

## RECENT CORPORATE GOVERNANCE REFORMS IN THE FIVE AFFECTED COUNTRIES

The governments of many East Asian countries, especially of those affected countries, are now committed to reforming their corporate governance and finance systems. Various reform measures have been proposed or implemented in the areas of corporate ownership, shareholder participation and protection, transparency and disclosure, and bankruptcy procedures. These have taken the form of amending various corporate and securities laws and regulations, introducing self-regulatory codes of corporate governance, and improving the institutional framework for promoting and enforcing rules of sound corporate governance.

### 4.1 Industry Concentration

In all the five countries, the crisis brought recognition of the scale of non-performing loans and the burden of debt facing companies and in particular conglomerates. All the countries introduced restructuring programs that involved closing unprofitable businesses and selling off non-core activities so as to lessen the burden of debt. It is notable that after the crisis, the Korean government ordered *chaebols* to concentrate on core businesses and streamline excessive diversification, abolish their group headquarters, increase the managerial independence of member companies, and stop such practices as providing loan guarantees and cross-subsidizing loss-making units. The 30 largest *chaebols* were ordered to reduce their debt-equity ratio of 4.1 by June 1998 to a maximum of 2.0 by the end of 1999. However, this has had limited success so far due to the lack of foreign buyers and the fact that many domestic companies themselves were struggling to raise their own finance. Debt restructuring has also proven to be slow.

## 4.2 Corporate Ownership

Some affected countries proposed or introduced measures involving relaxing or imposing restrictions on shareholdings by specific groups, aimed at achieving a more balanced ownership structure. In Malaysia, the Securities Commission announced in February 1998 a revision of the regulations governing the distribution of shareholdings of companies seeking listing on the KLSE. Companies seeking main board listing are required to ensure that at least 25 percent of shares are held by a minimum number of dispersed public shareholders holding not less than 1,000 shares each. The minimum number is 750 or 1,000, depending on whether a company has a paid-up capital of less or more than Malaysian ringgit (RM) 100 million. In May 1998, Korea eliminated the ceiling on foreign equity ownership and liberalized hostile takeovers by foreigners. In Indonesia, the Capital Market Supervisory Agency has allowed the listed companies to offer additional equity directly to the public, not limited to the existing shareholders. Companies are allowed to buy back up to 10 percent of their shares.

## 4.3 Shareholder Participation and Protection

Current initiatives or proposed reforms in the area of shareholder participation and protection have aimed mainly at strengthening the system of the board of directors, improving the role of AGMs, and strengthening minority shareholder legal rights and protections. These measures include (i) requiring the listed companies to elect outside directors and set up special committees with participation by outside directors in order to determine matters relating to auditing, remuneration and nomination; (ii) delineating duties and responsibilities of directors; (iii) limiting voting rights of directors in relation to connected transactions; (iv) lowering the requirements for shareholders to participate in corporate decision making; and (v) improving access by minority shareholders to legal means such as class suits.

In Korea, the KSE regulations on listing requirements were amended in February 1998 and the listed corporations were obliged to elect outside independent directors up to at least a quarter of the board members. From April 1998, all the listed corporations and those belonging to the 30 top business groups and subject to external auditing are obliged to form a nomination committee for selecting an independent

auditing firm. Lower minimum ownership levels are now required in order to file derivative suits (reduced from 1.0 to 0.01 percent), review financial data (reduced from 3.0 to 0.5 percent), and ask for the replacement of directors (reduced from 1.0 to 0.25 percent). Class action suits have been introduced. The shareholder proposal right, introduced in April 1997, can be exercised by a shareholder holding a minimum of 1.0 percent (0.5 percent for firms with equity capital of Korean won 100 billion or above) of total voting shares. Controlling shareholders are urged to register formally as directors, thus making them less shielded against liability claims by other shareholders. The abolition of the shadow-voting regulations for financial institutions in September 1998 provides them with greater incentives to monitor and participate in corporate governance. Proxy voting is recognized, cumulative voting is allowed and the fiduciary duties of directors have been introduced.

In Malaysia, a self-regulatory Code of Corporate Governance was recommended by the *Finance Committee Report on Corporate Governance* in early 1999. The Code requires that one third of board members should be made up of independent directors and recommends that nomination and remuneration committees, comprising wholly or mainly non-executive directors, be set up to select directors and determine their remuneration through a formal and transparent process. The Code sets out an additional function for the audit committee, which is to consider and investigate any matter that raises questions about management integrity, possible conflicts of interest or abuses by a significant or controlling shareholder. The Code further recommends that if the board fails to take any action on the findings of the audit committee, the directors of the audit committee should be required under the listing rules of the KLSE to report the matter directly to the KLSE. The *Finance Committee Report on Corporate Governance* also recommends the codification of restrictions on voting rights of controlling shareholders in related or connected party transactions and the fiduciary duties of directors in the Companies Act. It calls for strengthening the position of nominee directors and voting by mails, among other changes. In March 1999 the KLSE imposed restrictions on the number of directorships in order to enhance the level of corporate governance exercised by directors of the listed companies in undertaking their duties. Directors are not allowed to hold more than 25 directorships in PLCs and more than 15 directorships in non-PLCs. These of course are still high numbers.

In Thailand, a new rule set by the Stock Exchange of Thailand (SET) requires that the existing listed companies establish audit

committees as a mandatory qualification. A two-tier board structure consisting of the main (or supervisory) board and the executive board is also being considered as a listing requirement. The government is drafting a proposal to amend the provisions for related and connected transactions of directors in the Public Company Act 1992. The proposal also clearly delineates the duty of care and loyalty and fiduciary responsibilities for directors of the publicly listed companies. The SET approved a process for determining if listed company executives who have acted inappropriately should be placed on a blacklist that disqualifies an executive from holding a managerial or board position in any listed company or any company seeking public listing. Thailand's SEC is looking at the possibility of bringing in the class action lawsuit so as to strengthen legal protection for minority shareholders. The Public Company Act of 1992 did not require public companies to use the cumulative voting procedure. The proposed amendment of the Act includes recommendations to require that all public companies use cumulative voting and ensure that the board of directors consists of representatives from all groups of shareholders.

In Indonesia, the Jakarta Stock Exchange has proposed changes in its listing requirements to strengthen corporate governance of the listed companies, with the inclusion of independent commissioners and a board committee to supervise the audit function.

#### **4.4 Transparency and Disclosure**

To promote greater transparency in the corporate sector, many countries introduced changes in accounting and auditing standards, financial reporting systems and disclosure requirements. In Korea, legal changes have been made so that domestic accounting practices conform to international standards. Group companies are required to compile consolidated financial statements beginning 1999. In 1998, the Financial Supervisory Commission (FSC) set new accounting and auditing rules in line with internationally accepted standards to enhance the reliability of the financial statements of corporations. Other areas of the reform include: (i) the revision of financial accounting standards that are primary sources of the Korean Generally Accepted Accounting Principles; (ii) the establishment of accounting standards for financial institutions; and (iii) the establishment of accounting standards for "combined" financial statements for *chaebols*. Under the new rules, firms must

recognise any gain or loss arising from currency transactions in current income statements, rather than optionally hold them off as deferred charges or credits. The revised standards also require that when the contractual terms of impaired loans are modified, both the creditors and debtors must adjust the carrying amount of the impaired loans to the present values reflecting the modified terms. For investments in the affiliated companies, the new rules require the adoption of market value methods instead of allowing a choice between the cost and market value methods. The revised standards also include disclosure requirements for business segments. It is stipulated that when a listed company decides an equity investment or a payment guarantee for another company amounting to at least 10 percent of its own capital stock, this decision has to be disclosed within one day. In addition, the listed companies are required to report the details of transactions with or for controlling shareholders within one day. Financial contracts for derivatives now must be reported as assets or liabilities in the balance sheet at fair values.

In Thailand, financial information from listed companies will soon be required to conform to the International Accounting Standards. The SET already required that listed companies' quarterly reports be directly comparable to annual statements. In Malaysia, the newly amended Securities Industry Act, effective from 1 November 1998, stipulates that securities accounts can be opened only in the name of the beneficial owners of deposited securities or in the name of an authorized nominee. KLSE also enhanced the disclosure requirements for PLCs on matters relating to mergers and takeovers. It amended listing requirements to support the new takeover code of the Securities Commission by extending the requirements of the new takeover code to directors and officers of listed companies, at the same time prescribing standards of disclosure for companies involved in takeovers. These amendments promote enhanced disclosure by the listed companies in terms of clarity, consistency, and quality of information and timeliness of announcements to shareholders and investors. Such enhanced disclosure serves to protect the interest of shareholders, particularly minority shareholders, which would be better positioned to evaluate a takeover offer. In March 1999, the KLSE announced the requirement on quarterly reporting of financial statements by PLCs. Quarterly reports are required to be filed within two months from the end of every financial quarter. In addition to the quarterly reports, companies are also required to issue their audited annual reports, within four months from the end of the financial year. To assist the public in making informed judgment and to

better enhance transparency of the Exchange, the KLSE has broadened the range of daily information it disseminates to the public on all listed companies starting from September 1998. In Indonesia, disclosure requirements have been tightened. In January 1998, the government required that every listed company name a Corporate Secretary responsible for corporate disclosure.

#### **4.5 Reforms in Bankruptcy Procedures**

Reforms in bankruptcy procedures are required to strengthen the role of creditors in disciplining companies and managers, to protect creditors' rights and to facilitate the process of corporate debt restructuring. Thailand introduced a new Bankruptcy Act Amendment in March 1999. The Amendment aims to prevent a company from going into bankruptcy because of temporary liquidity problems. At the same, it eliminates loopholes that may prolong the proceedings and put creditors at a disadvantageous position. In particular, it introduced reorganization provisions, the Framework for Corporate Debt Restructuring (the so called "Bangkok Rules"), to the Bankruptcy Act of 1940. This provided for court supervised formal restructuring along the lines of Chapter 11 of the US Bankruptcy Code. The government also amended the Foreclosure Act to reduce delays in foreclosure proceedings.

In Indonesia, a new revised bankruptcy law together with a special commercial court became effective in August 1998. Important changes in the framework, setting it apart from earlier practices, include (i) more efficient and transparent procedural rules in bankruptcy proceedings; (ii) provisions allowing for the appointment of receivers and administrators from the private sector to administer the estate of the debtors; (iii) greater protection of the debtors' assets, including protection against insiders and fraudulent transactions; (iv) limitations on the ability of secured creditors to foreclose on collateral during the proceedings, thus making reorganizations more likely; and (v) acceleration of out-of-court settlements with the consent of only 50 percent of unsecured creditors representing no less than two thirds of outstanding claims.

In Malaysia, to address the need for debt rehabilitation, the government set up the Corporate Debt Restructuring Committee (CDRC). The CDRC aims to facilitate voluntary corporate debt restructuring by coordinating voluntary negotiations and workouts between creditors and corporate debtors. The CDRC intends to minimize losses to creditors,

shareholders and other stakeholders, preserve viable businesses and implement a comprehensive framework for debt restructuring. This is a variant of the London Approach.

In February 1998 Korea simplified its legal procedures pertaining to corporate rehabilitation and bankruptcy filings, so as to expedite rulings on the exit of non-viable firms and ensure better representation of creditor banks in the resolution process for the court receivership or court-supervised composition. The improved procedures reduced barriers to expeditious workouts between creditor banks and corporations with troubled debts. The new law requires that the parties agree on a final reorganization plan within one year from the date of the court order placing a company in receivership or face immediate liquidation.

Although the progress so far is encouraging, corporate governance reforms in the five affected countries will be a long drawn-out process. In some countries the scope of corporate governance reforms is still relatively limited and needs to be widened. In the other countries, although the reform proposals have been comprehensive, the implementation of these proposals needs to be expedited.

Recent and proposed reforms in corporate governance in the five affected countries are summarized in Table 11.

**Table 11**  
**Recent and Proposed Reforms in Corporate Governance\***

	Indonesia	Korea	Malaysia	Philippines	Thailand
Ownership Structure	<ul style="list-style-type: none"> <li>• Allowing new shares to be directly offered to the public</li> <li>• Allowing listed companies to buy-back up to 10% of their shares</li> </ul>	<ul style="list-style-type: none"> <li>• Eliminating ceilings on equity ownership by foreigners</li> <li>• Allowing hostile takeovers by foreigners</li> <li>• Curbing indirect cross ownership</li> </ul>	<ul style="list-style-type: none"> <li>• Raising minimum requirements for shareholdings by the dispersed public of companies seeking KLSE listing</li> </ul>		
Shareholder Control and Protections		<ul style="list-style-type: none"> <li>• Requiring listed companies to appoint outside directors</li> <li>• Establishing subcommittees in boards of directors</li> <li>• Lowering minimum ownership requirements to file derivative suits, to review financial data, and to ask for the replacement of directors</li> <li>• Introducing class action suits</li> <li>• Requiring the registration of controlling shareholders as directors</li> <li>• Introducing an intensive voting system that allows minority shareholders to designate board members</li> <li>• Allowing the exercise of proposal right by shareholders with a holding at, or exceeding 1% of total voting shares</li> </ul>	<ul style="list-style-type: none"> <li>• Proposing the Malaysian Code on Corporate Governance</li> <li>• Proposing an institutional shareholder watchdog committee to monitor and combat abuses by company insiders against minority shareholders</li> <li>• Restricting the number of directorships that a director can accept</li> <li>• Amending provisions in the Companies Act, particularly on the acquisition/disposal of properties by directors, and penalties to insider trading</li> </ul>		<ul style="list-style-type: none"> <li>• Removing minimum shareholding requirements for minority shareholders to request the board of directors to call an extraordinary general meeting</li> <li>• Requiring more than a quarter of board members to be independent directors</li> <li>• Requiring all listed companies to adopt cumulative voting</li> <li>• Introducing class action suits</li> </ul>

	<ul style="list-style-type: none"> <li>Eliminating shadow-voting regulations for institutional investors</li> <li>Recognizing proxy voting and allowing cumulative voting</li> <li>Introducing fiduciary duties of directors</li> </ul>	<ul style="list-style-type: none"> <li>KLSE tightening trading suspension guidelines</li> </ul>	<ul style="list-style-type: none"> <li>Amending provisions related to related and connected transactions of directors in the Public Company Act of 1992</li> <li>Delineating duty of care and loyalty and fiduciary responsibility for directors of listed companies</li> <li>Barring any executive from holding any managerial or board position in any PLC if found acting inappropriately</li> </ul>	<ul style="list-style-type: none"> <li>Amending provisions related to related and connected transactions of directors in the Public Company Act of 1992</li> <li>Delineating duty of care and loyalty and fiduciary responsibility for directors of listed companies</li> <li>Barring any executive from holding any managerial or board position in any PLC if found acting inappropriately</li> </ul>
<p>Transparency and Disclosure</p>	<ul style="list-style-type: none"> <li>Strengthening audit function of independent commissioners and the board committee</li> <li>Requiring the listed companies to appoint a corporate secretary responsible for corporate disclosure</li> </ul>	<ul style="list-style-type: none"> <li>Replacing the statutory auditor system with an independent audit committee system</li> <li>Conforming local accounting practices with international standards</li> <li>Introducing a compliance officer system</li> <li>Requiring group companies to compile consolidated financial statements</li> <li>Revising accounting standards for financial institutions and <i>chaebols</i></li> </ul>	<ul style="list-style-type: none"> <li>Requiring the setting up of an audit committee in the board with the majority members being non-executive directors</li> <li>Amending the Securities Industry Act and requiring that securities accounts be opened only in names of beneficial owners or authorized nominees</li> </ul>	<ul style="list-style-type: none"> <li>Activating regulatory measures to expand disclosure requirements on banks' position</li> <li>Requiring the establishment of audit subcommittees in boards in all listed companies</li> <li>Aligning local accounting practices with international standards</li> <li>Requiring quarterly reports of the listed companies to be comparable to annual statements</li> </ul>

\* This table does not cover reforms introduced or proposed after the middle of 1999.

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	Indonesia	Korea	Malaysia	Philippines	Thailand
Bankruptcy and Foreclosure Procedures	<ul style="list-style-type: none"> <li>• Amending the Bankruptcy Law</li> <li>• Setting up Special Commercial Courts</li> <li>• Drafting a new Secured Transactions Law</li> </ul>	<ul style="list-style-type: none"> <li>• Requiring investment trust firms to provide reports on investment and trust assets to their investors</li> <li>• Strengthening the reporting requirements for transactions by controlling shareholders</li> </ul>	<ul style="list-style-type: none"> <li>• Issuing "Practice Notes to the Listing Requirements" to improve content, consistency and frequency of corporate disclosure</li> <li>• Amending the listing requirements to support the new Takeover Code of the Securities Commission</li> <li>• Requiring quarterly reporting of financial statements</li> <li>• Amending the Companies Act, requiring shareholders with substantial holdings to disclose their holdings</li> <li>• Introducing new accounting and auditing rules in line with international standards</li> </ul>	<ul style="list-style-type: none"> <li>• Adopting new rules and procedures for SEC-administered processes for suspension of payments</li> </ul>	<ul style="list-style-type: none"> <li>• Amending the Bankruptcy Act to add reorganization provisions</li> <li>• Establishing the Bankruptcy Court to adjudicate both liquidations proceedings and formal reorganization proceedings</li> <li>• Amending the Foreclosure Act to hasten foreclosure proceedings</li> </ul>
Bankruptcy and Foreclosure Procedures	<ul style="list-style-type: none"> <li>• Amending the Bankruptcy Law</li> <li>• Setting up Special Commercial Courts</li> <li>• Drafting a new Secured Transactions Law</li> </ul>	<ul style="list-style-type: none"> <li>• Overhauling bankruptcy procedures, including: <ul style="list-style-type: none"> <li>• Shortening the reorganization planning period</li> <li>• Introducing new rules for court receivership</li> <li>• Requiring the setting up of management committees comprising experts in the legal, accounting and economics professions for expeditious proceeding in the cases of court receivership</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>• Introducing amendments to Section 176 of the Companies Act to facilitate market-based debt restructuring</li> </ul>	<ul style="list-style-type: none"> <li>• Adopting new rules and procedures for SEC-administered processes for suspension of payments</li> </ul>	<ul style="list-style-type: none"> <li>• Amending the Bankruptcy Act to add reorganization provisions</li> <li>• Establishing the Bankruptcy Court to adjudicate both liquidations proceedings and formal reorganization proceedings</li> <li>• Amending the Foreclosure Act to hasten foreclosure proceedings</li> </ul>

	<ul style="list-style-type: none"> <li>• Allowing creditors to revoke court receivership</li> <li>• Amending the Composition Act to narrow the eligibility to apply for court-supervised composition to prevent abuses by corporate insiders</li> </ul>	<ul style="list-style-type: none"> <li>• Voluntary restructuring, e.g., abolishing informal group, selling non-core businesses, reducing debt-equity ratios</li> <li>• Involuntary exit or withdrawal of creditor support</li> <li>• Out-of-court workouts for debt-rescheduling, interest reductions, write-offs and conversion of debt into equity</li> <li>• Preventing unfair intra-group transactions</li> <li>• Introducing the Code of Best Practices of Corporate Governance</li> <li>• Eliminating tax-related constraints</li> </ul>	<ul style="list-style-type: none"> <li>• Setting up CDRAC to assist in voluntary debt restructuring</li> <li>• Restructuring via the national asset management corporation, Danaharta</li> <li>• Court-supervised restructuring under Section 176 of the Companies Act</li> <li>• Amending public listing requirements related to mergers and takeover</li> <li>• Modernizing Corporate Law for greater accountability, transparency and higher standards of corporate governance</li> </ul>	<ul style="list-style-type: none"> <li>• Internal business restructuring through cost cutting strategies</li> <li>• Acquisition and takeover by investors in capital market</li> <li>• Application for legal protection to conduct reorganization, liquidation, payment suspension to creditors</li> </ul>	<ul style="list-style-type: none"> <li>• Introducing the Secured Transaction Law</li> <li>• Establishing the CDRAC to assist in voluntary debt restructuring process</li> </ul>
<p>Corporate and Debt Restructuring</p> <ul style="list-style-type: none"> <li>• Forming INDRAC to provide domestic and foreign creditors involved in restructuring with foreign exchange rate risk protection</li> <li>• Forming Jakarta initiative to facilitate voluntary out-of-court restructuring</li> <li>• Internal business restructuring</li> <li>• Eliminating obstacles on debt-to-equity conversion</li> <li>• Eliminating tax and regulatory obstacles for mergers, debt-to-equity conversions and for other corporate restructuring schemes</li> </ul>					

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	Indonesia	Korea	Malaysia	Philippines	Thailand
	<ul style="list-style-type: none"> <li>Exploring the possibility of a corporate restructuring law that would create legislations similar to the "Chapter 11" statute of the US Bankruptcy Code</li> </ul>	<ul style="list-style-type: none"> <li>Strengthening the prudential regulations of asset management</li> <li>Strengthening the supervisory functions on asset management</li> <li>Expanding the powers of the publicly-owned Korean Asset Management Corporation to facilitate bank restructuring</li> </ul>	<ul style="list-style-type: none"> <li>Setting up an asset management company, Danaharta, to reduce NPL levels</li> <li>Setting up Danamodal to recapitalize banking institutions to restore their lending capacity</li> <li>Reducing statutory reserve ratio of eligible liabilities to improve liquidity system</li> <li>Establishing loan rehabilitation units to ensure intensive management of problem loans</li> </ul>		
Banking Restructuring	<ul style="list-style-type: none"> <li>Setting up IBRA to assist problem banks and setting up an asset management unit to manage problem loans</li> <li>Drafting a new Central Banking Law to provide Bank Indonesia with enhanced autonomy</li> </ul>				<ul style="list-style-type: none"> <li>Setting up banks' own asset management companies</li> <li>Taking "haircuts" for banks</li> <li>Entering into out-of-court agreements for a restructuring plan as preferred by banks</li> <li>Consolidating banks and their subsidiaries for better regulations of net foreign exchange currency positions</li> <li>Reducing statutory reserve requirements on banks and raising liquidity reserves</li> </ul>