its own list, which is finalised by the

Selection Board. Based on this process, some argued that there are no political nominees on boards. However, some consider that independent directors not necessarily meet a fit and proper test. Except in Kerala, where independent directors are selected by independent committees. It was also remembered that there still hundreds of non-profitable CPSEs, some with very low turnovers and many beyond any reforms.

India focus 2: The role of competition in fostering SOE efficiency.

Corporate governance reforms are relevant only as much as they affect the performance of SOEs. **Ms. Suryanarayana**, consultant for the World Bank presented the results of a study of SOE performance as compared with the one of private sector companies. This study is however limited to the financial performance and thus does not take into account the number of other mandates that the SOEs might have. The study is based on a comprehensive model assessing the impact of ownership, deregulation and firm specific effects on the performance of SOEs. It shows a lag in the performance of SOEs versus that of the private sector, and that lag is increasing in time. It also shows the importance of firm specific investment which has a huge impact on performance. Regulation also makes a difference, as both private and public sector companies perform poorly in regulated industries. This study is however only work in progress and other policy variables will be added in the future. For example the impact of the MOU process should be studied to nuance the story. Other missing variables are related to the degree of competition.

Mr. Agrawal, Executive Director at the National Thermal Power Corporation Limited, suggested looking at the impact of the MOU system, which should be very positive, and segmenting sectors with respect of the size of SOEs. He also explained the deterioration of comparative performance since the mid 90's by the capacity of the private sector to better adjust to an unstable environment. He also suggested adding another variable regarding the competition for talents. As SOEs are not free to compensate their staff outside of the DPE guidelines, using for example pay for performance schemes, they are always a loser in this front.

Mr. Padmakumar, from the Public Sector Restructuring and Internal Audit Board Industries (RIAB) Department of the Government of Kerala, mentioned about qualitative aspects such as high level of politicization and knowledge gaps in the governance structure at the State level. He also suggested capturing variables external to the firm such as changes in tariff structure, and use of system dynamic models in the study.

Dr. Mishra, from the Institute of Public Enterprise, complimented the Bank for its comprehensive and rigorous study capturing much truth. However, he criticized the too numerous dummies and the absence of policy conclusions. He also questioned the validity of the conclusions because of missing variables and lack of like-to-like comparisons in terms of sector, size, innovation, life span, openness, etc. The private sector sample is too large and many studies have been left over in the literature review.

The DPE called for caution about the conclusion of the WB study, as it seems to depend on the sample studied. It has done similar studies and arrived at opposite conclusions. SCOPE also mentioned a study showing the public sector performance well above the private sector one. SOEs tend to be concentrated in sectors with less competition. The SOE sample is also burdened by loss-making SOEs that are difficult to get rid of, in part due to the lack of adequate bankruptcy mechanisms in India.

The general discussion then covered the excessive accountability mechanisms and the important question of talent management and recruitment. In countries where SOEs do perform better on average than private sector companies, such as Singapore, SOEs outstand in talent management and SOE management gets better paid than in the private sector. Some also suggested using EVA as performance indicator.

The World Bank answered that if the fight for talent had a severe effect on SOE performance; it was difficult to account for it in the model. It also recognized the importance of external factors and will

include sector level consideration in the future model, as well as fine tune it with the degree of competitiveness. A key conclusion is however that firm specific decisions make a tremendous difference. This raises the question of how autonomous and independent are SOEs; what sort of policies can be put in place to force SOEs to think like private sector companies; and how this is linked to the composition of the board.

Landscape session

Dr. Jos Luhukay, Chair of the Corporate Governance Committee in Indonesia, presented the main challenges regarding SOE governance in his country. These challenges include the specific board structure which is a dual model with two boards at the same level, i.e. the board of directors and the board of commissioners, resulting in a failure of control over management. Boards of commissioners are typically composed of bureaucrats and retired generals, as well as political appointees, and are very passive. SOEs became more professionals but not commissioners. Moreover, there are systemic conflicts of interest as senior bureaucrats serve as commissioners in companies they are supposed to regulate. Recently more professionals from the private sector have been hired to serve in boards of commissioners. However, potential candidates are reluctant with regard to the risks undertaken, as mismanagement in SOEs is considered as corruption and could be prosecuted very severely. The lack of experienced professionals is also a real issue and the state begins to import talents from overseas.

Current reforms include the strengthening of governance rules and guidelines. The Code of Corporate Governance has been revised last year, covering also SOEs, while the Code on Public Governance is being adopted and published in the summer 2008. A specific committee has been set up to focus on SOEs, listed companies and companies handling public money. Some reforms are also being undertaken to move towards a single board structure. The CEOs are now supposed to attend the Board of Commissioners' meetings, and even to lead them, while bureaucrats are being withdrawn from them. For example, all officials from the Ministry of Finance have been withdrawn from SOE boards this spring. Boards are being professionalized and the cases of conflicts of interests reduced. Finally, a 2003 Decree by the Ministry of SOEs is finally being implemented, requiring setting specialized committees in SOE boards.

Mr. Fuad Azim Hashimi, Chairman of the PICG (Pakistan Institute of Corporate Governance), updated the Network about current reforms in Pakistan regarding SOE governance. These include the proposed draft regulations for public sector companies, aligned with the OECD Guidelines. A Task Force is also reviewing the Code of Corporate Governance. One of the main remaining challenges is the independence of boards. The roles of Chairman and CEO have still to be separated and the role of non-executive directors to be increased. Reforms are being undertaken, but there is still a long way to go.

Mr. J.J. Moreno, Vice-President of the Philippines Stock Exchange, described the many initiatives undertaken in the Philippines in order to improve SOE governance and focusing on implementation. These include the review of the corporate governance code and the Presidential Memorandum adopted last year in junction with the last Network meeting. This Memorandum mandates the development of performance evaluation systems for SOE boards, the setting up of specialized committees and requires all directors to take an orientation seminar in corporate governance. A specialized Corporate Governance Circle has been created to work with the SOEs themselves, selecting the ten leading ones who could make the difference, based on their score in the first corporate governance scorecard. This scorecard is being reviewed with the circle; it will be carried out once again in 2008 and integrated with the scorecard for listed companies. Finally, an Institute for Public Corporate Governance has been set up. Remaining challenges to improve SOE governance include lack of public awareness and support.

Dr. Areepong Bhoocha-oom, Director General of the State enterprise Policy Office in the Ministry of Finance of Thailand, described how the current reforms in Thailand focus on SOE boards. The main

problem lies in the transparency of the nomination process and continuity of board members. SOEs are usually established by specific laws, with sector Ministries in charge with appointing board members. When governments change, board members change also. To improve the situation, the Act on Qualification of Board has been revised. Candidates must now be under 65, have no political affiliation and no conflicts of interests. In June 2008, a law has been adopted to create a pool for credible and competent SOE directors. The selection committee for this pool comprises of persons known as non-political, independent-minded and who engage their credibility. The pool comprises of 50 people so far and the objective is to find additional 200 candidates with expertise in different areas and sectors. Applications to enter this pool can be received from the public, from head hunters, or from the members of the selection committee. All candidates are then scrutinized by the selection committee to ensure their competence and credibility. According to the law, one third of the board members will have to come from this Directors Pool, eventually the experts for specialized committees. No matter the changes in the governments, the directors coming from this pool should not be changed. But the selection process is not part of the Law. The idea of creating a specific IOD for the public sector is also considered. Apart from this focus on boards, Thailand has also adopted international standards of corporate governance, and the new revised corporate governance code will be adopted soon. Finally, following the recommendations of the OECD Guidelines, Thailand is trying to develop an ownership policy document and it should be adopted this year.

The general discussion focused mainly on board issues, how to professionalize SOE boards and whether SOE board members should be certified. In many countries, SOE directors cannot be paid sufficiently and people serving on SOE boards need to have a sense of national duty as well. However, increasingly SOEs are paying better compensation for better qualified directors. As a conclusion, the Chair reminded that to carry out effective reforms, prioritisation is of the utmost importance. It is necessary to undertake sustainable reforms and progress step by step, not doing too many things at the same time. One has to move towards building capacity for sustainable long term improvement. Steps have to be taken to put in place a capacity to sustain the desired changes for the long term.

After this update on current reforms in Asia, the World Bank and OECD updated the Network participants about their activity regarding SOE governance. **Dr. David Robinett**, economist in the Corporate Governance Unit, presented a summary of the World Bank's main findings after a number of SOE reviews of SOE governance carried out in a number of non-OECD economies, with a focus on Bhutan. In most countries where a review has been undertaken, major reforms have been introduced afterwards. One important finding is that the dual model of ownership is prevailing, with both the Ministry of Finance, typically, and a line ministry supervising the SOEs. Weaknesses associated with this model include a limited focus on corporate governance, little private sector culture, political influence if not interference, etc. Ministers (or officials second in line) serve often directly in SOE boards, while other directors tend to be investors' representatives. There are no independent directors. As for CEOs, they are often civil servants, paid according to the civil service pay scales. In some countries there are still political appointees, CEOs changing with governments and without business experiences. MOU or similar systems for agreeing on objectives are not common and there are typically a lot of implicit social objectives with very large fiscal implications not widely understood. There is at the same time too much and too little auditing, often the wrong kind of auditing. One way performance has been enhanced in a number of countries is through listing. This is a global trend, leading to more transparency and better governance. In Bhutan, these issues have been addressed through bold reforms including the establishment in 2007 of a holding company Druk Holdings and Investment. The role of the Ministry of Finance has been reduced. The Druk Holding makes decisions about the SOE boards and has introduced a MOU-type system. But there are remaining and important challenges. As the economy has been dominated by SOEs for so long, it is difficult to switch to a more private sector like model. Practices are deeply embedded inside the SOEs themselves.

Dr. Mathilde Mesnard, economist at the OECD, presented the main features and issues covered by the Transparency and Accountability Guide about to be published, explaining why the OECD Working group

on Privatisation and Corporate Governance of SOEs choose to focus on transparency and accountability issues. Transparency gives substance to shareholders rights and is a choice remedy for fraud and manipulation. In the case of SOEs, accountability is also vital as it underpins public trust. The objectives of the Guide are to facilitate the implementation of the OECD Guidelines on Corporate Governance of SOEs in the area of transparency and accountability, to help evaluating current practices and framework and to provide policy options and roadmaps. The Guide also provides specific examples of good practices.

Theme I: Monitoring and Reviewing SOE Performance

The Chair of the Thematic Session I, **Mr. Chandra, Chairman of the Task Force on MOU**, highlighted the significant changes in the economic environment, requiring much greater flexibility from the SOEs. They need to be more competitive than they used to be when they functioned in a protected environment. However, they still have important social objectives, especially in a large country like India with pockets deprived of economic growth. It is still necessary for SOEs to focus on providing basic inputs, prices are still administrated for some products, such as oil, and certain sectors are still reserved for SOEs. Of course, the whole economy is being liberalized, but most SOEs still suffer from hindrances in their operations. All these factors need to be kept in mind when discussing the system for setting objectives.

Dr. Kumar, Advisor in the Department of Public Enterprises, provided an in-depth historical overview to explain the relevance and rise of SOEs, from the necessity to catch up for late comers in the industrial revolution, to market failures, the rise in Keynesian economics, etc. He explains the main macro objectives of SOEs, i.e. economic growth, ensuring sufficiency, low and stable prices, long term equilibrium of the balance of payment, raising aggregate demand, etc. He then exposed the continued relevance of SOEs in the Indian context, with continuing gaps between the needs for investment and both domestic and foreign investment, especially in the infrastructure sectors. Large investments by SOEs will continue to serve the objectives of development. Price stability is also an important objective, especially in face of growing primary prices. As for company-specific objectives, the MOU system allows agreeing on company-specific objectives, with yearly performance evaluation based on balance scorecards. Evaluation is crucial as what gets measured gets done. “If you don’t measure results, you can tell success from failure. If you can’t see success you are probably rewarding failure. If you can’t see success you can’t learn from it”.

Mr. Choudhury explained that the first target of SOEs in Bangladesh should be efficiency, i.e. reducing the cost of production without affecting quality. There is still a huge scope for cost reduction, with a lot of wastes and leakages which are the main reasons for SOE failures. Then there is profit maximization. As long as money has been invested, one should not forget the returns. The third objective is financial sustainability and the reduction of dependence from public finance. As for compliance with good practices in terms of corporate governance, one size does not fit all and it is important to be realistic in terms of implementation. There are some social and political realities that should be taken in consideration. Reforms should be progressive as too ambitious reforms might be counterproductive. It is useful to develop Guidelines and to update them often in view of external shocks.

The general discussion focused on the role of the board in doing trade-offs and prioritizing among conflicting objectives. Some would prefer the idea of “marrying” these different objectives. De facto SOEs have multiple masters but the government should not interfere into this, once the objectives have been set up. The ultimate objective is to ensure sustainability. The costs of social or policy objectives should be covered by the budget in a transparent manner. This issue is covered in a specific session of the TrAc Guide. Another important discussion covered the process of performance benchmarking, its difficulty and most appropriate indicators, including return to shareholders. Comments on the Indian situation were made, underlying the significant improvements in India, where SOEs could now be considered as professionally managed, with management appointed no more by the ministries but by the PSAB.

Theme II: Monitoring and Review SOE performance

Mr. Behuria, Chairman of SCOPE and Indian Oil Corporation, underlined the fact that the Indian system to monitor and review SOE performance is comprehensive and robust. All PSEs have to ensure compliance with SEBI Guidelines. In addition, accountability is effectively ensured through various mechanisms⁸.

Mr. Katheerayson, Senior Vice-President in the Transformation Management Office of Khazanah, presented the comprehensive reform undergoing in Malaysia in terms of SOE governance. The Transformation Program for GLCs (government linked companies) is part of a broader and long term modernization program of the national economy. Launch with the “transformation manual” in 2004, it is based on benchmarking of performance and look at foreign experiences. It begins to show results now, with the 20 largest SOEs outperforming the KLPCI by 2.7%. Ten initiatives have been launched, with the development of in-house guidelines. The program is realistic, performance-focused and highlights governance issue and shareholder value. One central initiative is to enhance the role of the GLICs as professional and active shareholders. SOE boards are at the center of this transformation program, with a “Green Book” on board effectiveness, describing an ideal director; requiring, inter alia, diversity in directors’ profiles, specialized committees and the separation of Chairman from CEOs. In practice, SOE boards have already transitioned away from using retired civil servant to serve in boards. A Director’s Academy has been set up, in collaboration of the IMD in Switzerland, in order to enhance the competencies of directors. The Silver Book focuses on stakeholders’ relations and the Orange Book on talent development, and recommends that human resources issues be discussed at board level. New CEOs have been brought in, they have now three years contracts with remuneration and renewal based on KPIs’ completion. It has been a difficult process but it is beginning to pay off. The next phase will be to review their benefits and compensation. Since 2006, GLCs report on their headline KPIs, and this is a very powerful mechanism to trigger changes. Next years a sector benchmarking will be performed.

Mr. Ramachandran, Director in the Department of Public Enterprises, discussed in more depth the monitoring system in India. In addition to the quarterly evaluation done by line ministries, annual reviews are also carried out with the help of the DPE. A special Task Force discusses SOE targets with both the CEO and line ministry concerned. Yearly performances are first evaluated by the SOEs themselves, then sent to the DPE, before being placed before the Task Force and evaluated on a scale of 1 to 5. The performance of CEOs and board members will be linked to this score, and in some cases it is link ed with performance based remuneration. In the case of Navratna companies, an inter-ministerial committee with the Secretary of the DPE, representatives from the Planning Commission and Ministry of Finance, reviews annually their performance and assesses whether or not they should be granted more autonomy. In addition, a “High-Power Committee” headed by the Cabinet Secretary of India reviews Navratnas’ performance every three years.

The general discussion focused on how detect poor performance and to link compensation to performance. It is usually difficult to identify poor performance and in many countries dismissals are still rare except for proven misconduct. In some countries such as Malaysia, it is possible to rely on continuous monitoring by boards and a sound accounting and auditing system is in place and able to pick up early signals. As for objectives, soft targeting is avoided using “smart” criteria, through industry benchmarks, both domestic

⁸ Quarterly reviews by line ministries; financial results published in news paper and on SOE websites, as well as annual MOUs; annual reports presented to Parliament and periodic reviews by parliamentary committees; the High Powered Committee of Secretaries assesses the performance of MOU signing central PSEs; a three tier audit system (internal, statutory audits and CAG); audit reports of the CAG presented to both houses of Parliament, examined by Parliamentary committee which calls top managers and Secretaries for oral examination; the Parliamentary committee makes recommendations; an action taken report on the recommendations of the committee is prepared, its compliance is watched and pursued; the CAG monitors the follow up action and its findings are presented to the Parliament again.

and foreign. Moreover, soft targets would be detected by the analyst community, the minority shareholders' associations, etc. A whole "eco system" or institutional framework has to be in place to be able to "discipline" the objective setting for SOEs. Regarding social objectives, there is a general need first to distinguish clearly between policy and social objectives and CSR and to focus CRS efforts.

As a conclusion, the reforms undertaken in Malaysia were commended, with a number of smart strategic decisions, including focusing on the biggest SOEs, putting in place competent management and boards, and establishing a MOU system to curb government interference in day-to-day management.

Theme III: Auditing Performance

Mr. Ved Jain, Chairman of ICAI, introduced the session by comparing an economy to an airplane, where both public and private governance must be solid. Accountability is an essential pillar of democracy, and must be to the public as soon as the resources managed are public. Audit activities have developed significantly in the past decade in India. However, the multiplicity of audits is a significant issue. Internal audit allows a critical appraisal of the functioning of an identity with a view to suggest improvements and add value. The ICAI plans to codify best practices in internal audit, providing some industry specific guidance. External and internal auditors should work in a complementary fashion. External auditors lend credibility to the published financial statements. They might also do compliance audit, value for money audits and audit public interest issues. They must be independent in fact and in appearance, and apply high standards of professionalism and ethics. The ICAI, an IFA member, has issued 35 auditing standards based on IAASB, and the full convergence with IASB/IFAC auditing standards will happen by December 2010.

Mr. Hashimi, President and CEO of Pakistan Institute of Governance, discussed the important role of audit committees. Independent directors have a crucial role to play, and as long as they are really independent, the internal auditor might perform his function and dig out problems. It is also important for the audit committee to have a charter, with one meeting should be dedicated to review the budget, one held with the external auditors without any executive director, and one with the internal auditor. SOEs are also usually late in the area of risk management, and their Annual Report, in Pakistan, do not include a corporate governance report, except those listed ones. The minutes of board meetings in financial institutions are now required to be sent to the central bank. It is a good alternate remedy to state audit. Independent directors feel confident that if they have issues it is documented and somebody will act. The Government Public Account Committee is too slow and goes after small issues rather than major ones. Mr Hashimi concluded by making two controversial recommendations. First, in a SOE, the internal audit department will never feel confident enough to be independent. To be effective it should thus be outsourced to specialists. It pays back very quickly. Secondly, external and state audits should never meet and remain totally separate. He thus fully disagreed with the idea of having joint audits.

Ms. Lopa Rahman, from the Bangladesh Enterprise Institute, discussed the key elements of a robust auditing system and described the main features of the Bangladesh audit system. She argued against the merger of the two audits (external and state audit) but call for avoiding duplication of efforts. In Bangladesh, state audit reports or objections are passed to the Parliamentary Standing Committee and the Public Account Committee looks at how to resolve the objections. A World Bank report however underlined that a large number of objections are never resolved. But the issues picked up are not always the most important ones. To improve the audit system, there is a clear need to set good audit objectives for the GAC with detailed work plan. It is also necessary to have qualified people performing state and external audits. External audit should be more independent, and the public account committee could also be strengthened. Finally, value for money audits should be developed.

The general discussion covered how to overcome information asymmetry for non-government shareholder.

One option is for the board to pass a resolution permitting the disclosure of state and/or internal audit reports to minority shareholders. Moreover, directors are supposed to represent all shareholders, including minority shareholders. In some cases, these later might also have some “representatives” seating in the board. Discussion also covered the issue of multiplicity of audits and their possible duplicity, as well as whether or not there should be any merger of two of them, with clear divergence within the group. The internal audit shall ensure that the system works according to standardized processes and that the figures are reliable. The external audit takes care of all stakeholders. Some questioned why the state, as a major shareholder, should need another audit, i.e. the state audit, especially if the external auditors are competent and independent. The state auditor might be mandated to look at a specific issue. As for the internal auditor, it should be sufficiently independent, reporting directly to the audit committee of the board.

Theme IV: Reporting on Aggregate Performance

Mr. Kallevig, Deputy Director General in the Norwegian Ministry of Trade and Industry, exposed the Norwegian six years experience in developing an aggregate report. He explained how such reports and the process for developing them contribute to greater transparency and openness of the state shareholder, which is thus perceived as a predictable and professional administrator of the state sector. It also introduces some competition between SOEs which get their own pages in the report. The report is released in May with a special conference to get public and media attention. Ownership entities need to have smart people focusing on it, but for no more than two years in a row. As for reporting to Parliament, the yearly aggregate report helps the politicians to keep abreast of the developments, accepting a formal report only every four years. An “Ownership Policy” has also been published in 2006, clarifying the government’s expectations from SOEs. Developing aggregate reports is a good thing but hard work; it strengthens the ownership unit, gives opportunity for many comparisons and builds trusts on how companies operate. It might also be a way to shame companies towards better compliance.

Ms. Thi Phuong Thuy Tran, from the State Capital Investment Company, explained how there is still a long way to go in Vietnam for the SCIC to be able to develop an aggregate report. She underlined the complexity of the Vietnamese situation where SOEs still play a leading role in the economy. In terms of reporting, most SOEs do have annual reports, but this is not compulsory. They are sent to line ministries, finance ministry and even the Prime Minister. However, in most cases these annual reports do not include audited financial reports, they are more public relation exercises. In addition, the Prime Minister receives different reporting from the line ministries, the SCIC and SOEs themselves. There is not a real picture of the SOE sector in a simple and short format. Even within the Ministry of Finance, the ministry which is in charge of financial management of the SOEs, it is difficult to build up an aggregate report. There is no requirement for reporting to the Parliament. Financial results of SOEs are independently audited. As for state audit, it does not cover systematically all SOEs annually. It is carried out at the request of the Prime Minister. However, there are some government bodies fulfilling financial inspection functions. There is no reporting on non-financial matters, no MOU-type of system. SOEs objectives are not clearly defined, enabling them to manipulate outcomes and performance. Most reports from SOEs do not reflect the real picture. There are many hidden items not appearing on the balance sheet and many SOEs make a loss. It is sometimes even difficult to consolidate financial reports within one SOE, in case it has different and many subsidiaries. The MOF has been requested to make assumptions for consolidation of accounts. Vietnam still applies a national accounting and reporting system. Although the VAS is converging towards IAS, it will take a long time to fully converge.. Because there is not a clear picture on SOE performance in general, there is a lack of strong evidence to put pressure for reform. The pressure on the Ministry of Finance to make a clear report on SOE performance is still weak. Another independent body should be responsible for developing an aggregate report. Moreover, there is a lack of competent media to use such aggregate reports and the general public is neither knowledgeable about the role of SOEs nor interested in their performance.

Mr. Kumar described the Indian experience in developing aggregate reports. Such reports present to all the stakeholders a clear picture on SOE performance in a concise way, building trust by sharing information. The format of such reports should make them easy to use and understood by ultimate users, the public. In India, the first aggregate report was published in 1961, covering all government companies more than 51% owned and statutory corporations. It is based on a survey made by the DPE based on audited and published annual results of all CPSEs. Currently, 156 out of the 217 CPSEs are profit making and the overall picture is solid. The growth in investment has been last year of 9.5% and dividend paid out of 26.5%, good by any yardstick. The Committee on Public Undertaking scrutinizes this report. In 2007, problems identified include price mechanisms, which adversely affect oil related CPSEs, board professionalisation as well as employee attrition. Regarding corporate governance, the framework is robust but there are still problems with implementation. SOEs have to comply in the correct spirit. A compliance study done by the CAG shows that 30 listed CPSEs are not compliant with Clause 49 (21 have less independent director than the prescribed ratio (1/3); 9 have no independent directors at all). 64 are non compliant on other parameters. All listed SOEs comply with the requirement of having an audit committee, but in 18 cases it is not composed as required. Next step is to move forward web-based communication. Another important issue to ensure dynamic disclosure is the training of the media, which play an important role in raising awareness, provided that they are competent. The Right to Information Act is also a powerful tool in the hands of the public, but it seems more abused than used.

Dr. Mak, Director of the Corporate Governance and Financial Reporting Centre in the National University of Singapore, provided some comments on the situation in Singapore, where Temasek has published since 2007 an annual review. This annual review differs from the annual report which is provided to the shareholders, it does not include auditors report, ect. But it is quite detailed, provides an overview of the performance as an investment house but also includes information on boards, corporate governance, risk management, major investments, etc... Invested companies do publish their own annual reports. Temasek board comprises a majority of private sector business leaders (4 out of 7). And its decisions are based only on commercial consideration. Temasek is an investment house, with more of its assets outside of Singapore. It has an objective of being a long term investor anchored in Asia, and an active shareholder.

Theme V: Disclosure by SOEs

Mr. P.D. Sudhakar, Additional Secretary in the Ministry of Corporate Affairs, explained how SOE disclosure has improved in India, including through e-governance. The purpose is to empower the citizens and focus on prevention rather than care. The challenge remains in developing mechanisms to encourage effective implementation. There is also a need for format standardization. The Right to Information act is a revolutionary step and has resulted in the availability of corporate information to various stakeholders.

Mr. Jeremias Paul Jr., Under Secretary in the Ministry of Finance of the Philippines, underlined that transparency and disclosure is not an end in itself, it is to build accountability. In principle, SOEs should be as transparent as listed companies. The key challenge in achieving that is to generate political support for governance reforms, which have to be embedded into a whole governance reform of a country. Another challenge is to foster corporate governance culture through, inter alia, education and training. This takes time. The third challenge lies in implementation. Close monitoring of implementation, benchmarking against international standards and stakeholder consultation are crucial. Finally, due consideration should be given to strategic communication. The disclosure policy needs to focus on material information and be risk-based. Timeliness is also very important. In practice, annual reports are available on line, usually covered by the media. In addition, most GOCCs submit quarterly financial reports to the department of finance. Many GOCCs organize regular press briefings and have websites. The Commission on Audit also publishes an aggregate report on GOCCs' financial performance. Finally, being transparent about special obligations is essential, as many governments consider SOEs as a way of putting off-balance sheet some public or social services. The disclosure policy is imbedded in some laws, charters and code of conduct and

ethical standards for public officials, but usually is expressed in general terms. There has not been a formal review of the existing disclosure policy, but there are some plans to do so. Similarly, disclosing the state ownership policy is also necessary. For the time being, it comes in bits and parts, but the overall policy remains unclear. Work has started to codify and update the existing ownership policy, building on the OECD Guidelines. Each of the GOCCs and various ownership entities try to improve transparency and disclosure, primarily to comply with the Presidential directive. But mechanisms to ensure effective implementation have to be tailored to the specific context and include incentives and penalties. It is important to articulate clearly what is in it for SOEs. Boards are key in this regard, setting the tone at the top. Strategic communication is also important to get the feedback from various stakeholders. Finally, SOEs should have the capacity to implement. Mechanisms include regular reporting, awards, press coverage, investor relations, information on the website, etc. Consistency in implementation is another challenge. But with various ownership entities, it is really difficult to have consolidated monitoring. Another challenge is to strengthen boards. The better the board governance the better the implementation.

Mr. Naresh Jain, CEO of the ICSI and member of the board of trustees of the NFCG, exposed the main challenges regarding SOE disclosure in the Indian context. These challenges include multiplicity of principals and regulators involved, the lengthy decision making process and the multiplicity of relevant guidelines and regulations, without mentioning the parliament's capacity to question SOE management and directors. Finally, the Right to Information Act is abused more than used in the right spirit. To encourage better implementation, it is necessary to decrease the number of authorities involved, and clearly separate ownership from management. Substantial progress has been made recently in India but a lot still needs to be done. Focus should also be put on the quality of disclosure.

Mr. Karma Yonten, CEO of Druk Holdings in Bhutan described the creation of the Druk Holding in 2007. This has solved the issue of numerous principals, as there is only one shareholder, the Ministry of Finance which communicates its main objectives once in a year in the AGM, first and foremost a dividend level. The Ministry also asks for an audit of Druk Holdings and its investments. A "Blue Ribbon" panel has been set up to select the board of Druk Holding and isolate it from political interference. There is also a trend towards contract-based employment for SOE senior officials, purely performance-based. Finally the MOU systems cover five areas, including corporate governance. Some specific CG Guidelines will also be developed, and capacity building and awareness raising will be done in this area.

The general discussion covered the methodology to develop and implement a corporate governance scorecard and the role of non-state actors in pushing for better SOE governance, as it is "too important to leave for governments only". There is a need to create pressure groups, to develop more open and transparent consultative processes. Industry associations, professional bodies, NGOs can all put pressure on state authorities. However, this role of non-state actors depends on the context. At the end of the day, this is a political issue. Ultimately, it is up to the government to do the key SOE reforms. NGO can do: advocacy, media can inform. But what is need is an appropriate institutional framework for governance.

Theme VI: Equitable Treatment of Shareholders

Dr. T.C. Nair, *Chairman* of SEBI, introduced the session by drawing the broad picture of the Indian context. With a large number of SOEs, the government is at the same time owner, manager and regulator. In this context, the focus on corporate governance is sometimes lost. Moreover, enforcement is weak. However, improving the transparency of SOE could only be better for minority shareholders.

Mr. Abdul Wahab Sidek, CEO of the Minority Shareholder Watchdog Group in Malaysia, insisted on the importance of the context for SOE governance reforms. In the Malaysian case, these reforms are embedded in a long term development plan and vision. A High Level Finance Committee has adopted an integrated approach the foster the development of the capital markets. Within this framework, a corporate governance

code has been adopted, mandating changes in the boards' composition, requiring more disclosure and protection of minority interests. For the Malaysian capital market to develop further, the protection of minority interest is a corner stone. The MSWG has been set up to enhance activism and protect minority interests. They should have the opportunity to obtain effective redress for violation of their rights. The main challenges in ensuring equitable treatment of shareholders include the adoption of a shareholder perspective by boards and improving communications and interaction between minority shareholders, board members and management. An Institute of Investors Relations has just been set up to further enhance this communication. The ownership entity has also a role in ensuring the equitable treatment of minority shareholders. Various measures have been put in place, including the tightening of rules for related party transactions and enhanced disclosure in this regard, the possibility for any shareholder to nominate board members, the tightening of the appointment process for independent auditors, etc. The corporate law has also been enhanced with more emphasis on protection of minority interests. It is the common view of both foreign and domestic investors that now an appropriate regulatory framework is in place. What is lagging is effective enforcement. Recently enforcement has improved and has been more timely, but there is still a long way to go. Enforcement has evolved towards using more civil action than criminal suits and provisions now exist for the SEC to take derivative action. So, reforms still need to go ahead but minority shareholders must also know their rights and be better informed.

Mr. Manoj Arora, Director in the Ministry of Company Affairs, commented that India is truly democratic in the area of corporate management, i.e. the one share - one vote rule applies, unlike the general democracy where the minority calls the shots rather than the majority. An effective system is needed to protect effectively, easily and conveniently against abuses by majority shareholders. At a broad level the legal system in India has adequate protection against abusive delisting, related party transactions and insider trading. But on a more day-to-day basis, decisions taken by the management do not always take into account the interests of minority shareholders. This is the case in private sector listed companies, but is even more acute in SOEs. This is a problem of ethics that can not be enforced in any manner at all.

Mr. Sumant Batra, Senior Partner at Kesar Dass B. & Associates, also underlined that, in theory, the law is quite sufficient in terms of provisions existing to protect minority shareholders. This is also the case for SOEs. Sufficient remedies are available, the same than in the private sector. Only few provisions are special, such as an exemption for SOEs for the section 265, i.e. the right of shareholders to have proportional representation on boards. Some general provisions, covering also SOEs, might require some review to allow minority shareholders to have a more effective participation in the decision making. For example, AGM could be organised in another place than only where the company is registered. Some recommendations were made - by the Irani committee in this respect. Efforts are made in the proposed company law to address these issues. However, if the law on the book is good, in practice shareholder democracy does not always prevail. Regarding enforcement, there are a number of provisions and grounds on which basis minority shareholders can approach the authorities for grievance, especially the Company Law Board. But in practice, the Company Law Board does not command that kind of authority over senior government officers. It is difficult for it to issue directions against the government as owner of SOE where allegations of mismanagement or oppression are being made. One of the most effective tools to protect minority shareholders remains the independent directors. The audit report of the Comptroller and Auditor General has shown that in this area SOE compliance is very low: more than 40 percent of SOEs don't have the adequate level of independent directors or no independent directors at all. Even if they have, the public perception is that they are not really independent and that they are appointed on considerations different from their merits, with political interference. This public perception, right or wrong, needs to be addressed. Further need to be done, and seen to be done, in improving the transparency in the appointment process of SOEs' independent directors.

The general discussion covered the importance of shareholder activism as well as shareholder education and awareness. Shareholders should raise their voice and be active to have the right to exercise their rights.

In Indian SOEs, minority shareholders are often banks and financial institutions which remain dormant shareholders even though they have nominee directors. Awareness amongst the retail shareholders is also crucial but there is no credible shareholder activist institution. It is important to encourage such institution as a good prevention against abuses. Other issues discussed covered the definition of minority interests, abuse and equitable treatment. Equitable is a term that can not be described precisely, often it is subject to interpretation and a judgment will have to be made. As long as decisions are based on the overall interest of the company, it is fine. But in the case of SOEs, the overall public interest might also be used to justify a decision. Related parties are also difficult to define in the case of SOEs, there are many explicit and implicit ones, it is difficult to recognize and disclose all of them. The discussion also underlined the key role of independent directors. What is needed is sufficiently empowered boards with a sufficient number of truly independent directors who are truly independently appointed. The role of the Chairman is also crucial in this regard. But an integrated approach is needed, including market discipline, shareholder activism, an appropriate regulatory framework and timely and effective enforcement. Special tribunals for these issues would also enhance enforcement, as well as more deterrent provisions in the Company Act.

Challenges in converging towards IFRS

In India, IFRS will be mandatory in 2011, for listed entities, large companies and financial sector companies, applying to both holdings and subsidiaries. India has adopted an all-at-once approach. Lot of work needs to be get done between now and 2011, lot of regulations need to be adjusted. **Mr Richard Rekhy**, COO of KPMG India, explained how important is this convergence towards IFRS and what will be the benefits for companies, investors, policy makers, regulators and other stakeholders. This include for companies reduced cost of capital and facilitated mergers and acquisitions; for investors better information, more confidence in the information presented and better understanding of risk and returns. It also facilitates comparison, and improves regulatory oversight and enforcement. This will also have an impact on P&Ls. There are significant regulatory challenges and huge needs in terms of training professionals. The specific challenges for SOEs, beside the presentation of financial statements and the extensive disclosure requirements, will include the use of fair values and the treatment of government grants.

Converging towards IFRS is not just a change in accounting standards, it is complex. The time and costs involved should not be underestimated. A good project management team must be put in place and spend time on planning, as well as adequate budget provided. It has to come on the CEO agenda as the tone at the top will drive a successful implementation. It will require dual reporting for a time, harmonizing internal and external reporting, changes in IT systems, a lot of training, and recertification of professionals. A lot of value judgments will be necessary and it will be challenging to find valuers. There might be a huge talent crunch, especially if the US also adopt IFRS.