

Fourth Round Table on Capital Market Reform in Asia

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Enhancing Corporate Governance of Thai Listed Companies

By Prasarn Trairatvorakul

***ORGANISATION FOR ECONOMIC CO-OPERATION AND
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Prasarn Trairatvorakul
Secretary-General
Securities and Exchange Commission
Thailand

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The government announced that 2002 is the year for governance reform in the Thai capital market and takes this issue as one of the most important measures under the Capital Market Master Plan announced by the Deputy Prime Minister on January 6, 2002.

The issue of corporate governance has gained much public attention during the past several years. However, the general Thai listed companies are still perceived as having weak governance because of their concentrated ownership structure, family style management, insufficient disclosure, etc.. Realizing that this perception is one of the key risks to building a strong capital market, the Securities and Exchange Commission (SEC) and the Stock Exchange of Thailand (SET) have issued measures to enhance corporate governance of listed companies and much progress have been achieved. Review of the current status and agenda for future endeavor are as follows:

1. Review of the Current Status

Thai economy, similar to other Asian countries, is more dependent on the banking sector and the capital market is relatively small. Most Thai listed companies evolved from successful family businesses and the inherited concentrated shareholding and management structure still remained even after being listed. Connected transactions within groups of companies are more often seen than not. Except for some 30-40 companies, the proportions of shares held by outside investors are relatively low. As a result, roles of outside investors in fostering good governance in these companies are still limited and most investors choose to exit a problem company at a loss rather than exercising their rights to reserve their investment value. These environments make it more challenging to build investors confidence in governance of Thai firms.

However, certain progress has been made during the past few years. On the regulatory side, the following endeavors have been taken:

- Frequency and timing of financial disclosure has long been above the regional average, i.e. listed companies have to submit financial statement on a quarterly basis, the annual statement has to be audited by accredited auditors and the quarterly statement has to be reviewed.
- Accounting standards have been revised and the current standards are already based on or similar to the IAS.
- Disclosure rules have been amended to require more precise and concise disclosure of non-financial information.
- Disclosure documents and financial statements of listed firms are rigorously monitored to be in compliance with the rules and regulations. In addition, to ensure that financial statements are reliable, auditors' performances are also closely reviewed and those that failed to meet auditing standard are severely sanctioned.
- From the year 2000, all listed companies are required to have an audit committee composing of at least 3 independent directors. Duties of the committee are to review the reliability of financial statement, comment whether the proposed connected transactions are fair and in the best interest of the company and review the sufficiency of internal control system.
- Code of best practice for directors and for audit committee have been issued and later updated in 2001. In addition, to encourage companies to practice those guidelines, listed companies are required to disclose in their annual reports whether they comply with those best practices. Any non-compliance has to be explained.
- ESOP programs have always been encouraged to increase commitment of management and employees. However, to prevent abusive use of these schemes that may cause unnecessary dilutions to shareholders, rules have been amended to ensure that sufficient disclosure is made in the notice to call shareholders meeting. In addition, schemes that give outright benefits to concentrated management have to be approved by a remuneration committee.

- To facilitate the exercise of shareholders right, proxy rules have been amended so that shareholders can specify how they want their proxy to vote.

In addition, series of educational programs and seminars have been introduced. The Institute of Director has also been established for training directors and about 300 directors have already passed the course. Most of them feel that the course is very useful and that they have new perspective of being a director.

These initiatives will be meaningless without changes in the practice of listed companies. So far, we have seen improvement in governance of companies particularly the larger ones that have more exposure to foreign investors. Disclosure documents have been much improved to contain fairly sufficient information. Many companies have investors relation units to provide information to investors. Issues on corporate governance and risk management are discussed at board level in many companies. Some companies are forced to improve governance as a result of corporate restructuring and the entering of new partners. Some large family conglomerate that used to have high level of cross shareholding and transactions among companies have restructured to have more transparent business structure. Proposals for some connected transactions have been canceled because of shareholders objection. Further improvements are expected to be underway.

2. Agenda for future endeavor

Attempts to enhance corporate governance of Thai companies during the past several years were mostly pushed by capital market regulators, the SEC and the SET, while the achievement of good corporate governance requires cooperation and coordination from all relevant public and private entities. The Cabinet, therefore, appointed a National Committee on Corporate Governance to determine agenda to create investors' confidence in governance of Thai firms as well as Thai financial intermediaries, synchronize plans of different agencies, and monitor performance of the relevant agencies to be in accordance with the plans.

The Committee is chaired by the Prime Minister or the Deputy Prime Minister and composes of representatives from both the public and private sectors with the SEC acting as the secretariat. Agenda of the Committee will include regulatory measures, disclosure standards, educational programs, incentive schemes for good governance companies, practices of financial intermediaries (banks, securities brokers, asset management companies and insurance companies) that enhance their own governance as well as fostering good governance of other companies. Some of the measures that will be undertaken are as follows:

2.1 Incentive schemes for good corporate governance companies

Although governance in many companies has improved, the overall market perception may not yet be and still be engrossed by the misconduct of a smaller percentage of companies. One of the reasons may be that, unlike financial performance, the practice of good governance principles cannot be as easily identified simply by analyzing a company from outside. Most investors cannot differentiate a good governance company from the weaker ones and, therefore, cannot attach value to those companies and find it difficult to use the level of good governance as one of the investment criteria. Without appreciation from investors, companies may not have sufficient market incentives to improve their corporate governance. One of the key elements of the Committee's agenda is to combine incentive schemes for good governance companies provided by different public agencies (SEC, SET, Company Registrar, and the Revenue Department) to strengthen the attractiveness of the schemes.

One of the main initiatives is to encourage corporate governance rating among listed companies. This rating will enable investors to differentiate the good governance companies from the rest and can then attach higher value to those firms. On the company side, the social prestige that comes with the high rating as well as the willingness of investors to give higher share premium

will serve as strong market incentives for companies to respect good governance principles. On top of that, the SEC will also provide additional regulatory incentives to companies that are highly rated, e.g. their applications with the SEC will get fast track treatment, they will get fee reduction from the SEC and SET that can cover rating expenses, they will be allowed to use certain good governance logo, etc.. Once ratings have been conducted, the SEC will also encourage institutional investors under SEC supervision to use governance rating as one of their investment criteria and disclose to the public.

To ensure that the rating agency that will conduct this governance rating is competent and the ratings are reliable, the SEC, after a careful consideration, has commissioned Thai Rating and Information Services Co., Ltd. (TRIS) to perform the task. It is expected that the rating criteria will be announced to the public sometimes in March 2002 followed by a seminar to provide an explanation to listed companies. So far several listed companies have shown their interests in the rating scheme.

2.2 Education programs

The SET has issued the revised best practices in 2001. Seminars and other educational programs will be arranged to create awareness and encourage compliance to those best practices. In addition, more guidelines on specific practices will be issued, e.g. guideline for fiduciary duty of directors, guidelines for disclosure in notice to call shareholders meeting. Similar programs will be arranged on the investors' side to equip them with more knowledge to protect their own rights.

Empowering Investors

(1) Support of investor association

Similar to requirements in other countries, the corporation law and other relevant regulations require that several issues have to be approved by shareholders and shareholders also have other rights in monitoring performance of the management. However, in practice, these check and balance mechanism cannot work effective as very

few investors exercise these rights to protect their own interest. Each investor may hold a small number of shares and do not have enough resources and knowledge to analyze the merits of management's proposals and monitor their performance.

The SEC, therefore, supported a group of market professional to set up an investor association that will function as activist in each listed company. They will monitor company information and scrutinize management's proposals. If shareholders' actions are needed, they will give out their views to members and solicit proxy to fight with the management. Currently, the SET and TSFC (Thai Securities Finance Corporation) have agreed to sponsor this association to ensure that this project is financially viable. The association is in the process of recruiting and making other preparation.

(2) Amendment of the Public Company Act

The SEC in cooperation with the Ministry of Commerce are revising the Public Company Act and will propose amendment to ensure that investors have sufficient rights to protect their own interest and can use those rights effectively. The threshold on the minimum percentage of shareholders that can exercise each right (e.g. right to make proposals, call a shareholders meeting, etc.) will be lowered but the shareholders will also have to justify the rationale for exercising those rights. More remedial rights will be provided to ensure that oppressed shareholders will be fairly treated. In addition, the roles and responsibility of directors will also be tightened.

(3) Tightening regulations on connected transactions

The flourish of connected transactions in listed companies has always been the major risk to building investors confidence in governance of the company. The SET regulation on connected transactions will be revised and closely monitored to ensure that the transactions executed are indeed fair and in the best interest of the company.

2.3 Law Enforcement

(1) Restructuring of supervisory body

Currently, the supervision of listed companies and enforcement lie with 3 separate agencies, i.e. SEC, SET, and the Ministry of Commerce as the company registrar and care taker of the Public Company Act. This arrangement will be restructured so that corporate governance issues under the Public Company Act will be centered at the SEC for more efficient supervision.

(2) Enforcement process

Under the current regime, all misconduct is criminal offense and has to be prosecuted through the Police Department and the Public Attorney before going to court. In the revision of the law, civil and administrative sanctions will be introduced to lower the “prove beyond reasonable doubt” burden and expedite the cases. In the meantime, more surveillance on potential abuses will be conducted to prevent damage from occurring and more social sanctions will be used.

Conclusion

Corporate governance takes time to evolve and the target keeps moving with the increasing new demands from investors. However, with the strong support from the government and the high level of commitment from the relevant parties, we believe that investors’ confidence in corporate governance of Thai listed companies will significantly increase over the next few years.
