

Improving Transparency and Standardizing Information Disclosure Is the Social Responsibility of State-owned Enterprises

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Ladies and gentlemen:

Glad to take part in this policy dialogue on corporate governance and thank Director Chen Xiaohong for his invitation. It is meaningful for Enterprise Research Institute under Development Research Center (ERI/DRC) of the State Council to hold this dialogue jointly with OECD, and it is for sure that the corporate governance of state-owned enterprises (SOE) will be further developed and promoted.

Corporate governance contains varied contents and it will also, along with continuous development of economy and the society, be increasingly developed due to the solving of problems. The process of developing corporate governance is also the process of lasting game playing between the trustor and the trustee as well as related stakeholders, and the key reason for this gaming is due to asymmetric information. Keeping improving transparency and information disclosure has always been demanded throughout the development of corporate governance, so this will be an everlasting topic and is receiving more and more attention. No matter Sarbanes-Oxley Act of the USA or existing instructions on going public and governance of companies in other countries, all of them focus on transparency and information disclosure. I believe that, in the future development of corporate governance, it will become even more important.

I Information disclosure is the key point for corporate governance at present

Corporate governance is the check and balance between stakeholders centering on the shareholder's benefit, and the key point of it is a whole set of mechanism for arrangement of the company's rights, division of responsibilities and constraint to protect the benefits of shareholders and stakeholders in accordance with laws and regulations. Disclosure of corporate information means releasing the company's financial and non-financial information completely, accurately, timely and openly to shareholders and stakeholders for the purpose of enhancing their participation and protecting their benefits. Never before has corporate governance been cared as nowadays, no matter the enterprises themselves or the administrative authority, both are trying their best to improve corporate governance.

A sophisticated structure of corporate governance is the precondition for satisfactory information disclosure, however, rules and governance structure is not enough to solve problem. Many companies, with public companies in particular, have established BOD, introduced outside directors as required, set up special committees and formulated rules of their own for corporate governance, and disclosed information as well. In terms of operation, however, there are still some problems. "Fraud show" is continuously performed. Governance structure is easy to establish, but in the aspect of information disclosure, quite a lot of problems are there, either not timely or incomplete, either packaged or disguised. If information disclosure is for some

other purpose, the purpose will inevitably become the induction, if information disclosure is for meeting requirement, the meeting will inevitably be coping with. As a result, true information disclosure will be a challenge to the company, but it is of critical meaning to shareholders and stakeholders. Information disclosure reflects not only the process of corporate governance but also the effect of the governance. A sophisticated mechanism for information disclosure is the key point for corporate governance at present.

II Improving transparency and voluntary information disclosure is the due social responsibility for SOEs

In China SOEs are also called enterprises owned by the whole people, so in this meaning they are public enterprises, in the narrow sense, stakeholders to these enterprises include financier representative, the creditor and employees etc., while in the generalized sense, they may include the whole people. Consequently, for the purpose of supervision by the whole people, SOEs shall be public enterprises with transparent operation and satisfactory information disclosure.

The reform of SOEs has always been the key point for China's economic reform. After many years of reforms such as administration and expanding decision-making power etc., big progress has been made by enterprises in terms of operational efficiency and being market-oriented. However, due to the rigorous control of enterprise by the operator (insider) and the flesh-and-blood relationship between the enterprise and its employees as well as the overlong agent chain, long absence of the financier representative and "taking enterprise as home", control by the insider is quite severe, and poor transparency and asymmetric information extensively exist. It may be put down to artificial control, but it shall be more attributed to the culture formed due to custom. Not only to the outside, even between the parent company and its subsidiaries within a group, the information is sealed and the transparency is absent. And this has become a problem hindering the development of SOEs that must be solved.

As China's economy is in its transformational stage, during the process of system conversion for enterprises, plenty of transactions occur, merger/acquisition and reorganization, restructuring for diversification, standardization for going public, personnel placement, assets disposal, and so on. Among all these, how to embody justness and efficiency has been the key point for the government and the public. With the deepened reform of modern enterprise system and the establishment of BOD, the financier will release more authorization, more and more approval will change into supervision, so, transparent operation and information disclosure, as the decisive factor or successful transformation, is becoming increasingly important. A fundamental engineering for China to develop market-oriented economy is to establish the good-faith system. SOEs are influential not only to the industry to which they belong and regional economy but also to national economy and are the dominant force for China's economy, as a result, they shall assume the key responsibility in the construction of social good-faith system which is based on transparency and information disclosure and shall play the role of a model to promote the forming of the social good-faith system.

III Principles for SOEs in information disclosure and improving transparency

“Trueness” is the most important principle for information disclosure. Information disclosed must be true and shall be simple and understandable as well, otherwise, they may be suspected of packing and dressing, avoiding and hiding, and pretending and covering. Trueness and justness of information disclosure, as an enterprise’s responsibility, is the commitment of the enterprise to all stakeholders to it as well as those potential stakeholders who pay attention to its growth.

“Completeness” is the fundamental requirement for information disclosure and it may also be the requirement for the content. Due to economic development, information required for corporate governance is all-sided. Though the attention point of information requirement by stakeholders may be varied, the requirement of completeness is a universal one. Different organizations have different requirements for information disclosure in different times. Roughly speaking, content of the information disclosed include financial and non-financial information. Financial information is most closely related to the company’s stakeholders and thereby is most frequently needed. The requirement for disclosure of financial information by modern corporate governance has been increasingly deepened, from only caring for ex post accounting to paying attention to the enterprise’s financial development. Financial information usually refers to the annual report, while non-financial information may stress on the environment and the society etc. I think that, as the content of information to be disclosed is concerned, in the aspect of stockholder and stock right: the end controller and the involvement, the concerted actor shall be detailed to natural person, and the end financier representative. In the aspect of BOD: structure and operational procedures, details of special committees, how directors are generated, including the mode of recommendation and nomination, salary and expenses for the top management, risk control, auditors, and details of associated dealings. In the aspect of operation: financial statements, report of critical dealings, purchase, sale and key customers etc. In the aspect of the society: environment, community and employee etc. Information disclosed shall not be limited to existing facts, but shall also include the forecast and analysis of future operation and financial conditions, financial report and governance report can be formed, and in addition, more non-financial information shall be disclosed.

“Timelines” is the value and vitality of information disclosure. Consequently, all issues important to information users shall be disclosed. When disclosing, hierarchies within the enterprise shall not merely disclose those information that are favorable for their benefits and avoid or delay the disclosure of unfavorable information. The company shall provide the shareholder (financer) with governance report and financial report of the year in time and shall also reveal in due time those decision-making information that have key influence on the shareholder’s (financer) benefits such as operational risk, incident, lawsuit, acquisition, merger and business etc. Information disclosure by use of modern information technology is the trend for information disclosure. It makes the company’s governance information further open and enhances information transparency, and what’s more, it enables the decision-maker to use these information for evaluation and making decision.

“Openness” is the requirement for the way of disclosing information which shall ensure easy finding and low cost of obtaining the information. As public companies, SOEs shall be voluntary to disclose information in an open way. Open information disclosure shall be able to

meet not only the requirement of the shareholder, but also other stakeholders, such as the creditor, potential investors and the public.

IV Transparency and information disclosure creates values for the enterprise

Due to increasingly sophisticated corporate governance, the supervisory authority and the investor has much more requirement for information disclosure by the company, which greatly increases the company's cost. According to relevant data, averagely the cost of American companies is increased by some 10 million US dollars due to Sarbanes-Oxley Act, and some other data show that, open and transparent salary has resulted in the increase of salary and compensation for the managers. But on the whole, the investors are willing to pay premium to companies with satisfactory governance and transparent information disclosure. They think the input is worthwhile.

The so-called external evaluation of corporate governance refers to nothing else but the judgment and analysis of the company's information disclosure. As a result, the premium for corporate governance is actually the premium for information disclosure. Information disclosure is a critical symbol for an enterprise to create a good social image and is also the basis for investors to trust in the enterprise and be willing to pay the premium, and this has been a rule at the capital market at home and abroad alike.

Transparency and information disclosure is based on sound inner management and control and at the same time is being able to promote the improvement of inner management and control. SOEs shall put more efforts in inner management and control so as to improve transparency and the quality of information disclosure. Attention shall be given to 4 aspects. First, standardizing internal governance and strictly implementing systems. Establishing a governance structure which centers on the BOD and intensifying the BOD's responsibility of supervision and risk control. Individual control shall be shifted to collective control and strict governance and internal systems shall be implemented. Second, techniques and management shall be employed to reduce artificial factors and to improve efficiency. Third, training shall be strengthened, from the top management to the technical hierarchy and first line employees, to cultivate their awareness of risk, control and flow, and thus to form a corporate culture of transparency and good faith. Fourth, BOD shall be the main body responsible for transparency and information disclosure. Facilitating the interaction between insiders and outsiders and enhancing inner management by virtue of transparency and information disclosure. At present days when credit is absent, transparency is the best way to create values.

China Chengtong Corporation Group is one of those central enterprises under the supervision and administration by SASAC of the State Council. As one of the 7 pilot enterprises for establishment of BOD selected by SASAC, the corporation regards the overall sophistication of information disclosure as the key task in mechanism restructuring for corporate governance. In 2003 we compiled and printed annual report 2002 in strict accordance with requirements for releasing annual report by PLCs and provided them to our corporation's stakeholders. In Aug. 2004 we released annual report 2003 at our website. In 2005 we are also going to release the governance report. These efforts have resulted in good effect, inner control is improved and higher requirement of the auditing organization is raised. Transparent information disclosure provides the corporation's investors with the opportunity for more convenient and deepened

understanding of us, and thus the cost is lowered and the investors are attracted.

V Suggestions on improving information disclosure and enhancing transparency for SOEs

With the problems existed in information disclosure by SOEs of our country in mind, the improvement shall be made mainly in 3 aspects as follows:

First, establish the system for information disclosure. State-owned assets supervisory and administrative authority shall formulate instructions on information disclosure for SOEs according to relevant laws and regulations such as Company Law and Interim Regulations on the Supervision and Administration of State-owned Assets etc., set down comprehensive and standardized requirement as well as implementing rules concerning the disclosure of financial and non-financial information, clarify the minimum requirement and suggested objectives, guide and encourage enterprises to actively disclose information, and incorporate this question into the BOD pilot project and the establishment of modern enterprise system. The enterprises shall also consciously establish an internal system for information disclosure to form the way for complete, timely, continuous and high quality information disclosure.

Second, establish a supervisory and administrative system for information disclosure. State-owned assets supervisory and administrative authority shall require all SOEs, except those involving national economic security, to openly disclose information and can set down a timetable for step-by-step promotion. In addition, information disclosure can be checked and examined on the basis of standardized and sophisticated corporate governance to ensure the trueness of information disclosure. By far, the most important thing is to strengthen the self-practiced supervision by SOEs to form in the end a supervisory system for information disclosure with joined self-practiced supervision and governmental supervision so that the public can make true and timely judgment of a company's value.

Third, improve the social environment and cultural environment for information disclosure. The cultural environment for information disclosure is good faith culture, and as a result, an economic culture shall be formed indeed, rather than replacing economic constraint with political judgment. Research institutes, the media and the economic community shall support those enterprises who actively, truly and openly disclose information. What we do not want to see is that, enterprises are given excessive attention and even are blamed as a result of information disclosure. The society shall be kind to enterprises who keep good faith.