



THE 7TH MEETING OF THE ASIA NETWORK
ON CORPORATE GOVERNANCE OF STATE-OWNED ENTERPRISES

Professionalization of State-Owned Enterprises

SUMMARY OF THE PROCEEDINGS

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1. Opening session

In his opening remarks, the Chair of the host organisation NCGI, **Mas Achmad Daniri**, described the corporate governance (CG) regime in Indonesia. The CG framework including laws, regulations, regulatory authorities, codes of CG, public governance, codes of shariah business, banking, insurance, risk management, ethics, audit and accounting standards, institutes of corporate directors have been making efforts to increase the credibility of the state and to create conducive business environment. He elaborated on their national CG code and its various challenges that Indonesia faces in implementing CG codes. He opined that for good CG it was important to build consensus on CG, system that affects corporate culture and to create a professional corporate culture implementing the right business processes.

In his opening remarks, the Chair of the Asia SOE Network, **Mr. John Lim**, provided a brief description of the Network, its achievements and proposed future steps. He elaborated on the previous 6 meetings of the Network and the Regional Policy Brief, providing a set of recommendations and priorities for policy reform to improve the corporate governance of state-owned enterprises (SOEs) in Asia. The Chair stressed the importance of remaining relevant and outcome focused, and opined that the idea of the Companies Circle (CC) can help achieve that objective and advance the activities of the Network.

In his opening remarks, the representative of Ministry of Strategy and Finance, Korea, **Mr. Young-jin Kim** noted that SOEs contributed significantly to the Asian economy in many sectors. They contribute 25% of the regional GDP and 10% of the employment and therefore it was important that they are effectively managed. In order to increase SOE efficiency, restructuring of SOEs, promotion of transparency, design feedback and evaluation, transparent procurement processes. He highlighted the achievements of various Asian countries in the area of CG. He reported on Korea's progress in improving the performance of SOEs, their governance system, their internal control system.

In his opening remarks, on behalf of the Chair of the OECD Working Party on State Ownership and Privatisation Practices, **Mr. Hans Christiansen** provided the global context in which SOEs are playing an important role in economic development and the changing role of SOEs as a result of the global financial crisis. Given this context, it was important that the Asia SOE Network raise its impact to affect policy making. He informed the participants of the future work that the OECD intends to start, among other projects, a cross-country study on funding and financing SOEs, good practices report on organizing boards, balancing commercial and non-commercial objectives.

A keynote address by a representative from the Indonesian Ministry of SOEs, **Mr. Sahala Lumban Gaol**, presented a profile of Indonesian SOEs, the policy directives relevant for SOEs in Indonesia and CG reform in Indonesia. Fully aware of the importance of good CG, the Ministry of State-owned Enterprises has prioritized steps to ensure implementation of GCG in SOEs since 2002 and has been implemented by different ministers ever since. He also provided a progress report of CG reforms in SOEs and the remaining challenges in implementing good CG programme.

2. SOE governance reforms in Indonesia: experiences & prospects

The session Chair, **Mr. Daniri**, provided a brief context of Indonesian SOEs and stressed that there should be clear separation between the political process and corporate process.

The representative of Pos Indonesia, **Mr. I. Ketut Mardjana**, talked about recent transformations seen in his company. Pos Indonesia needed to transform itself for 3 main reasons i.e. technological changes, changes in government policies (liberalized postal industry, introduced public service obligations, no change in tariffs) and changing competition in the market (private companies and co-operatives). In addition, there was an increased financial burden due to the ratio of number of employees (28000) to pensioners (16000). The traditional mail delivery service was declining in Indonesia like in most countries around the world, forcing Pos Indonesia to diversify into other areas like financial services, parcel delivery, postal retail, logistics, insurance, real estate, e-commerce for rural areas. Their transformation approach included focus on 3 areas i.e. business strategy, implementation of CG and changing the corporate culture and management style. There is a restructuring committee to implement the transformation program. Its responsibilities include specifically how Pos Indonesia can increase its market share and improve its performance, develop an efficient logistics company. To achieve this transformation the structure of the company has now changed from geographical areas to business areas. For good CG, pos Indonesia is trying to implement reforms at the board level, enterprise risk management, internal control and IT governance. Pos Indonesia will become a listed SOE by 2013 in order to further enhance its performance and welfare of its employees. The transformation program has helped improve its performance since 2009. Participants believed there was too much diversification which was not related to its core business, but this was justified by the speaker as its assets were underutilised.

Mr. Indra Utoyo from Telkom Indonesia shared his ideas on implementing good CG in his company. It is listed on NYSE (complying with Sarbanes-Oxley), IDEX and LSE. The government owns 53% of the company. Their turnover was close to \$ 5.5bn in 2011, and has 30000 employees. It is a holding company with 8 subsidiaries and the cellular phone subsidiary contributes to about 65% of their total revenue. Given telecommunications sector being a very dynamic sector, telecom needs to transform. He talked of unfair competition between his company and private competitors in the case when band-width is increased, complementary revenues go to the competitors. Another source of unfairness arguably derives from the higher number regulations that his SOE has to comply with compared with its private sector competitors. Telecom also diversified into entertainment and media. It has standardised its business system and simplified the business cycle in order to be more efficient. In order to align all business units to the overall strategy of the company and create synergy in their operations, they have adopted a parenting system.

Mr. Gusrizal from Pertamina, Indonesia spoke about CG and risk management at his company. The implementation of good CG in Pertamina was initiated in 2003. It involved leadership development, people management and culture change. Leadership development focused on analysing the leadership gap, transforming the leadership engine and recruitment. People management focused on implementing performance management and incentives based performance evaluation. In order to implement good CG practices, the company established its vision, mission and corporate values, conducted a diagnostic assessment and developed a Code of Conduct. Good CG was implemented by applying and reviewing technical regulations and CG best practices i.e. Enterprise Risk Management system. CG monitoring was done by reviewing GCG implementation and evaluating GCG principles at the company level. CG structure at Pertamina includes General Meeting of Shareholders, Board of Commissioners (BoC) and the

Board of Directors. Its supporting structure includes Committees at BoC (Audit, Investment Planning and Risk Management, Upstream, Refinery, Marketing and Trading, HR, General Affairs and Technology, Monitoring), Internal Auditor, Enterprise Risk Management, Corporate Secretary, Compliance Function, HR Function, Information Technology Function, Corporate Legal and Finance. The good CG roadmap and its implementation have so far been to comply and conform to several regulations but they intend to become an ethics driven and professionally managed company working towards sustainable growth. The national economic mandate at Pertamina is to increase domestic consumption and domestic oil production.

All SOEs in the country are required to comply with the various regulations that the Ministry of SOEs issues. The representative of the Ministry of SOEs provided a list of various regulations that have been issued by his ministry since 2002 and the overall objective of these regulations was to separate the political process from the corporate functioning.

3. SOE governance reform in other Asian countries: experiences and prospects

The session focussed on progress reporting was chaired by **Mr. Selim Yesilbas**, of the Turkish Treasury as representative of the OECD Working Party on State Ownership and Privatisation Practices.

Mr. Karma Yonten from Bhutan provided a summary of the reforms which had been undertaken in Bhutan pursuant to the policy brief. The Druk Holdings and Investment's ownership policy was published and has been in effect since May 2010, the policy document provides broad guidelines on the functioning of board directors including the appointment of directors. DHI has developed Compact Guidelines which contain key performance thrust areas, SOEs have developed specific annual targets under the relevant thrust areas with objective indicators, the performance compacts between DHI and SOEs are published on DHI's website. DHI board reviews SOE performance semi annually and their performance data are published in the DHI's annual report. DHI has been organizing board orientation programs annually for all new directors since 2010, two workshops for 40 directors were conducted in 2011 and 2012 with World Bank assistance. In addition, a CG code and a board charter will be developed through World Bank assistance in 2012. Current compact and performance management systems have been reviewed. Currently boards are evaluated on the basis of qualitative measures.

Mr. Zhengjun Zhang from China outlined the progress taken place in terms of SOE CG reform. He highlighted three areas where significant progress has been made – risk control, improving efficiency and information disclosure. Under risk management, SASAC established the monitoring system to oversee bond issuing by SOEs, it examined SOEs' legal work in the past three years to eliminate the legal risks of local SOEs are taking. SASAC now requires SOEs to establish internal control system. SASAC also issued the "Abroad State Ownership Management Rules for Central SOEs" and "Abroad State Asset Management Rules", in order to increase supervision of SOEs operating abroad. In terms of other achievements, 8 new SOEs have established boards taking the total number to 40. In China, independent directors are those which are independent of all stakeholders, SOEs and are not from SASAC. In the future, China needs to establish boards in all SOEs, a proper segregation of commercial and non-commercial objectives, and publish an ownership policy document.

Mr. Arun Kumar Sinha from India outlined the progress in CG especially that of Maharatnas and Navratnas. Since 2010 enhanced powers have been delegated to their Boards to facilitate expansion of their operations, both in domestic as well as global markets. In 2008 a new Variable

Pay/ Performance Related Pay (PRP) directly linked to the profits of the SOEs/ units and performance of the executives was introduced. SOE are required to establish a remuneration committee headed by an independent director to decide on PRP. The DPE has also been involved in formulating a policy for acquisition of raw material/assets abroad by SOEs, publishing a national survey on State Level Public Enterprises (SLPEs) and a code of ethics for the employees of SOEs. DPE has initiated other plans and reforms for the future i.e. listing & partial disinvestment of SOEs, updating the MoU mechanism, further engaging with stakeholders establishing strategy Committee/nomination Committee in boards and a periodic review of performance of independent directors. Of the 173 SOEs which had signed MoU in 2009/10, 73 of them were evaluated to have excellent performance. In India, a challenge remains in protecting the interests of minority shareholders.

Ms. Lya Rahman from Malaysia outlined some key CG reforms implemented since 2011 which included issuance of Capital Market Masterplan 2, issuance of CG Blueprint and issuance of Malaysian Code on Corporate Governance 2012. The Malaysian code on CG puts emphasis on the roles and responsibilities of the board, composition of the board, independence of directors, commitment of directors, integrity in financial reporting, risk management framework and internal control system, timely and quality disclosure and the relationship between company and the shareholders. The main challenge faced by Malaysia is to ensure that in implementing CG practices, SOEs and their directors must truly embrace the spirit of CG instead of merely complying. Malaysia needs further reform for non-listed GLICs in the areas of transparency and accountability, RPTs, nomination of directors and their evaluations.

Mr. Fuad Hashimi from Pakistan outlined the progress made by SECP (Securities and Exchange Commission of Pakistan) in bringing about reforms in CG. SECP issued draft Public Sector Companies (Corporate Governance) Regulations (Draft regulations) in December 2007 which were peer reviewed and advised on by Pakistan Institute of Corporate Governance (PICG). These were updated in 2009. The Economic Reforms Unit (ERU) of MoF put together a Task Force for review of the draft regulations. In early 2012, SECP issued the draft regulations incorporating the Task Force recommendations, as a consultative document. This document is now undergoing public debate through roundtable discussions engaging all stakeholders. The new code stresses on increasing competencies in SOE boards and providing proper training to board members. He elaborated on the shortcomings of the current regime and highlighted 4 of them i.e. lack of transparency in appointment and election of members, absence of formulated strategy making process, lack of aggregate reports on SOEs and a lack of independence on boards.

Mr. Cesar L. Villanueva from the Philippines highlighted the functions of the new Governance Commission of GOCCs. It is a collegial commission with awesome powers (several participants were sceptical about these powers and their functionality) and it is a relatively autonomous body, under the Office of the President. Its powers and mandates include ability to classify, re-classify, as well as sub-classify GOCCs, conduct periodic studies, examination, evaluation and require reports on their operations and management; and evaluate their performance and determine the relevance of GOCCs, to determine whether a GOCC should be reorganized or rationalized; merged or streamlined; abolished; or privatized. In addition, to pursue good governance practices, provide technical advice and assistance to supervising agencies in setting performance objectives and targets for their attached GOCCs, monitor established objectives, operations and targets of GOCCs, conduct Compensation Studies in order to come up with a Compensation Position Classification System and review and recommend to the President for approval the plan by any Government Agency on any new subsidiary or purchase of another corporation. However, the code of CG does not discuss independent directors and all directors are considered public officials.

Mr. Tran Tho Hai from Vietnam articulated his government's ambitious programme on restructuring SOEs and improving their performance. The reform program to be undertaken during 2011-2015 is one of the 3 core reforms targeted for the entire economy. The objective of the reform of the State - owned Enterprises is to improve the performance of SOEs, strengthen their role in both domestic and international economy. After 2015, the country will have 692 SOEs with 100% state capital; they will be organized into 44 groups, corporations with 150 subsidiaries. To achieve the main objectives of the reform program, the state has adopted the following measures - promulgate the criteria on classifying the State - owned Enterprises according to the sectors, to strengthen the capitalization of SOEs, to improve the capacity and efficiency of enterprise management, and to innovate, strengthen the State supervision management.

4. Competitive neutrality

The session was chaired by **Ms. Anne Molyneux** as representative of the Business and Industry Advisory Committee to the OECD.

In his introductory presentation **Mr. Christiansen** informed the participants that OECD was keen on engaging with non-member countries on competitive neutrality and to what extent it is relevant in their jurisdictions and invited them to engage bilaterally with the OECD on this. He also mentioned that in the beginning of 2013, OECD will decide whether and how to proceed on shared thinking on this topic. He elaborated on the methodology used in producing the OECD best practices report on Competitive Neutrality, the importance of competitive neutrality, options or the eight building blocks that are available to countries to obtain and enforce competitive neutrality. Mr. Christiansen stressed that even though very few countries have comprehensive CN frameworks in place; most jurisdictions have implemented elements of the eight building blocks and hence in effect taken steps toward Competitive Neutrality.

Mr. Lawrence Lee from Chinese Taipei talked about how competitive neutrality was enforced in his domestic economy. Between 1989 and 2008, 37 SOEs were privatized, another 17 were shut down. Now 10 SOEs remain and most are public utilities and large-scale SOEs. Chinese Taipei is engaging to promote efficient competitive neutrality between SOEs and private enterprises through the enforcement of competition regulations. As their legal framework does not regulate the way in which SOEs compete with the private sector, SOE operations are considered no different from that of private enterprises. Business laws and regulations such as Company Act and the Fair Trade Act and individual laws which regulate specific sectors such as the Electricity Act and Petroleum Administration Act are applicable to both SOEs and private sector companies in the economy. He provided the example of Chunghwa Post and how, besides mail delivery, the authorities do not restrict competition between Chunghwa Post and private sector. Profit maximization is not the only objective of SOEs, and thus their profitability is suppressed. Furthermore, SOEs are subject to a variety of regulations and policy. When there is an increase in international material prices or a financial crisis, in order to stabilize the prices of materials in the domestic market and protect consumers' rights, the SOEs may introduce special measures according to policy instruction. All SOEs comply with the Government Procurement Act. Besides, SOEs do not receive subsidies, favourable regulatory treatment, or easier access to finance. Under some circumstances, SOEs are more regulated than private enterprises. He put forward two examples of malpractices in public procurement. To provide a level playing field for both SOEs and private sector companies, Chinese Taipei faces some challenges like legal definition of SOEs, clarifying the scope of exclusive right to SOEs, setting the standard of corporate governance to SOEs, strengthening the external monitoring evaluation system,

enhancing internal check and balance system and appointing professional executive personnel system.

Mr. Ram Kumar Mishra from India spoke about mixed economy in India and the idea of a balance of SOE and private sector that is envisaged. He argued that the concept of competitive neutrality is not relevant at a country level, but is applicable in the global context. Public procurement in India is plagued by private sector practices with companies low-balling their bids and failing to deliver on their promises, which tends to stall the production cycle. This discourages SOEs from opening their procurement to private sector competition. Political and social conditions of a country determine the level of competition and competitiveness within the economy. Mr. Mishra highlighted the role of competent regulators, trade associations in propagating competitive neutrality.

Participants were unanimous that competitive neutrality is a potentially useful concept and should guide policy makers' thinking, but they also agreed that this idea is not simple to enforce and would need a strong commitment from governments. Whereas competitive neutrality may be a useful frame of mind, in reality obtaining total competitive neutrality seems utopian. The concept cannot be an end in itself: realities of the world need to be considered when neutrality is pursued, including the level of economic development to of countries and the context of their development policies. In the words of one participant, his "country is trying push forward the idea of competitive neutrality, but the concept cannot be allowed to influence the national SOE reform process". Other participants noted that in many markets the private sector may have a clear competitive advantage. One participant suggested that the extant Global Competitiveness Index should be augmented to include the 8 building blocks of competitive neutrality

5. Professionalisation of SOE boards of directors

In his opening remarks the session Chair, **Mr. Lim**, noted that boards of directors have a major role to play in steering the company and in the success of the company. Codes of governance have placed a lot more emphasis on independent directors, nomination and appointment of directors but lately that emphasis is changing towards competence. The new codes of CG in Malaysia and Singapore emphasize on competence of directors in terms of what is required, their character, integrity, courage and commitment. Training of directors and their continued development is important to keep themselves relevant as times are changing rapidly. Directors have a great accountability for strategy and for overseeing and monitoring management, and there is a need for their commitment to understand the nature of the business of the company.

Part A: Directors' training

Mr. Li Bing from China spoke about directors' training programme undertaken by SASAC. There are 117 central SOEs under the supervision of SASAC. Since 2005 42 SOEs have established standard board of directors. A responsible, well-running and balanced corporate governance structure was established by clarifying the responsibilities of shareholders' meeting, board of directors, board of supervisors and executive management. China has 3 kinds of directors on its SOE boards: external director, non-external director and employee director. Both SASAC and Chinese SOEs attach great importance to the training of directors. Chinese SOEs take different measures to improve directors' capability, such as visiting subsidiaries, attending lectures, meeting with management team, communicating with experts and consulting firms, etc. The objectives of their training program are to enhance the construction of directors' team, and make the board more standard and effective, to cultivate the culture of corporate governance, and achieve sustainable development, to increase directors' awareness of responsibility and risk

management, and make them more capable and qualified, to share the best practices on corporate governance and board operation. Towards the training program SASAC has undertaken the following measures - organizing training program together with Tsinghua University, designing individual training program for new board members, communicating with the board of SOEs quarterly and organizing business trip abroad for SOEs' directors to learn from other countries like Singapore (Temasek) and Australia. There is no Institute of Directors in China currently. The training of the SASAC-Tsinghua University program includes the following topics - board operation and corporate governance guidelines, necessary financial knowledge, investment decision-making, strategic management, audit committee and internal control and recruitment, leadership and performance assessment of managers. A specialised unit in SASAC is in charge of the training of directors in SOEs. SOEs are required to report its progress on the training of directors to SASAC in their annual reporting.

Mr. Jesus Estanislao from the Philippines provided his perspective on boards training from the experience gained in his country. Training of Directors is not an academic exercise; it is a practical undertaking which is carried out by existing directors. They adapted the long list of directors' duties and responsibilities, into a framework (the "Tricker Model") to group together those duties and responsibilities and to provide tighter coherence between them. The current model being used in the country includes 6 duties and responsibilities of corporate directors. These are strategy, policy, monitoring, accountability, ethics & social responsibility and governance culture. The Professional Directors Program takes a full week to complete. The methodology used during the training program includes actual case studies (monitoring and accountability), a balanced scorecard framework (strategy and policy) adapted into local circumstances using the Norton-Kaplan BSc strategy execution approach. The practice guidelines for strategy and policy, following the balanced scorecard framework, have been put together---and are constantly being refined and updated based on actual experience in different corporate board rooms---under our Performance Governance System. This is presented as a set of recommended practices, which can be gradually phased under the leadership of corporate boards through corporate directors into their respective corporations. The phases are: initiation, compliance, proficiency and institutionalization. Training of directors is not considered as a one-shot requirement. It has to extend to a process that is sustained until it delivers breakthrough, transformative results. The program has a holistic approach, the program has adapted the best models from around the world, and is strategy and outcome focused for sustainable performance.

Mr. Abdul Aziz Abu Bakar from Malaysia spoke about the directors training program in his country. In Malaysia, the training program is referred to as directors' development. The training program puts a lot of emphasis on board effectiveness as a team rather than individual directors. An effective board is one which is performance oriented whereas earlier the board members who were mostly bureaucrats believed in efficiency or compliance driven. The training program caters towards the mindset or what a director believes in. The training approach followed in Malaysia is again a holistic one with class room learning, case studies, peer sharing and on the job learning and coaching, keeping in mind the different levels of experience, knowledge, skills and expertise that directors bring with them to the board. They train directors in order to ensure that they maintain professional relationship via inter/intra personal communication within the board, with the stakeholders and with the senior management. The Malaysian program also includes calibrated training for different levels of directors and mentoring by experienced chairpersons. Malaysia also requires mandatory training for new directors, that director training program must be disclosed in the annual report and explains if directors have not been trained, and board effectiveness assessment.

During the open discussion, participants expressed concerns that the mindset of directors of SOEs is a challenge when offering them training. They agreed that training and development should be mandated, that boards need to understand the role of the state and their relationship with the state and boards need to be aware of different behaviours, difficult discussions and risk.

Part B: Risk management at the board level

The session Chair said in his opening remarks that risk management is a responsibility which is generally not well understood by directors, although regulators are now looking at risk management processes much more closely. Boards are responsible for risk governance and risk appetite of the company and management is responsible for developing and implementing an adequate framework and processes for internal control. And boards are equally responsible that the management fulfils its duties related to internal control.

Mr. Rana Assad Amin from Pakistan spoke about risk oversight, risk committees, risk regulations and risk intelligence maps. Risk oversight has become important because of global crises, increased regulation and governments pressurizing SOEs to improve their efficiency and effectiveness. For the board to manage risk, it was necessary to give them greater powers and autonomy, enhancing their composition and ensuring their independence. Risk committees at the board level are slowly developing, and that US SEC requires that disclosure of the board's role with regard to risk oversight in the company's annual proxy statement. In Pakistan, SOEs have a high risk appetite. For risk determination, management and mitigation, which are highly technical in nature and boards, have been relying on audit committees. But audit committees are not equipped to manage the complex nature of risk. There is a need for risk committees in Pakistan. There is currently no legal requirement for SOEs other than FIs to form a risk management committee at the board level. The central bank of Pakistan, has issued risk management guidelines for FIs as per Basel II. The draft version of the new code of corporate governance recommends formation of risk management committees in NBFIs. The responsibilities of the risk management committee at the National Bank of Pakistan include approving, reviewing and monitoring the bank's overall risk appetite, reviewing capital adequacy, reviewing stress test reports on credit, market, operational and liquidity risk, reviewing key risk exposures of the bank and advising the board on risk strategy.

Mr. Antonius Alijoyo from Indonesia talked about how risk is managed in his country. A new ministerial decree of 2011 talks about risk management, internal control and whistle blower mechanisms. The decree requires that the board must take into account risk in the decision making process and it must establish and implement an integrated corporate risk management. It also requires that risk management either through a separate unit at the board or as part of an existing board committee. Board is responsible for submitting the SOE risk profile and its mitigation through regular (quarterly) reporting to the Ministry of SOEs. From a risk management perspective, if SOEs are managed well crisis can be prevented. The main questions for a board in terms of risk management are if the company is taking the right risks, if the company is taking the right amount of risks, and if the company has the right infrastructure and processes to manage risks. The process for managing risk should include risk assessment, identification, analysis, evaluation and treatment.

Mr. Naresh Kumar Nagpal from India elaborated on the risk management system put in place at GAIL. Risk management in India is mandated by the following regulations Clause 49 of Listing Agreement of the stock exchanges and DPE guidelines on Corporate Governance. GAIL institutionalized Risk Management Framework in 2007 and its features include key risk indicators, maintenance of risk registers, designated risk officer and risk owner, and constitution

of a corporate level risk steering committee. The risk management framework is reviewed by the Audit Committee & Board. At GAIL, there are 49 risk units/registers, the total number of risks identified & captured in risk database was 1179, the total number of key risks in unit risk registers was 171 and the total number of corporate level key risks was 10. GAIL uses sophisticated risk rating criteria for its risk management, and on the basis of these criteria risks are scored.

During the open discussion, participants agreed that risk management usually focuses on financial risks but does not adequately include risks related to corruption and fraud, key staff (CEO succession) and reputation. The board is key in determining the risk appetite of the company and its management follows from there. Much of risk management is critically dependent on how the risk management frameworks are implemented. Associated with risks are opportunities and it is very important for the board to understand those risks relative to the company's objectives and weigh the opportunities of growth. When boards are made aware of risks faced, it has the responsibility to take action and for this it needs soft skills of discernment.

6. Professionalisation of the State ownership function

This session focused on external factors which contributed to the inefficiencies and distortions in running SOEs professionally or running SOEs as their private sector counterparts. The session Chair, **Mr. John Kim** of Korea, set the context for this session. There are frequently constraints imposed on SOEs either by the public or the government. The constraints placed on SOEs from the government include pricing, regulations and other demands which conflict with their functioning as commercial entities in the private sector. There are constraints imposed by the society on SOEs and these become their public obligations (often referred to as corporate social responsibility – CSR). Although the concept is itself very fuzzy and distortionary, countries have come up with interesting frameworks to implement CSR activities.

Part A: Categorising SOEs and balancing their commercial and non-commercial objectives

Mr. Young-jin Kim from Korea opened the discussions with a presentation of public institutions in Korea which have been established and financed by government to provide public services closely related to people's livelihood such as infrastructure, transportation, energy, healthcare, education, and agriculture. He described the evolution of public institutions since 1960s when they were established to aid Korea's industrialization. Public institutions require both autonomy and control for their functioning. One of the significant governance mechanisms for public institutions in Korea was the performance management evaluation system. This was established in 1983. Public institutions are benchmarked against the best global companies in their respective sectors. He talked about the different public institutions and their governance structures. To set up a fair personnel system, candidates for the executives are nominated by the Executive Nominating Committee at the board level, which mainly consisting of non-standing directors and outside experts from the private sector. He also described the evolution of the executive appointment system which was earlier the responsibility of the concerned ministries and is now the sole responsibility of the board. The current executive personnel system provides an incentive based approach to the term of directors' which can be extended by 1 yr or dismissed before the term expires based on their performance.

The existence of both commercial and non-commercial objectives may not always be contradicting and are fundamental feature of public institutions in Korea. Public institutions have both these objectives because they help in reducing social burden and in improving social integrity. If public institutions pursue non-commercial objectives voluntarily, there must be some

principles to prevent moral hazard problems. There should be consensus building and open and transparent decision-making around those non-commercial objectives, minimum interference if possible, compensation for loss in pursuing obligatory non-commercial objectives. There are many types of non-commercial objectives that Korean public institutions pursue either voluntarily or compulsorily. The typical non-commercial objectives in Korea include reinforced transparency and ethics rule, cooperation in operating macro economy, implementing government policy recommendations, promoting SME industries, stabilizing the labor market and tackling inequalities in the society etc.

Mr. Zhang from China spoke about why and how Chinese SOEs are categorized according to their objectives and provided a comparison with other countries around the world. He presented the conclusions of a study on this subject and established that there are different classes or categories of SOEs, and even in an SOE, there are different sorts of responsibilities. Some are special and aimed at public interest. He further pointed out that undertaking special obligations should be mandated by law or regulation and that the ownership policy objectives should be strategic and be composed of all SOEs' commercial responsibilities and special obligations. It was necessary to identify special obligations of SOEs, and certain scope of discussion and negotiation was necessary. The objectives of an SOE should be based on all its responsibilities, and should be implemented by setting a set of performance indicators and assessment. In China SOEs are categorized either as "SOEs with special obligations" or as "competitive SOEs". SOEs with special obligations are further divided in terms of their objectives for the long run, objectives for a certain stage of development, provision of public goods and strategic objectives (contribution to GDP, support to other industries, new sectors which needs significant seed investment, major drivers of growth). However in reality there were many challenges in categorizing SOEs including difficulty finding universal criteria for categorizing SOEs, negotiations involved in categoring SOEs (between different government agencies, SOEs) are usually a long process and these can become distorted, for an effective categorization depends on execution. The chair commented that the categorization followed in China was reasonable.

Mr. David Robinett from the World Bank spoke about managing public service obligations. The six steps to follow there included figuring out what public service obligations are, the cost of providing those obligations, how they are paid for and if these obligations are disclosed (and how), measure of delivery and incentives provided for the delivery of these obligations. It was accepted that at most times the government did not want to hear about the costs of delivery of public service obligations and would demand SOEs to provide these services irrespective of costs.

Ms. Angela E. Ignacio from the Philippines shared national experience in categorizing SOEs. 158 SOEs in the Philippines are active 7 sectors i.e. Government Financial Institutions, Social Services and Housing, Land and Water Resources, Power, Support Services, Commercial, Trade and Tourism, Transportation, Infrastructure and Communications and are categorized into 4 according to their objectives i.e. Developmental / Social, Commercial, Government Financial, Investment and Trust Institutions and Corporations with Regulatory Functions. The Philippine experience suggested that given lack of an overall ownership policy and poor regulation, there was a proliferation of SOEs without any exit strategy, agency functions were performed by SOE, SOEs remained in existence despite sufficient private sector presence, and increased government financial support. Many SOEs are burdened by non-commercial objectives are supported by the government through subsidies, equity and lending. One of the most significant recent reforms in the country has established the Governance Commission for GOCCs (GCG) which is a central advisory, monitoring, and oversight body with authority to formulate, implement and coordinate policies. Its responsibilities include carrying out a clear policy direction, ensuring that SOEs are used as financially viable tools in achieving inclusive growth and economic development and

fiscal Discipline on the part of the State in subsidizing the operations of SOEs. The GCG amongst other policies has laid down a framework and system for balancing commercial and non-commercial programs and prefers that non-commercial programs be carried out by regular government agencies, restraining SOE participation in activities adequately serviced by the private sector, and requiring SOEs to have a well-thought out feasibility studies that identify measurable objectives, target beneficiaries, a program timeframe, a clear monitoring system, and impact assessment/evaluation. The GCG is looking at a holistic approach to measuring SOE performance on the basis of criteria like social impact, internal process, stakeholders, learning & growth and finance. GCG is also looking at institutionalizing incentives for SOEs meeting their objectives.

During the open discussion a participant argued that when SOEs have mixed mandates and are provided with subsidies for their non-commercial objectives, SOEs will over state their costs to fulfil their public service obligations will help them show profits in their commercial activities. In monopoly sectors, where prices are fixed, there is creative cost accounting and it is difficult to get these issues solved while negotiating the performance compact with SOEs.

Part B: Corporate social responsibility, accountability and ethics

Mr. Jogiranjana Panigrahi from India talked about CSR in India in the context of a concept known as 3P (People, Profit and Planet). India SOEs' commitment is to operate in an economically, socially, environmentally sustainable manner while recognizing the interest of its stakeholders and their CSR commitments went beyond statutory requirements. Comprehensive guidelines on CSR for SOEs were issued in April 2010. Guidelines were brought about after wide-ranging consultations with SOEs, Administrative Ministries, as well as the Standing Conference of Public Enterprises (SCOPE) on the subject. A committee of Secretaries deliberated extensively and on their recommendations, the guidelines were approved by Minister, Heavy Industries and Public Enterprises. The guidelines were voluntary in the beginning and but are now mandatory for all SOEs. SOEs are mandated to spend a certain proportion of their profit after tax on CSR. This is mandatory on the basis of guidelines issues by DPE and may become part of Companies Law when it is amended in the near future.

CSR is now a professional management process, with a long-term strategy integrated with its corporate strategies. The long-term CSR plan is broken down into short-term and medium term plans, specifying activities to be undertaken, budgets allocated, responsibilities defined and measurable results expected. Monitoring of the CSR projects is important. In India, the Board of SOE, Administrative ministry discuss the implementation of CSR activities on a regular basis. CSR activities are to be articulated in a separate chapter in the Annual Report of the SOE. In MoU, 5 marks out of 100 are earmarked for CSR. For monitoring of CSR activities, companies are mandated to appoint a CSR sub committee headed by an independent director. CSR projects are to be evaluated by an independent external agency.

According to his presentation, SOEs had undertaken CSR initiatives exceptionally well. SOEs contributed in large measure to victims of natural disasters in India under CSR. CSR Projects cover broadly education, community health, housing, rural development, promotion of sports-culture, skill development, women empowerment, disaster management programme etc. with an objective of creating social value and assets. A CSR Hub has been created for compilation of data, advocacy, research, promotional activities on CSR. The hub organizes seminars for propagation of ideas and sharing experience on CSR initiatives. So far the total CSR expenditure incurred by 21 Maharatna and Navaratna SOEs in 2010-11 is US\$ Million 115 down from US\$ Million 160 in 2009-10.

Ms. Lijie Chen from China Mobile talked about CSR activities at her company. Ever since its establishment, China Mobile has been attaching great importance to CSR and aims at a balance between company operation and social responsibility, in order to create value for stakeholders, achieve overall, coordinated and sustainable development and grow up together in harmony with stakeholders. Some of their CSR practices are: fulfill the universal service responsibility to enable a better life with information solutions. Village Connection Project provides communications services featured by broad Network coverage, excellent quality of service and favourable prices. It promotes the Wireless City initiative, aiming at linking governance, public affairs, transportation, health care, education, and employment. China Mobile looks into the demands of the disadvantaged groups, with on-going charity projects for education promotion in the Middle and Western Regions of China, children orphaned by AIDS and children with congenital heart disease that live in poverty, etc. The company promotes the construction of a resource-conserving and environmental-friendly society via the green office and service initiatives under Green Action Plan as well as other energy-saving and environmental-friendly ICT solutions. At China Mobile there is a strong emphasis on employees and their welfare. The Company attaches a great priority to harmonious labour relationship, and to establish an excellent platform for employee development while ensuring their rights and interests. China Mobile's CSR practices have received wide recognition - since 2008, China Mobile has been selected to the Dow Jones Sustainability Index for 4 consecutive years. CSR does not mean giving away money for charity but it is based on the interest of relevant parties which does not contradict the profit motive. The motivation behind CSR at China Mobile is that CSR is part of its corporate strategy to grow in a sustainable way.

At the macro level, SASAC requires that all SOEs report in their annual report about their CSR activities, it has been found that CSR in SOEs is higher in China compared to their private sector counterparts.

Mr. Rainier B. Butalid from the Philippines addressed the issues of CSR, ethics and accountability. The Governance Act 2011 was enacted in record time in recognition of the importance of good governance. Three documents were submitted by GCG in pursuant to the Act - ownership and operations manual for GOCCs, code of CG for GoCCs and fit and proper rule. The office of the president has reviewed the documents. He elaborated on duty of care and extraordinary diligence, duty of loyalty and duty in dealing with GOCC properties and monies that has been emphasized in the documents related to the governance of GoCCs. He also elaborated on their code of CG which clearly defines CSR and SOEs' relationship with their stakeholders and suggested that their code of CG was inspired from the OECD guidelines. CSR is mandated in the Philippines by law.

During the open discussion an Indonesian participant mentioned that the existing Indonesian law mandates that SOEs allocate 2.5% of net profit towards community development programmes and he wanted to know what ethics related measures can be undertaken to prevent corporate scandals. Participants also raised concerns about jurisdictions which mandate SOEs to incur a certain percentage of their net profit towards CSR, the role of boards then becomes very important in ensuring that CSR activities are related to the core business of the SOE and are not pilfered for political patronage.

7. Future roadmap

This session was led by Chairman **John Lim**, **Mr. Waluyo** of NCGI and **Mr. Christiansen** from OECD. The session started with a brief background on what was agreed at the 6th Asia SOE Network Meeting in Seoul. The Network had agreed to establish a Core Group which would be

responsible for the contents of future Network meetings, future strategies and long term priorities, topical issues of mutual interest, identifying case studies or topics to be taken by the Network. Authorities from China, India and Korea joined the core group. A phone conference was set up for the core group members and also the Chair of the Network to discuss the contents of the agenda for the 7th Asia SOE Network meeting in April 2012. During the teleconference, the core group decided that the options for future roadmap for the Network should be discussed with participants of the Network in a brain storming session. Some of those options brought forward to ensure that tangible and substantive Corporate Governance reforms in SOEs are undertaken around the region included, more analytical work, case studies on sectors and countries, assessing the quality of governance reforms both at macro and micro level, disseminating the work of the Network to policy makers and how to go about establishing a Companies Circle (CC).

The Network Chair proposed a brainstorming to gather inputs from the participants. He stressed that the objective of the Network is to ensure that sustainable, tangible and substantive reforms take place in the region's SOEs. He noted that, so far, the Network has provided a useful platform for dialogue in terms of policy changes, areas of priorities and how each country saw its own priorities for reform. Most countries have by now put in framework, regulations and guidelines for SOEs. Going forward, the Chair said, the challenge will be to translate this into changes at the ground level – i.e. the objective of the Network should be to ensure that what has been obtained so far will produce results at the enterprise level. So the question put forward to the Network participants was - does the Network need to change in terms of its form and structure?

The idea of a Companies Circle was to add participants who are responsible for running SOEs, implementing CG reforms, and who are faced with the challenges of bringing change at the enterprise level. This would bring together SOE executives to share with their colleagues and government officials examples of successes with implementing reforms, and highlighting the challenges they have had to overcome. The CC could act as a model and learning ground for others embarking on similar reforms. The Chair wanted the Network to consider (as already agreed by many participants in the previous meeting in Seoul) if CC would be a good vehicle for making further progress. He urged participants to take up the task of and be accountable for including SOE representatives from their jurisdictions. The Chair also talked about the Core Group and the need for additional people as part of the Group who are ready to devote their energies to guiding the Network in the next phase of its life.

During the open discussion, numerous participants came forward with suggestions. One participant pointed out that before embarking on a future roadmap it was important to celebrate the success of the Network and what it has achieved since its inception. The driving forces behind the Network were the weight of SOEs in Asian economies and the importance of good governance for their success. Concrete and progressive steps have been taken in different countries in line with an evolving consensus that the discussions at the Network meetings should claim their share of credit for. This momentum should be kept up by continuing to devote energies to the Network with a focus on implementation and concrete outcomes. Participants expressed unanimous support to keep the Network running, but to adjust its methods moving forward. There was also a suggestion to use the Network to monitor progress in privatisation participating countries.

Given that regulators across the region have taken inspiration from OECD's SOE Guidelines (and the Network's own Policy Brief), one suggestion was to create a common framework for a compliance scorecard and let all jurisdictions implement this exercise at the enterprise level. This could be one way to attract SOEs to participate at the Network meetings as they would be interested in knowing their compliance scores. There was a suggestion that a more "modest"

approach might consist of benchmarking SOEs not in terms of their entire CG regime but focusing on certain areas (e.g. board nominations or risk management) There was also a word of caution from the OECD that benchmarking SOEs is a resource intensive exercise. Some delegates cautioned that there might be a need for OECD to revise the SOE Guidelines; they were told by the Secretariat that there are plans to do so in the period 2013/14.

Participants from China expressed an appreciation of the Network, mentioning that China has benefited from knowledge sharing and benchmarking itself against other Asian countries. More SOE executives in China are becoming responsible for implementing CG reform, and they might benefit from a forum enabling them to communicate with their peers around the region. In this context, CC would be a good vehicle for exchange of knowledge.

Participants from Korea aligned themselves with the consensus view that the Network should continue. They suggested that one reason why it has been difficult to attract SOEs to the Network is that they consider themselves as “under scrutiny” and therefore do not seek to be part of a Network which has predominantly attracted agencies responsible for oversight, regulation and evaluation. To secure active participation from SOEs, organising “semi autonomous” events for the CC might be needed, giving SOEs a freer hand in deciding on the agenda. Companies in Korea have expressed interest in participating in a founding event. The future Network would be primarily for enterprises, with public sector participants as additional participants, perhaps with one session dedicated to their concerns and priority topics. To get the CC started, the Korean participants suggested focusing on one sector; for example, it is not unthinkable that Korean SOEs in the energy sector would be willing to take a lead and organize such a meeting. The Korean participants indicated a potential willingness to support such an undertaking going forward.

Agreeing with the ideas of the Korean participants, the Chair further suggested that each jurisdiction identify well performing SOEs and recognize them at Network meetings by giving away awards for their CG reform efforts. Participants from India, Indonesia and Malaysia voiced support for this approach. The Network was informed of an annual awards ceremony for good CG run in Indonesia, and it was suggested that SOEs which win awards at those annual events should be invited to the Network meetings to present their experience in implementing CG reforms.

Summing up, there was a broad agreement that the Network should continue, but that the structure of future meetings should be changed in order to include more practitioners, augmented perhaps with industry bodies, investor organizations, academic institutions and other “CG practitioners”. Specific suggestions such as benchmarking of companies or CG issues, good governance awards to individual companies and sectoral focus were deferred to further discussions by the Network’s Core Group, which will review them in light of resource availability. The Korean offer to host an exploratory meeting of the Company Circle was received positively by all participants.