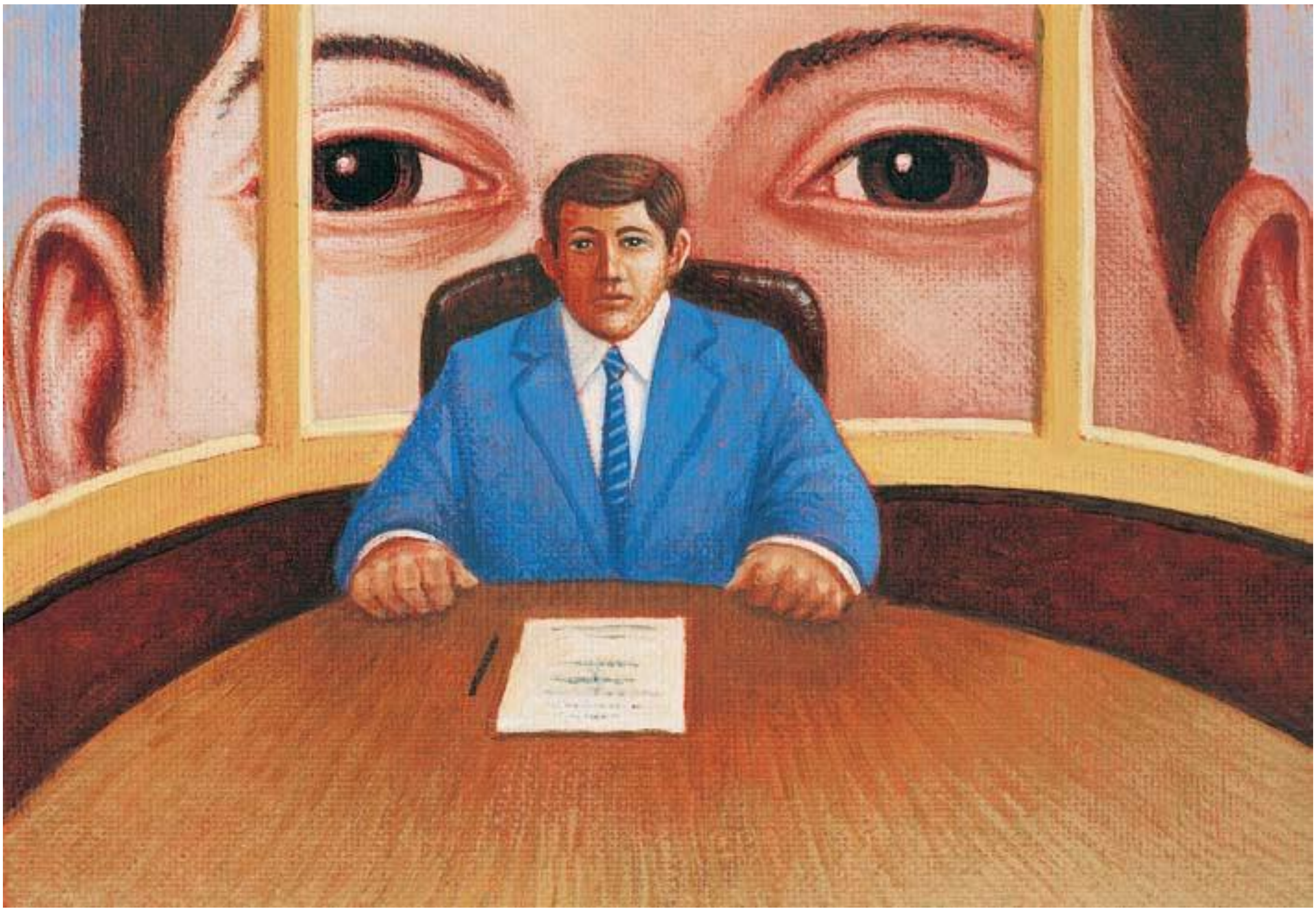

Voluntary Goodwill

Lacking of institutional investors, Asian companies are sometimes less formal with corporate governance guidelines and practice. Good corporate governance is nevertheless significant for companies in attracting investment. by **Havier Dong**

After Enron, we have seen further emphasis on the significance of corporate governance throughout academia, businesses, laws and regulations. New theories and ideas have been developed to improve corporate governance. Such development can be seen in wide aspects of corporate governance, especially in the rules and responsibilities of the board, corporate liabilities, auditing, compensation and enforcement. Corporate governance can be mainly divided into several segments. These segments basically relate to the owners, shareholders (those with voting rights), Board of Directors (BOD), Executives (senior managers), creditors, suppliers and customers. The interests of these stakeholders contribute to the interest of the corporation.

The US experience is costly and precious, not to mention that they have a much developed system. Compared to US counterparts, Asian companies are less developed, with a unique characteristic: its controlling shareholder. In Asia, it is quite often the case that the controlling shareholder of the company is a single entity, in the form of a powerful individual, family, or the state. Management and business practices are also influenced by Asian values. In order to adopt good corporate governance practices, it is important that we understand this unique character and the impact it carries to corporate governance in Asian companies and develop specific policies against specific problems.

Corporate Governance

Corporate governance is both internal and external, it is also associated with the culture of the company. In the context of corporate governance, the interests of the company's stakeholders are being taken care of while good corporate governance also plays a role in social-economic development. Poor corporate governance, on the other hand may result in lower share valuation and restricted access to equity finance. In theory, good corporate governance brings several benefits to the growth of the corporation:

- Good corporate governance increases access to financing, therefore reduce the cost of capital and results in higher valuation;
- Good corporate governance can improve operational performance;
- Good corporate governance improves the relationship with stakeholders, thus provides an improved business environment.

Shareholders

Among all stakeholders of the corporation, shareholders are most important, since they have decision-making rights. However, where the major controlling shareholder has an overwhelming voice on decision-making, abusive situations may occur in ignoring or rejecting the minority shareholders' rights. For example, a simple abusive activity is that the owner of the company extracts funds for its own interest. For listed companies, such abusive activity is monitored by various external vehicles such as the Company Law, Accounting standards, Securities regulations, etc. that would result in serious consequences (including de-listing). On that note, there is also argument that such announcement and execution of punishment could lead to a drastic drop in share price, while ultimately damages the minority shareholder's interest of which the regulators were supposed to protect. Moreover, there are many other complex ways to bypass minority shareholders.

In the case of pyramid control , where the controlling shareholder owns smaller proportion of shares but in fact have greater voting rights, they do not need to hold enough shares to effectively control a company. And with the involvement of allied shareholders and passive votes, the controlling shareholder rarely needs 50% of the votes to prevent unwanted takeovers, appoint directors, and determine the outcome of a vote. In some cases, such control can be done with as low as 30% of the votes. Pyramids structure has the benefit of bringing a group of companies together under a well-known brand, but the separation of ownership and control has a potential conflict between dominating shareholder and minority shareholder, where they can take actions that benefit themselves at the expense of minority shareholders. These actions include tunnelling, of which the company's insiders can take out assets, as mentioned earlier. The insiders of the company also enjoy privileged information, which allows them to achieve personal gains on purchasing additional shares before share prices go up (for example, before the announcement of a new project or a new deal, factors that are likely to push up share price). In the pyramid structure, it is also possible for the controlling shareholder to grant contracts on favourable terms to the company that controlling shareholders effectively control. Such assets transfer damages not only the interest of minority shareholders, but also the interest of long-term creditors.

To contain such abuse, internal corporate governance framework and guidelines need to be set up and to imply tight control and scrutiny, shareholders' approval should be acquired and appraisal rights should be obtained. In some legal systems, shareholders are allowed to act collectively, such empowerment allows minority shareholders to better protect their interests. Regulators play an important part in monitoring corporate governance for listed companies. They are required to provide information on corporate governance structure. Some accounting codes require companies to disclose its related parties, to prevent controlling shareholders or BODs acting on their own interest. There is also an increasing demand on reporting and disclosing requirements of company information, including non-financial information, which used to be voluntary. Nevertheless, both transparency and accountability are the key criterias, and the foundation of good corporate governance.

The responsibility of the BODs is another important part of corporate governance. In some cases, members of the BOD are family members, and since the controlling shareholder have the power of appointing directors, it is on their best interest to have someone closer, and these new directors may feel an obligation to the controlling shareholder and therefore take sides, while lose their independence. Good corporate governance ensures the composition, independence, and professionalism of BODs, the use of adequate number of independent and non-executive Board members, and prompts the BOD to maximize value and protect the interest of all shareholders and stakeholders.

ABOUT THE AUTHOR

Havier is a graduate of Northumbria University of the UK. He can be reached at *havier.dong@uhy-my.com*