Table of Contents

PREFACE

EXECUTIVE SUMMARY

I. INTRODUCTION 1

- A. The Background 1
- B. The Objectives 3
- C. Expected Results 3
- D. Dissemination of the Results 5

II. RESEARCH METHODS 7

- A. Surveyed Companies 7
- B. Research Instrument 7
- C. Data Collection 8
- D. Evaluation Methods 8
- E. Research Members 10

III. EMPIRICAL RESULTS 11

- A. Rights of Shareholders 11
  - A.1. Rights Defined 12
  - A.2. Rights Disclosed 15
  - A.3. Takeover Rules 21
  - A.4. Penalty 23
- B. Equitable treatment of Shareholders 24
  - B.1. Voting Rights For Share 24
  - B.2. Shareholders Conflict 26
  - B.3. Proxy Voting/ AGM Procedures 29
  - B.4. Penalty 31
- C. Role of Stakeholders 32
  - C.1. Rights Recognition 33
- D. Disclosure and Transparency 37
  - D.1. Ownership Structure 39
  - D.2. Annual Report 40

D.3. Financial Statements ………………………………………… 42
D.4. Access To Information …………………………………… 43
D.5. Comparison to 2004 48
E. Responsibility of the Board 48
E.1. Monitoring/Control 49
E.2. Board Performance Evaluation 60
E.3. Conflict Of Interest 61
E. 4. Board Composition... 67
E.5. Communication and Bonus 69
IV. ANALYSES 71
A. Corporate Governance Performance.. 71
A.1. Overall Performance 71
A.2. Performance Comparison for Sixty Leading Companies…… 72
B. Corporate Governance and Economic Performance ………........... 74
C. Industry Analysis 75
D. IDEA Net Comparison 80
V. CONCLUSIONS AND RECOMMENDATIONS 82
A. Conclusions 82
a. Rights of Shareholders 82
b. Equitable Treatment of Shareholders 83
c.. Role of Stakeholders 83
d. Disclosure and Transparency 84
e. Responsibility of Board 85
f. Overall Corporate Governance Performance 86
B. Recommendations 87
Lists of Surveyed Indonesian Listed Companies

EXECUTIVE SUMMARY

The second study aimed to provide evidence on corporate governance practices of listed firms in the Jakarta Stock Exchange. It assessed the performance of corporate governance practices of Indonesian publicly listed companies by using a unique method of research that relied on publicly available information, such as company's annual report, financial report, notice to call AGM, reports on results of AGM, corporate laws, regulations, etc. The instrument of the assessment was developed based on international standard practices promulgated by the Organization for Economic Development and Cooperation (OECD), consisting of five (5) principles, namely rights of shareholders, equitable treatment of shareholders, role of stakeholders, disclosure and transparency, and responsibilities of the board. It was the IOD in Thailand that first developed the instrument before it was subsequently adopted for use by five member countries of the Institute for Directorship of East Asia (IDEA.Net), namely Thailand, China, Hong Kong, Indonesia, and the Philippines. It is hoped that the results of the study can be used to improve corporate governance practices in Indonesia and the surrounding regions as well.

We found that in general, publicly-listed companies implemented corporate governance practices simply to comply with the laws and regulations, as shown by the overall mean score that reached 61.26 per cent (see Table 1 below for detail). Therefore, the implementation of best practices that are in accord with international standards still remains a challenge for all surveyed companies.

Table 1.
Corporate Governance Performance
by Individual OECD Principles

OECD Principles	Mean Score (%)
Rights of Shareholders	51.23
Equitable Treatment of Shareholders	83.02
Role of Stakeholders	58.76
Disclosure and Transparency	66.64
Responsibilities of the Board	52.36
Overall Mean Score	61.26

Some companies, however, especially those which are highly regulated, such as banks and state-owned enterprises (SOEs), and other companies pioneering corporate governance, have shown their commitment to meet international standard practices, as shown in Table 2 below.

Tabel 2.
Corporate Governance Performance
by SOEs, Bank, and Overall

Category	Mean Score of Corporate Governance Performance (%)	
	Current Study (2005)	Previous Study (2004)
SOEs	74.63	76.38
Banking	70.70	74.91
Overall	61.26	67.29

When comparing corporate governance score between the two consecutive studies (2005 and 2004), we can see that there is a slight decrease in the above three categories. Two major factors that distinguished the present study from the previous one are as follows:

1. The use of a more stringent instrument.
2. The study involved low-performance companies.

However, when comparing the two studies by the same subject companies (60 companies for overall, 12 companies for SOEs, and 9 companies for banks), we can see that there is improvement in the performance, as indicated in the following table.

Table 3.
Performance Comparison by the same subject companies

Year of Study	Mean Score of Corporate Governance Performance (per cent)		
	Overall N = 60	Banks N = 9	SOEs N = 12
2005	69.50	78.00	76.51
2004	67.29	74.91	76.38

To a certain extent, the improvement can be attributed to the efforts conducted by the IICD through the dissemination of the results of the first study, workshops on international corporate governance standards, and other programs for professional directors.

The gap in corporate governance performance between top quartile and bottom quartile firms was quite high. In terms of the overall mean score, the top quartile performance reached 71.52 per cent, while the bottom one was only 52.71 per cent. The most challenging tasks facing companies, regulatory bodies, and other governance-related institutions are to make the bottom quartile companies, as well as those companies with corporate governance performance between the top and the bottom quartile, more committed in implementing good corporate governance practices. It should be noted, however, that this does not mean that the top quartile firms no longer need to pay a particular attention to good corporate governance practices. In conclusion, we suggest that good corporate governance practices could have a significant correlation with a company's economic performance.

I. INTRODUCTION

A. The Background

It had been recognized by most analysts that the economic crisis that hit the nation in 1997 was greatly caused by poor corporate governance practices among publicly owned companies, including SOEs. During this period, the stock exchange markets collapsed, credit ratings of most Indonesian corporations plummeted, and investors lost their trust in such companies. Research findings showed that investors are actually willing to pay a premium for shares of well-managed companies. Good corporate governance is also viewed as an important factor by bondholders. Therefore, good corporate governance does matter and can contribute a significant value for companies and the national economy as a whole.

In spite of the increasing importance of good corporate governance practices in the global economy as well as in Indonesia, many Indonesian companies are still far behind other countries in the implementation of good corporate governance practices that are in accord with the principles set by both the National Committee on Corporate Governance and the international standards as well. The corporate governance practices in Indonesia are relatively deficient in terms of disclosure and transparencies, professionalism in board practices, compliances with the laws and regulations, etc. The existence of the laws and regulations does not guarantee the directors' compliance since the law enforcement in Indonesia still remains the biggest challenge.

The efforts to strengthen good corporate governance practices in terms of the right of shareholders, the equitable treatment of shareholders, the role of stakeholders, disclosure and transparency, and the board responsibility are still very much needed. Adopting the international standards that fit local characteristics and legal traditions are necessary to create values for

Indonesian companies and to strengthen their competitive power in the global world. In addition, optimizing the legal and regulatory framework is important.

As part of its role in advocating good practices of corporate governance and directorship in Indonesia, the IICD (Indonesian Institute for Corporate Directorship) had initiated a study on the corporate governance scorecard involving 61 leading Indonesian public-listed companies. The comprehensive assessment was conducted in 2005. Based on the results of the study, the state of corporate governance practices in 61 companies can be summarized as follows:

1. The corporate governance practices did not provide appropriate protection and facilities to shareholders in exercising their rights
2. The controlling shareholders were very powerful in the determination of the board members (board of commissioners and board of directors) because cross-shareholdings and pyramidal ownership structure were still a common practice
3. To a certain extent, as required by the laws and rules and regulations, the surveyed companies appeared to show their commitment to disclosure and transparency. From the perspective of investors, however, disclosure and transparency with respect to the ownership structure, the beneficial ownership, the corporate structure, the determination of board compensation, and the use of analysts and the press still need to be improved for the purpose of better public understanding.
4. The role of independent commissioners was not clear yet and the competence of board members in exercising their duties effectively were still inadequate at present and in the future.
5. The role of corporate governance in Indonesia seemed to be promising for sustainability of market performance. We found that high corporate governance scorecard led to high Tobin's Q.

B. The Objectives

The main objectives of the Indonesian Corporate Governance Scorecard were as follows:

1. To provide an analytical tool for improving the implementation of good corporate governance principles
2. To help the regulatory bodies strengthen corporate governance practices and accountability
3. To provide information for investors and creditors in assessing corporate governance practices of Indonesian public-listed companies
4. To benchmark the Indonesian corporate governance practices against similar practices in other Asian countries, especially the IDEA.NET member countries (Singapore – Malaysia - The Philippines - Hong Kong – Thailand – Vietnam - South Korea - China - Taiwan – Indonesia). It is hoped that this benchmark can be used to continuously improve the implementation of corporate governance practices in Indonesia.

C. Expected Results

The second comprehensive study of corporate governance scorecard is expected to give the following impacts on the corporate governance implementation:

1. Closer cooperation between IICD and the Association of Indonesian Public Listed Companies (AEI-Asosiasi Emiten Indonesia) will increase the chances for the acceptance of good corporate governance practices by Indonesian publicly-listed companies.

2. The results of the study will influence the market perception, an important variable needed to improve good corporate governance practices in Indonesia.
3. The project will pave the way for corporate governance related institutions, regulators, and public-listed companies in establishing a good corporate governance model in Indonesia.
4. Using the results of the study, the Indonesian corporate governance practices can be benchmarked against similar practices in other Asian countries, especially the IDEA.NET member countries (Singapore – Malaysia - The Philippines - Hong Kong – Thailand – Vietnam - South Korea - China - Taiwan – Indonesia). This benchmark is hoped to continuously improve the implementation of corporate governance practices in Indonesia.

The success of the present study would be measured by the following criteria:

1. Improvement in transparency and disclosure of reporting systems, such as annual report, financial report, and other public information, issued by publicly listed companies
2. Gradual improvement in the corporate governance performance, at least for the LQ45 (leading publicly-listed companies), from an average of 67.37 per cent in 2005 to 75.00 per cent in 2010.
3. Corporate governance practices will be gradually shifted from the local standard practices to the global ones. The IICD currently aids companies in making adequate public information available based on the OECD international standard codes of good corporate governance practices.

The first study of corporate governance scorecard, which was was intended to identify the state of corporate governance practices among the 61 surveyed companies (under LQ-45 from December 2004 to September 2005), was conducted in 2005. The scorecard was chosen as an analytical tool to improve the implementation of good corporate governance principles and to be able to benchmark the results against those from similar studies conducted by the IDEA.net members. The research methodology used in the study was based on the methodology adopted from the Thai IOD. IICD has presented the survey results in five (5) International and local seminars & forums in various occasions. One of the them has been especially designed for presentation to more than 150 directors and commissioners who belong as members of the association of the Indonesian Public Listed Companies (AEI-Asosiasi Emiten Indonesia). The impact of the study on these companies was beyond the expectation, as evidenced by the following:

1. The association of the Indonesian Public Listed Companies (AEI) in cooperation with the IICD would like to conduct more formal studies in the corporate governance scorecard starting from 2006.
2. The IICD and the association of the Indonesian Public Listed Companies (AEI) signed an agreement in December 2005 to cooperate in improving corporate governance practices in publicly-listed companies.
3. The surveyed companies reacted positively to the results and they asked for the IICD's advice on how to provide valuable information on good corporate governance practices for the public.
4. A positive reaction was also shown by the Indonesian chamber of commerce. There is a plan to hold a discussion on GCG topics between the chamber and the IICD.

D. Dissemination of the Results

Methods of disseminating the results used in the first study will be replicated in the second study, namely:

1. Specific Public and In-House Seminars
2. Directors' forum in cooperation with the Association of Indonesian Publicly Listed Companies (AEI), in the form of corporate governance rewards.

3. Written reports will be distributed to the surveyed companies, regulators, and other related parties in Indonesia, and to international agencies or organizations such as IFC, OECD,USAID, AUSAID, ADB, CIPE, and World Bank.
4. Special time allocation for the Professional Director Programs (PDP) held by the IICD (Recently, IICD conducted 32 PDPs that were attended by more than 600 Directors & Commissioners alumni).

II. RESEARCH METHODS

A. Surveyed Companies

The number of companies targeted for the present study were 329 members of the Association of Public Listed Companies (AEI, Asosiasi Emiten Indonesia).

B. Research Instrument

The corporate governance scorecard evaluation was developed based on the International Standard Code on GCG established by the Organization of Economic Cooperation and Development (OECD). The instrument was used to assess the following five (5) major areas:

- The right of shareholders
- The equitable treatment of shareholders
- The role of stakeholders
- Disclosure and transparency
- The responsibility of the board

Because there were no common practices of corporate governance, the OECD's International Standard Code of Practices on Good Corporate Governance were used as guidelines. By doing this, we were able to benchmark the research findings of this study against similar research findings conducted by other IDEA.net members in Singapore, Malaysia, The Philippines, Hong Kong, Thailand, Vietnam, South Korea, China, and Taiwan.

C. Data Collection

The data collection was based on a wide variety of publicly available information, such as annual reports and financial reports disclosed by those 329 companies in July 2006, companies' websites, securities and commission (BAPEPAM) filings, Jakarta Stock Exchange filings, meeting minutes and notes from corporate shareholders' meetings, and other publicly available sources. The data collection method was designed as if the researchers were outside investors, i.e., the researchers would assume the viewpoint of outside investors. By doing this, we hope that the findings of the study could benefit the investors, the regulatory bodies, governance-related institutions, and the market as a whole.

A data collection method that makes use of publicly available information has the following advantages:

- It is possible to include a large number of surveyed companies without necessarily asking for their permission
- It is possible to conduct longitudinal studies with the same samples. Such studies are needed to compare the corporate governance performance of surveyed companies year-by-year
- It is possible to compare the results of the studies among the IDEA.net members.

D. Evaluation Methods

The total weighted score was used to evaluate the level of corporate governance of each individual company. To avoid the element of subjectivity in evaluating the corporate governance practices of each company, we applied the check and balance techniques. A research team consisting of thirty (30) members was established to implement the tasks of evaluating the corporate government practices in each company. The thirty member team was subdivided into smaller teams consisting of two (2) assessors. The two assessors cross-checked every score assigned to each scorecard question to ensure accuracy and consistency.

The results were interpreted based on the following criteria:

Total Weighted Score	Performance	Interpretation
90 – 100 %	**Excellent**	Companies comply with the international standards of GCG-code promulgated by OECD as stated in the scorecard.
80 – 89 %	**Good**	Companies comply with more than the minimum regulatory requirements and less than the international standards of GCG-code as stated in the scorecard and show positive commitment to good corporate governance practices.
60 – 79 %	**Fair**	Companies comply with the minimum regulatory requirements.
Less than 60 %	**Poor**	Companies do not comply with the minimum regulatory requirements and do not show enough commitment to good corporate governance practices.

Tobin's Q analysis was used to measure whether the market performance of the participating companies was the result of implementing good corporate governance practices. The analysis showed whether good corporate governance practices led to high market valuation or not. The results would benefit the management of participating companies when considering the application of good corporate governance practices.

E. Research Members

a. Research Team Advisors:

- *Prof. Dr. Djisman Simanjuntak*
- *Sukono Soebekti, PhD*

b. Research Team:

- **Coordinator:** *James Simanjuntak, PhD*
- **Research Members:**
  - *Prof. Sidharta Utama, PhD CFA*
  - *Setio Anggoro Dewo, PhD*
  - *Chrysanti Hasibuan Sedyono, MiM*
  - *Ir. Dodi Prawira, MBA*
  - *Ir. Tony Silitonga, MBM, MBA, $DBA_{Can.}$*
  - *Kirti Peniwati, PhD*
  - *Ir. Johan Dharmawan, Msc*

III. EMPIRICAL RESULTS

A. Rights of Shareholders

In evaluating the implementation of the rights of shareholders, the first major area listed in the scorecard, a number of indicators consisting of 23 questions were used to examine how the rights are defined, how participation in shareholders' annual meeting is measured, and how the takeover rules are implemented. In general, the surveyed companies received the lowest score in this area compared to the scores in the other four major areas. Table 1 shows the overall performance of surveyed companies on the rights of shareholders.

Table 1
Performance of the Implementation of the Rights of Shareholders

Measures	Score (Current Assessment)	Score (Previous Assessment)
Mean	51.23	45.57
Minimum	42.03	37.33
Maximum	76.81	60.00

Note: The overall mean of the five major areas was 61.26 per cent (see p.74).

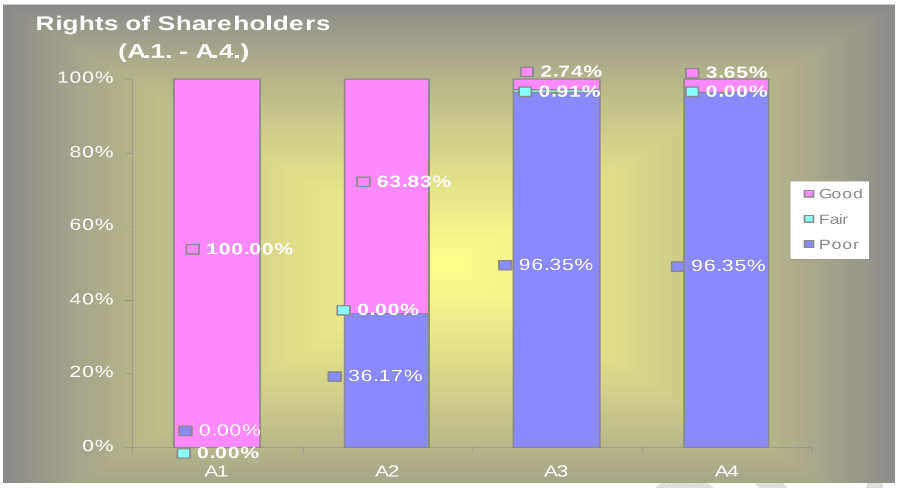
As shown in Table 1, there was improvement in all three categories (i.e., mean score; minimum score; and maximum score) compared to those found in the previous study. However, the average performance for all subject companies (51.23per cent per cent) was still below the overall mean (61.26 per cent) and even below the minimum regulatory requirements (60.00 per cent). In spite of this improvement, it seems that the rights of shareholders to participate and to be well-informed, and the other basic rights in shareholders' meetings were still inadequately provided by the surveyed companies. There were only three companies performed above the overall mean score. They were ANTM (69.57 per cent), MEDC (76.81 per cent), and PBRX (62.32 per cent).

With respect to the performance of surveyed companies on each indicator of the rights of shareholders, only a few of them such as other ownership rights in addition to the right to vote, the remuneration approval of the boards, the reasons or notes for the meeting agenda, the absence of cross-holdings, the share ownership by boards' members, and the consistency in carrying out the meeting agenda, had been implemented adequately by the majority of surveyed companies,. Most of the items were still poorly implemented by the majority of companies. The following is the performance of surveyed companies on each individual indicator..

A.1. Rights Defined

Questions A.1. to A.4. were designed to measure how the subject companies define the rights of shareholders. The rights of Shareholders need to be clearly defined to avoid misuse of responsibility since the boards may not act in the interests of shareholders effectively. Furthermore, the presence of the board of commissioners (BOC) in the corporate structure does not guarantee the protection of shareholders if their rights are not clearly defined.

OECD Principle 1: Rights of Shareholders – Rights Defined



A.1. Does the company offer another type of the ownership right in addition to the right to vote?

A.2. Is the decision on the remuneration of board members (directors and commissioners) approved by the shareholders annually?

A.3. How is the remuneration of the board presented?

A.4. Does the company allow shareholders to elect board members individually?

As stated previously, several indicators of the Rights of Shareholders had been implemented adequately. For Question A.1, all surveyed companies (100 per cent) provided other ownership rights such as the claim of company profit and the right for share repurchase, in addition to the right to vote, All subjects receive a good score in protecting the shareholders rights. Although improvement did occur compared to that in the previous study (85.20 per cent), it was not surprising since the Indonesia corporate law and other regulations issued by BAPEPAM (SEC) require that these rights of shareholders be provided.

The board remuneration received lots of attention since it is associated with one of corporate governance mechanisms which can be implemented effectively. This is why the OECD principles of good corporate governance require that the board remuneration be approved by the shareholders annually. With respect to this aspect, 63.83 per cent of surveyed companies asked for the shareholders' approval in the annual general meeting (AGM). These companies were rated good. 36.17 per cent of the total surveyed firms, however, seemed to ignore this aspect, i.e., their shareholders were not given any opportunity to exercise their right to approve or disprove the compensation of the boards. It should also be noted that there is a slight improvement compared to result of the previous assessment (52.20 per cent). The improvement was somehow unexpected since the current study used a more stringent instrument and involved the low-performance companies.

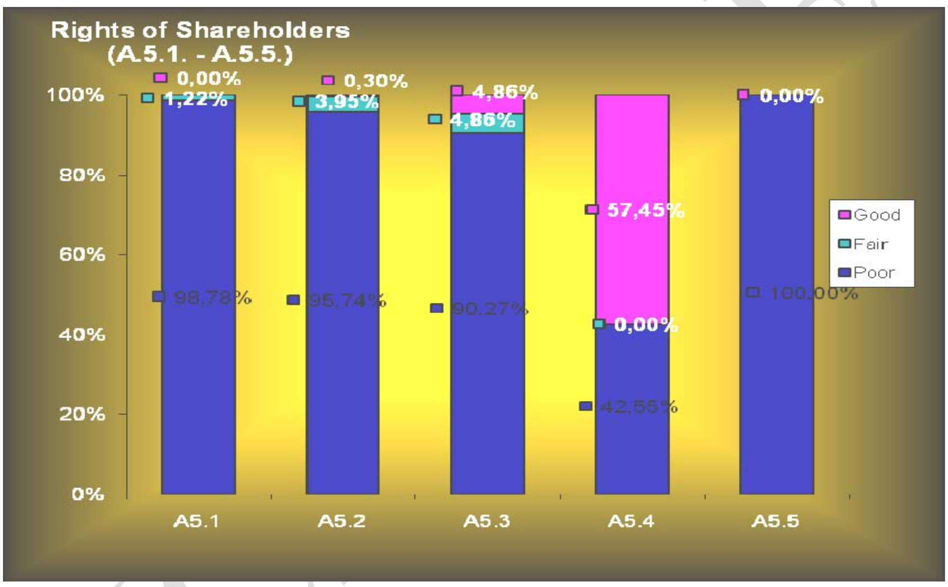
Although the majority of the firms asked for the approval of boards compensation for directors and commissioners annually, but details of the compensation (i.e., individual board compensation) were not presented by most companies (96.35 per cent). Such companies were rated poor. Only 2.74 per cent of them were considered good for practicing this item. Compared to the result of the previous study, however, a slight improvement did occur. It can be concluded that shareholders were provided with information on the total amount of compensation for the whole board members. They were given the opportunity to exercise their right to approve or disprove the board compensation annually, but they were not informed on how the board compensation structure was exactly determined.

Question A.4, constructed to measure the rights of shareholders in electing members of the boards, was a new item in the current scorecard assessment. It measured the voting procedure(s) used in the election. We found that only 3.65 per cent of the surveyed firms allowed their shareholders to elect board members with clear voting procedures. The majority of them (96.35per cent) either did not provide their shareholders with the opportunity to elect individual members of the boards or they did but without making clear voting procedures available.

A.2. Rights Disclosed

It is difficult to see how shareholders can exercise their rights if they are not well- informed about the agenda of the notice to call and the notice of results of the annual general shareholders' meeting (AGM). The OECD principles require that corporations provide shareholders with sufficient and timely information pertaining to the agenda of the AGM and give them the opportunity to raise questions about strategic issues.

OECD Principles 1: Rights of Shareholders – Rights Disclosed



A.5. Assess the quality of the notice to call the annual general shareholders' meeting in the past one year. Does the notice include (***A.5.1 – A.5.5***):

- A.5.1. Appointment of directors and commissioners, with names and profiles provided
- A.5.2. Appointment of auditors, with names and fees provided
- A.5.3. Dividend policy, with the amount of the dividend and its explanation provided
- A.5.4. Objective and reason for each item in the agenda
- A.5.5. Director's comment and opinion for each item in the agenda

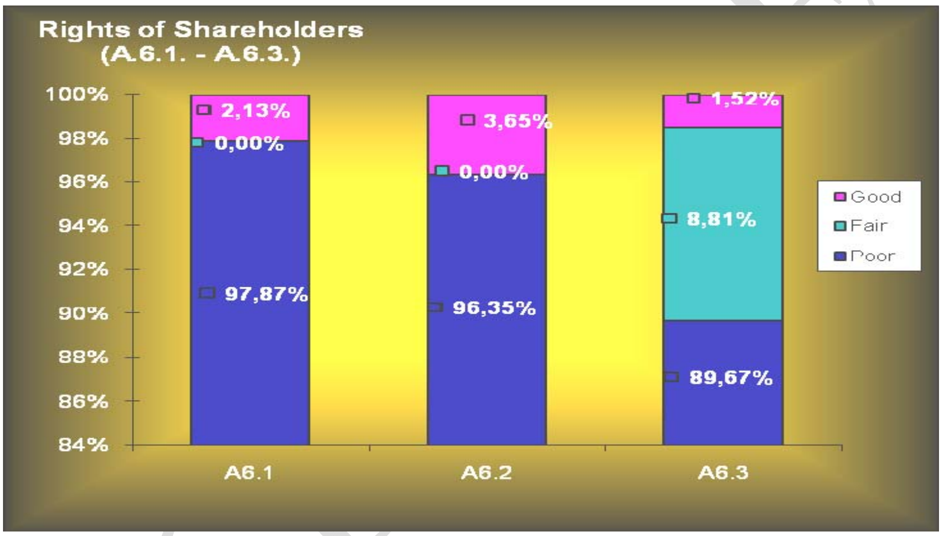
Items A.5.1. to A.5.5. were intended to measure the quality of notice to call the annual general meeting. As indicated by question A.5.1., the majority of surveyed companies (98.78 per cent) did not provide names and profiles of the directors and commissioners appointment in the notice to call annual general meeting, although the appointment of directors and commissioner was stated by all companies in the notice to call as an item in the agenda. These companies were rated poor in this aspect. It can be concluded that almost all companies did not provide their shareholders with information about the nominees for the members of the boards. Similar to the result of the previous study, the nomination practices found in the present study were still poorly implemented. Only 1.22 per cent included either names or profiles. Such companies were rated fair. Overall, the result was worse compared to that found in the previous assessment in which 3.30 per cent of firms met the international standard.

The same practices were also found in the appointment of external auditors (item A.5.2). Shareholders were ill-informed about the appointment of auditors. The majority of the subjects firms (95.74 per cent) did not include the names and fees of the auditors in the agenda of notice to call. Very few subjects (3.95 per cent) provided either names or fees. Only 0.30 per cent of subjects were rated good for this aspect, i.e., they provided both the names and fees of the auditors. It should be noted, however, that overall, there was a slight improvement compared to the result of the previous assessment in which all firms received a poor score.

With respect to Question A.5.3., the dividend policy, 90.27 per cent of surveyed companies received a poor score because they did not provide the amount of the dividend and its explanation in their dividend policy. Several companies (4.86 per cent) provided only one of the two. These companies were rated fair. Meanwhile, the rest (4.86), which included the two types of information in their agenda of notice to call annual general meeting, received a good score. Overall, the shareholders were better informed about the dividend policy compared to that found in the previous study (i.e., all firms received a poor score).

Question A.5.4. was designed to assess the objectives and reasons for each agenda listed in the notice to call annual general meeting. 57.45 per cent of surveyed firms, which provided the information, received a good score, while the rest (42.55 per cent), which did not include the information were rated poor. In the meantime, all the directors of surveyed companies (100 per cent), who did not provide any comment and opinion for each agenda listed in the notice to call, received a poor score.

OECD Principles 1: Rights of Shareholders – Rights Disclosed



A.6.1. Evaluate the voting method and vote counting system

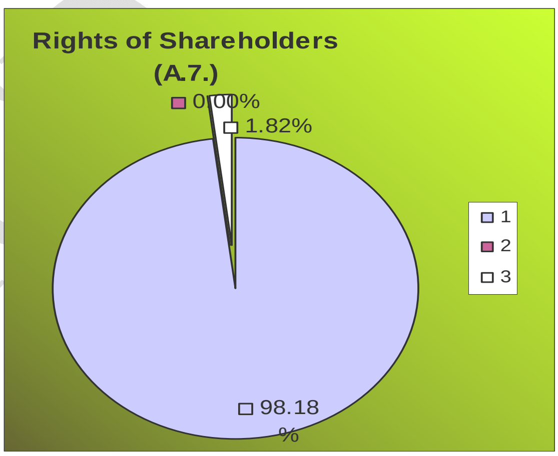
A.6.2. Do AGM minutes contain the chances given to the shareholders to ask questions or raise issues in the past one year? Also, is there a record of answers and questions?

A.6.3. Do the AGM minutes include any resolution(s) with voting results containing both agreeing and dissenting votes for each agenda item?

Treating the annual general meeting minutes as public information is still not a common practice for public corporations in Indonesia. Therefore, it is almost impossible to investigate how the companies protect the rights of their shareholders, especially the rights of the minority shareholders, such as the voting system, the opportunity to raise issues, and the resolution(s) taken to resolve the issues. With respect to iItem A.6.1, almost all companies (97.87 per cent) did not provide any information on the voting method, i.e., one that described how they made decisions that may affect the interests of shareholders. Such companies received a poor score. A few firms (2.13 per cent), which provided such information, received a good score.

The same situation was also found for Item A.6.2. The shareholders in most companies were not given the opportunity to raise issues in the annual general meeting. With respect to this aspect, 96.35 per cent received a poor score and only 3.65 per cent received a good score. Another piece of evidence was shown by the poor practices of the resolution on issues and the voting results (Question A.6.3). The majority of the firms (89.67 per cent) did not include the resolution and the voting results in the annual general meeting minutes. Several firms (8.81 per cent), which provided one item, received a fair score. The rest (1.52 per cent), which provided both the resolution and the voting results, received a good score.

OECD Principles 1: Rights of Shareholders – Rights Disclosed

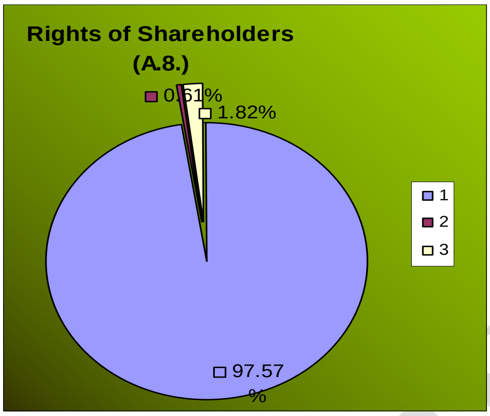


A.7. Is a name list of board attendance available?

For Question A.7., almost all firms (98.18 per cent) did not provide a list of the board members that attended the annual general meeting. Such firms received a poor score. Only less than two per cent (1.82 per cent) provided the list and these firms received a good score.

The percentage of the latter was slightly worse compared to that in the first scorecard assessment (i.e., 3.30 per cent received a good score)

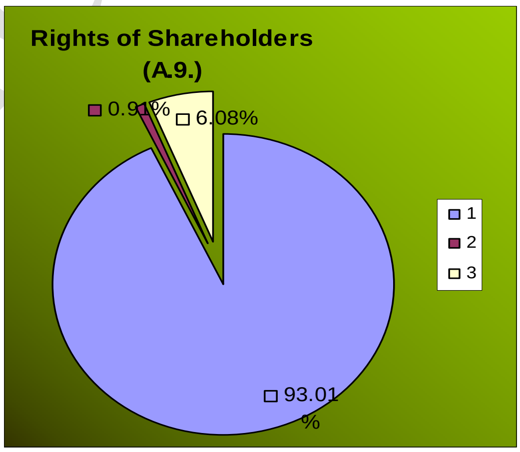
OECD Principles 1: Rights of Shareholders – Rights Disclosed



A.8. Did the chairman of the board attend at least one of the last two annual general shareholders' meeting?

For question A.8., the majority of surveyed companies (97.57 per cent) did not state whether the chairman of the board of commissioner attended the annual general meeting and therefore they received a poor score in this respect. Only 1.82 per cent of them received a good score and 0.61 per cent received a fair score.

OECD Principles 1: Rights of Shareholders – Rights Disclosed

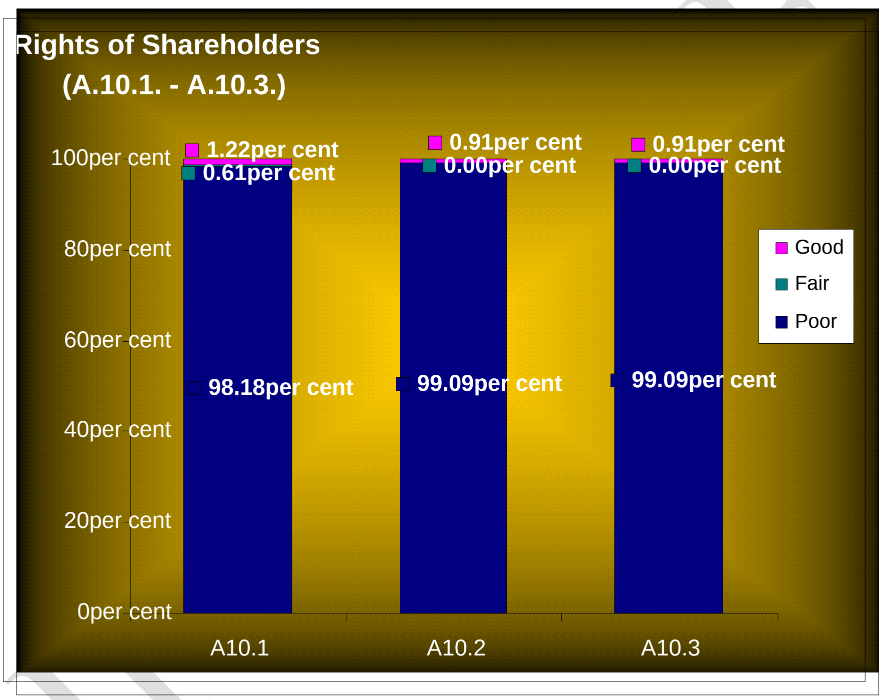


A.9. Did the CEO/managing director attend at least one of the last two annual general shareholders' meeting?

A quite similar result was shown by the responses to Question A.9. The majority of surveyed firms (93.01 per cent) were rated poor. Very few firms (6.08 per cent) received a good score, while the rest (0.9 per cent) received a fair score.

The results of Questions A.8. and A.9. were quite similar to those found in the previous study (i.e., 93.40 per cent and 98.40 per cent respectively)

OECD Principles 1: Rights of Shareholders – Rights Disclosed



A.10.1. Did the chairman of the audit committee attend at least one of the last two AGMs?

A.10.2. Did the chairman of the compensation committee attend at least one of the last two AGMs?

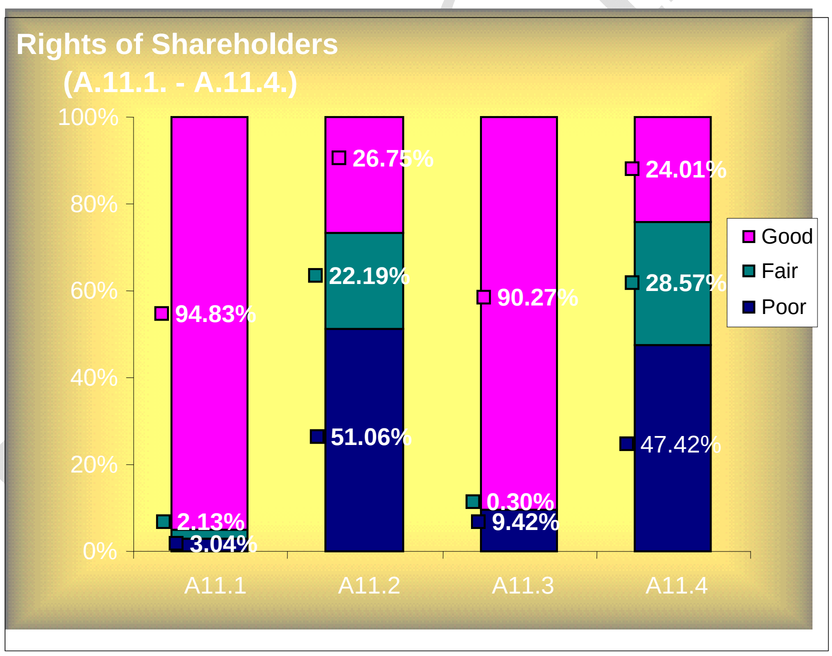
A.10.3. Did the chairman of the nomination committee attend at least one of the last two AGMs?

Questions A.10.1., A.10.2., and A.10.3. were first introduced in the present study. The results of these three questions were similar to those found in the previous questions. Most firms (98.18 per cent, 99.09 per cent, and 99.09 per cent respectively) did not state whether the chairman of the audit, the compensation, and the nomination committees respectively attended the annual general meeting. Such firms received a poor score poor with respect to these three questions.

A.3. Takeover Rules

The rights of shareholders in the corporate governance framework include the exercise of control over the corporation disproportionate to shareholders' equity ownership in the company. However, cross-shareholdings and pyramid structures may allow companies to establish anti-takeover mechanisms. These anti-takeover mechanisms can be used by management as devices to shield them from the monitoring by shareholders.

OECD Principles 1: Rights of Shareholders – Takeover Rules



A.11. Does the company have anti-takeover defences? (***A.11.1 – A.11.2***):

A.111. Is the cross-holding apparent?

A.11.2. Is the pyramid-holding apparent?

A.11.3. Do board members hold more than 25per cent of outstanding shares?

A.11.4. What is the proportion of outstanding shares considered as 'free float'?

Questions A.11.1., A.11.2., A.11.3., and A.11.4. were designed to investigate whether the surveyed companies established some takeover defence mechanism. The absence of cross-shareholding and pyramid holding provided an opportunity for shareholders to apply the external market mechanism through takeover to discipline ineffective directors or those who were involved in blatant opportunism. The ownership structure in terms of the board ownership as well as the proportion of free float did have a similar impact on the takeover defence.

The result of Question A.11.1. showed that the cross-shareholding was not apparent. The majority of companies (94.83 per cent) did not incorporate the cross-shareholding in their ownership structure. Such firms received a good score. Very few companies (3.04 per cent) received a poor score and 2.13 per cent of the firms were likely to establish the takeover defence. A slightly more than a half (51.06 per cent), which were practicing the pyramid holding, received a poor score. Some firms (26.75 per cent), in which the pyramid holding was not apparent, received a good score, while 22.19 per cent of them, which were likely to practice the pyramid holding ownership, received a fair score.

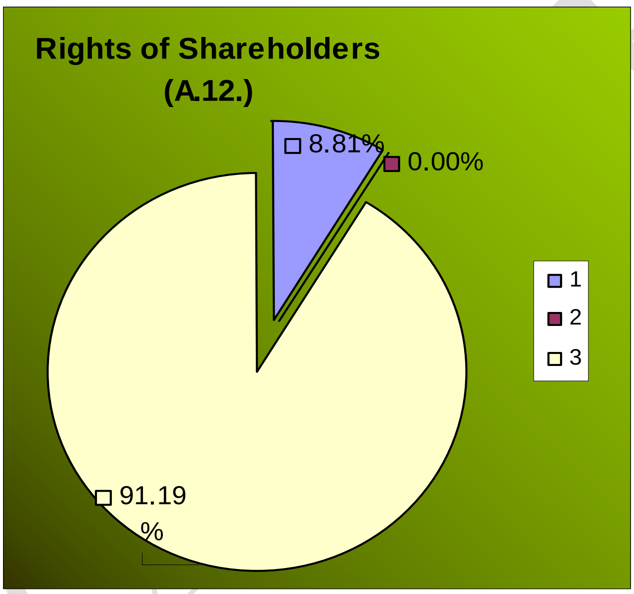
With respect to the board members share ownership, the majority of surveyed companies (90.27 per cent) indicated that the ownership of outstanding stock by board members was not significant (i.e., less than 25 per cent of total outstanding stock). Slightly less than one-tenth (9.42 per cent) received a poor score, and 0.30 per cent received a fair score.

The majority of subject firms (47.42 per cent), whose free float of their outstanding stock was less than 25 per cent, received a poor score.. Some companies (28.57 per cent), whose free float was between 25 and 40 per cent, received a fair score. Only 24.01 per cent received a good score because the proportion of their free float was 40 per cent or larger.

A.4. Penalty

Good corporate governance practices should not allow management to withhold some items of the agenda for their own interests. The shareholders have the rights to be better informed in timely manner about the issues at the AGM.

OECD Principles 1: Rights of Shareholders – Penalty



A.12. There was an additional agenda item(s) at the AGM/EGM that was not included in the notice to call meeting.

Question A.12. was designed to investigate whether or not the surveyed companies fully informed their sharehoders of the items of the agenda in the notice to call annual general meeting. Witholding some items of the agenda can be considered as abuse of information because the shareholders have the rights to know in advance all the items of the agenda in the AGM notice.

The majority of surveyed companies (91.19 per cent), whose shareholders were fully informed in advance about the items of the agenda in the AGM notice, received a good score. 8.81 per cent of them, which received a poor score, tended to withold some items of the agenda in the AGM notice.

B. Equitable treatment of Shareholders

The OECD principles stated that “the corporate governance framework should ensure the equitable treatment of shareholders. All shareholders should have the opportunity to obtain effective redress for violation of their rights”. This section discusses whether all shareholders, especially the minority shareholders and foreign shareholders, are treated fairly and equally. Table 2 summarizes the performance of equitable treatment of shareholders.

Table 2:
The performance of Equitable Treatment of Share holders

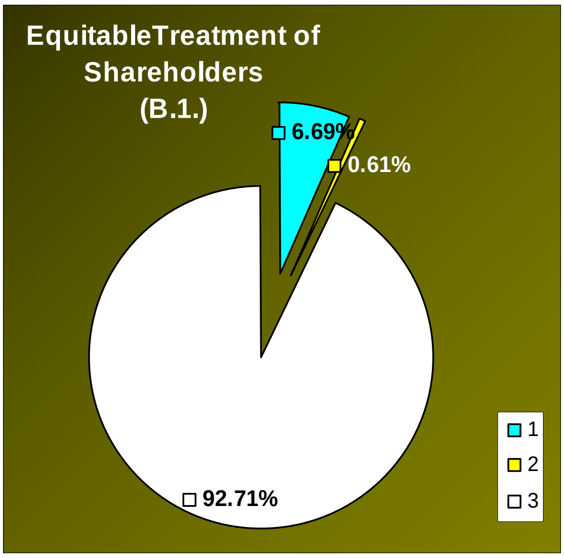
Measures	Score (Current Study)	Score Previous Study
Mean	83.05 %	88.14 %
Minimum	52.78. %	83.33 %
Maximum	100 %	93.33 %

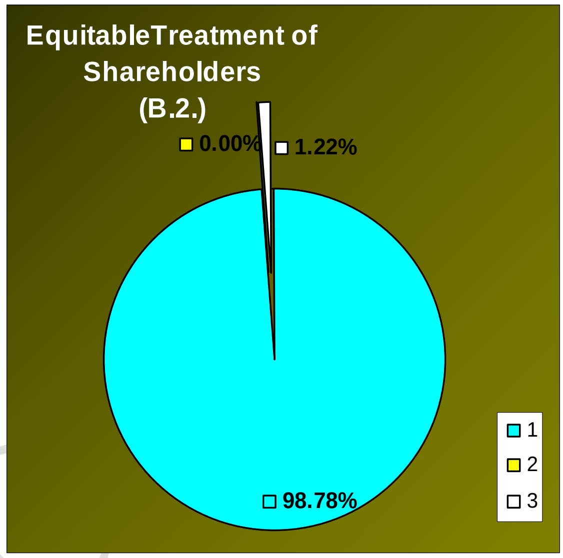
As we see in Table 2, the performance of equitable treatment of shareholders decreased compared to that in the previous study. The gap between the minimum and maximum performance also became wider. It should be noted, however, that unlike the previous study, the present study involved the low-performance firms and the use of a more stringent instrument.

B.1. Voting Rights For Share

All shareholders, including the minority and foreign shareholders, should be treated equitably regarding the voting rights attached to all classes of shares they possess. Incorporating these voting rights is important since it may play a role in affecting the composition of the boards.

OECD Principles 2: Equitable Treatment of Shareholders – Voting Rights for Shares





B.1. Does the company offer one-share-one-vote?

B.2 Is there any mechanism provided by the company to enable the minor shareholders to play a role in affecting the board composition (BOC and BOD)?

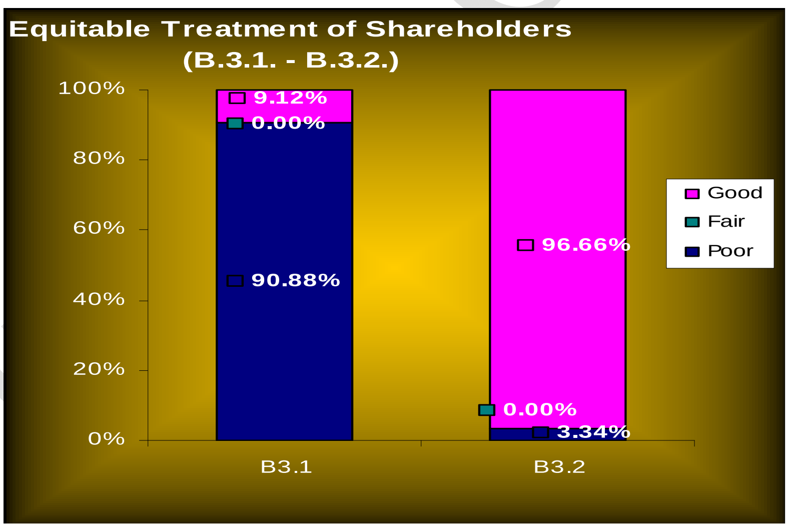
With respect to Question B.1., the majority of surveyed firms (92,71 per cent) turned out to apply the one-share-one-vote system and therefore received a good score. Although the law requires that one share should carry the weight of one vote, several companies, especially state-owned enterprises, offered two different classes of share and only one of them incorporated the one-share-one-vote system. Therefore, such firms (6.69 per cent) received a poor score.

Regarding Question B.2., our study found that the protection for minority shareholders was still poorly implemented by almost all surveyed companies (98.78 per cent). Such companies did not establish a mechanism to protect the interest of the minority shareholders. The cumulative voting system by the minority shareholders was still an uncommon practice in Indonesia. 1.22 per cent of the firms, which received a good score, provided a mechanism to protect the minority shareholders.

B.2. Shareholders Conflict

Incorporating the equitable treatment of shareholders is important in the corporate governance framework for the purpose of avoiding the conflict. Good practices that are in accord with the OECD principles require that the minority shareholders be protected from abusive acts by the controlling shareholders such as the use of insider information, the insider trading, and inapropriate related-party transactions. Questions B.3.1. to B.5. were meant to assess the shareholders conflict that may occur between the minority and themajority shareholders.

OECD Principles 2: Equitable Treatment of Shareholders
Shareholders Conflict



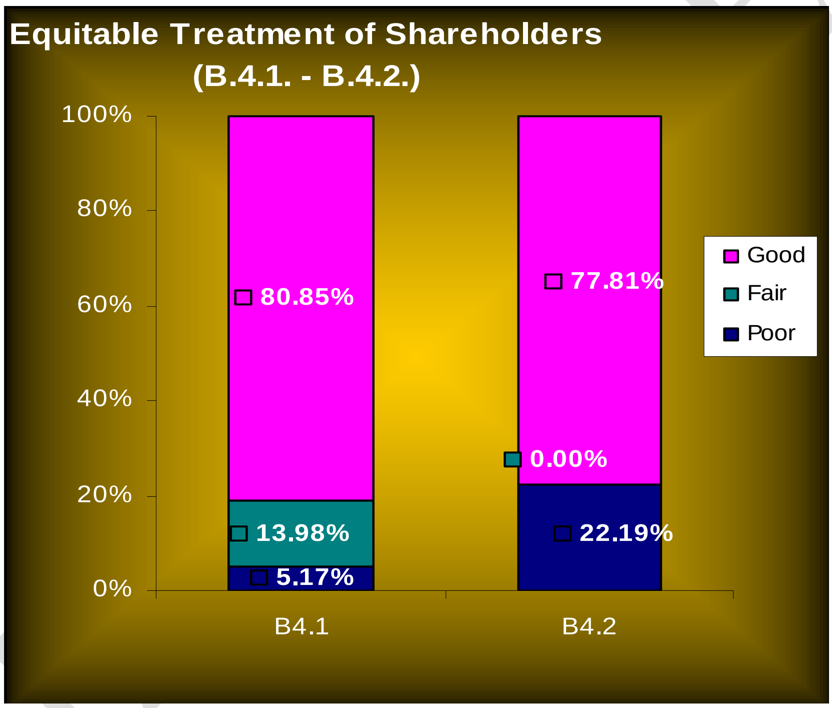
B.3.1. Does the company establish a system that prevents insider trading?

B.3.2. Have there been any cases of insider trading involving the company directors and management in the past two years?

With respect to Question B.3.1., we found that the majority of surveyed companies (90.88 per cent) did not establish a system and a policy to prevent insider trading and therefore received a poor score in this respect. Only a few companies (9.12 per cent) received a good score.

Almosf all firms (96.66 per cent) stated that there was no evidence of insider trading involving their members of the boards in the last two years. Several firms (3.34 per cent), which showed the evidence, received a poor score, as shown by the result of Question B.3.2.

OECD Principles 2: Equitable Treatment of Shareholders
Shareholder Conflict



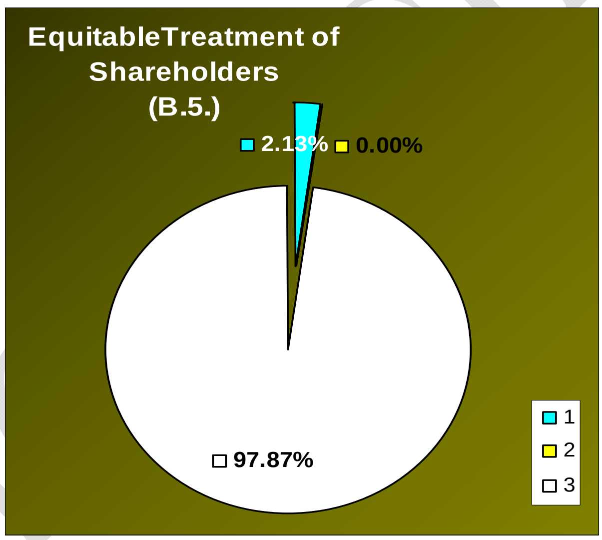
B.4.1. Does the company provide a rationale or an explanation for any related-party transactions that may affecti the corporation?

B.4.2. Is the company a part of an economic group where the majority shareholders control key suppliers, customers, and/or similar businesses?

The majority of companies (80.85 per cent) provided an explanation for their related-party transactions by disclosing the details of the transactions (i.e., by including names, parties, policy, and value). 5.17 per cent of surveyed companies, which did not provide any explanation for their related-party transactions, received a poor score), while 13.98 per cent, which received a fair score, provided an incomplete explanation for their related-party transactions..

With respect to Question B.4.2., our study found that the majority of surveyed companies did not operate as an economic group. Although transactions with their affiliates existed, the amount of transactions was less than 20 per cent. Such companies were rated good. 22.19 per cent of firms, however, operated as an economic group in which the parent companies controlled their key suppliers and customers more than 20 per cent. These companies received a poor score.

OECD Principles 2: Equitable Treatment of Shareholders
Shareholders Conflict



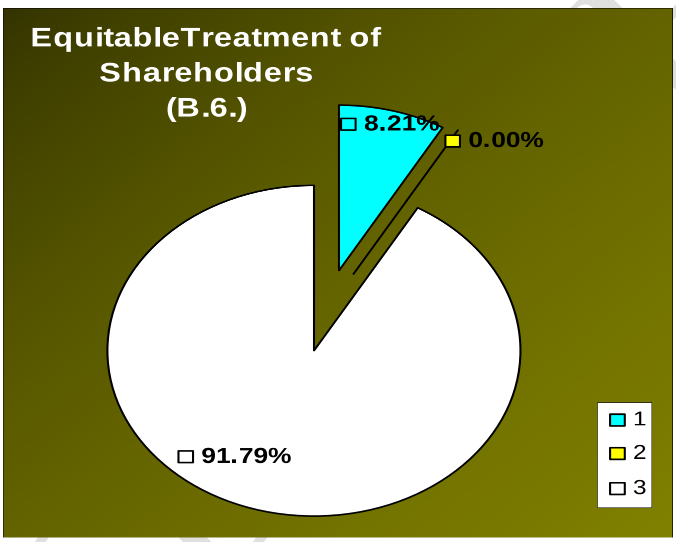
B.5 Have there been any cases of non-compliance with the law and regulation regarding the related-party transactions in the past two years?

The majority of firms (97.87 per cent) received a good score for their compliance with the law and regulation as well as the international standard regarding related-party transactions. Only 2.13 per cent of surveyed companies received a poor score because of non-compliance. Overall, the percentage of poor performance increased slightly compared to the percentage found in the previous study (1.60 per cent)

B.3. Proxy Voting/ AGM Procedures

Voting by proxy is an effective way to encourage shareholders to exercise their rights to vote at the AGM. Through this, the shareholders can delegate their voting rights to custodian institutions. However, good practices require that custodian institutions provide shareholders with any information pertaining to the options in exercising their voting rights.

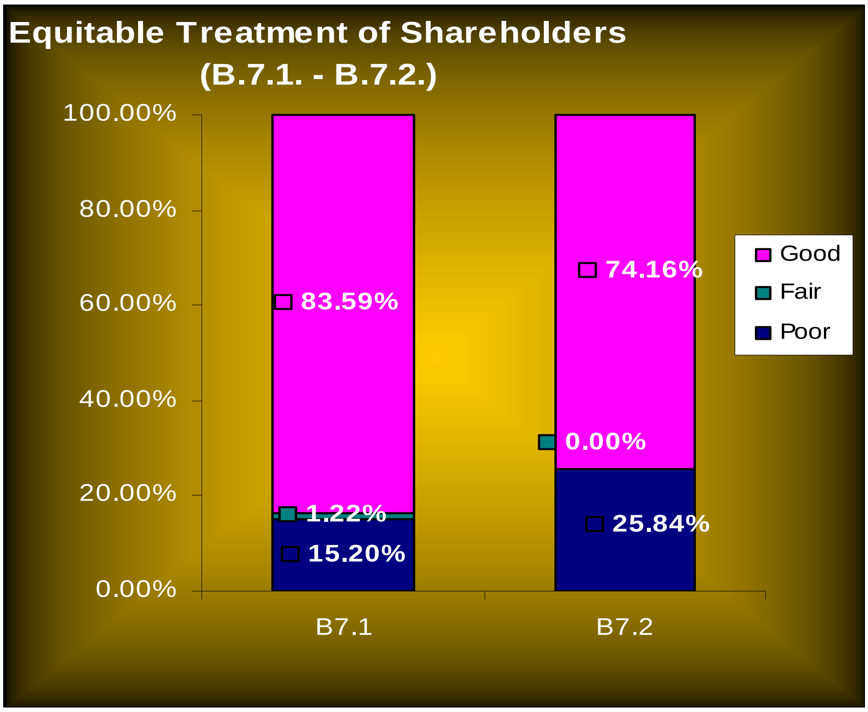
OECD Principles 2: Equitable Treatment of Shareholders
Proxy Voting/AGM Procedures



B.6 Does the company make voting by proxy available?

Voting by proxy turned out to be a common practice in Indonesia. As shown by the result from Question B.6., almost all companies (91.79 per cent) made voting by proxy available. Only 8.21 per cent of surveyed companies received a poor score because they did not make voting by proxy available.

OECD Principles 2: Equitable Treatment of Shareholders
Proxy Voting/AGM Procedures



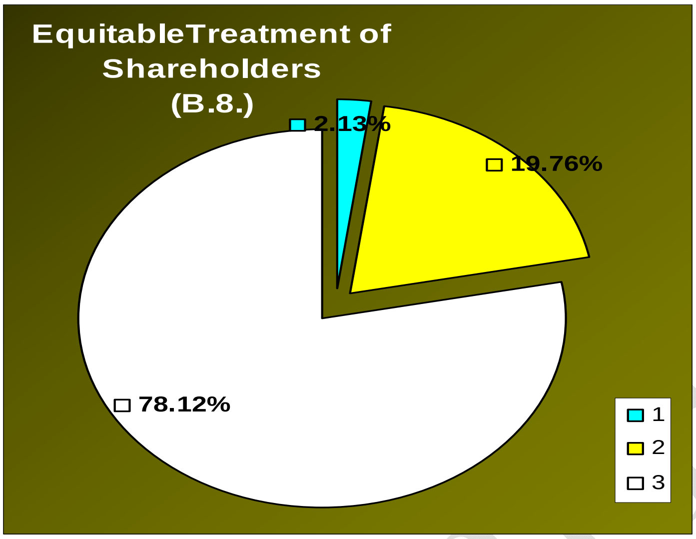
B.7.1. Does the notice to shareholders specify the documents required to be proxy?

B.7.2. Is there any requirement for a proxy appointment to be notarized?

The majority of companies (83.59 per cent) clearly specified the documents required for proxy voting as shown by the result from Question B.7.1. Such companies were rated good in this respect. Some companies (16.41 per cent), however, received a poor score because they did not specify the documents required for proxy.

With respect to Question B.7.2., we found that that the majority of surveyed companies (74.16 per cent) did not require a proxy appointment to be notarized. Such companies received a good score in this respect. 25.84 per cent of companies, however, required a proxy appointment to be notarized and they received a poor score for this.

OECD Principles 2: Equitable Treatment of Shareholders
Proxy Voting/AGM Procedures



B.8. How many days in advance does the company send out the notice for the annual general meeting?

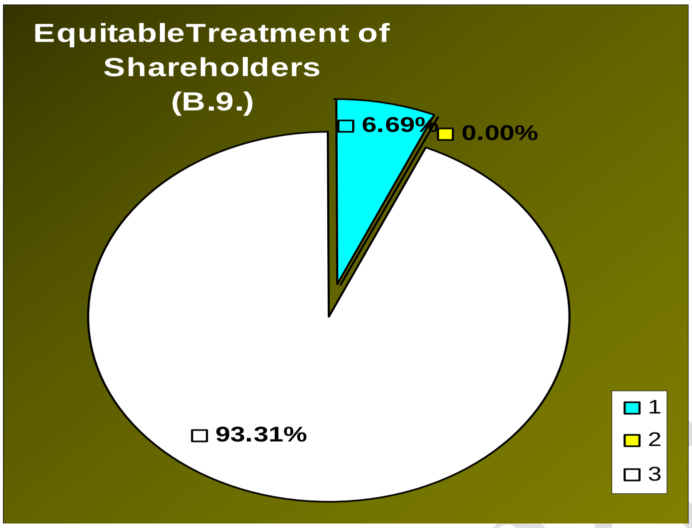
The majority of firms (78,12 per cent) sent out the notice for the annual general meeting 21 days or more in advance. Because of this, the shareholders were believed to able to scrutinize the proposed agenda. However, we found that the shareholders were not well-informed about the items listed in the agenda..

Some companies (19.76 per cent), which received a fair score, sent out the notice to call from seven to less than twenty one days in advance, while 2.13 per cent of them, which received a poor score, sent out the notice less than seven days.

B.4. Penalty

Good corporate governance practices require that any related party transactions, including financial assistance to non-subsidiary companies, be disclosed in order to avoid abusive acts by the controlling shareholders.

OECD Principles 2: Equitable Treatment of Shareholders
Penalty



B.9. Were there any related party transactions that can be classified as financial assistance to non-subsidiary companies?

Question B.9. were first introduced in the current assessment. It was designed to investigate whether any financial assistance to non-subsidiary companies, such as loan or loan guarantee, were given by surveyed companies in their related-party transactions. We found that the majority of surveyed companies (93.31 per cent) did not provide any financial assistance to non-subsidiary companies in their related-party transactions. Such companies received a good score in this respect. Several companies (6.69 per cent) however, received a poor score in this respect.

C. Role of Stakeholders

The third element of the OECD principles of good corporate governance refers to the role of stakeholders. Corporate governance goes beyond the agency relationships. It represents relationships among stakeholders used to develop and monitor the company's strategic issues. A corporate governance framework should recognize the rights of stakeholders established by the law or through mutual agreements and encourage active cooperation between the corporations and the stakeholders in creating wealth, jobs, and the sustainability of financially-sound enterprises. Overall, the results of the performance of the role of stakeholders can be seen in Table 3.

Table 3: The Performance of the Role of Stakeholders

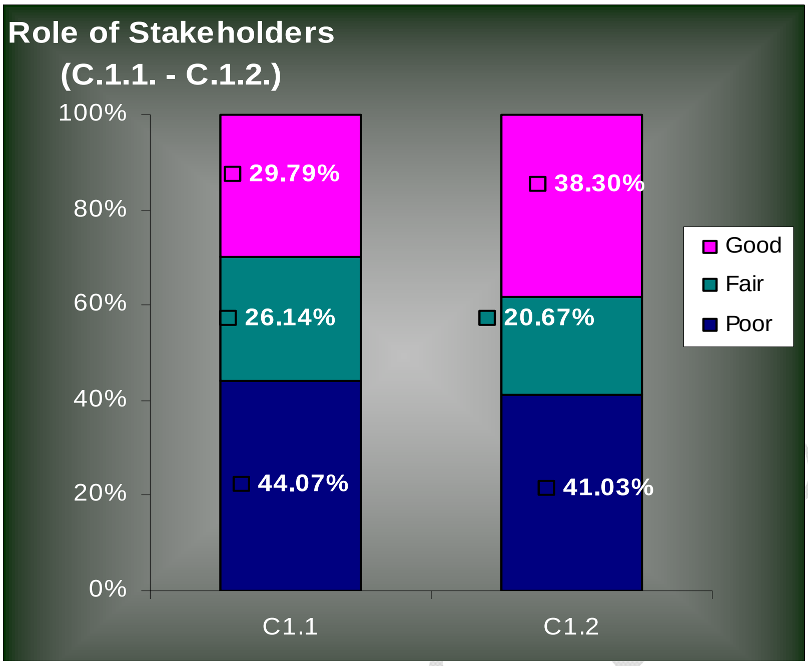
Measures	Score (Current Study)	Score Previous Study)
Mean	58.76 per cent	68.99 per cent
Minimum	33.33 per cent	33.33 per cent
Maximum	100.00 per cent	100.00 per cent

As we see in Table 3, the mean score of the performance of the role of stakeholders was lower than that found in the previous study. This lower performance may be attributed to the use of a more stringent instrument and the inclusion of the low-performance companies.

C.1. Rights Recognition

Recognizing the rights of other key stakeholders such as customers, employees, suppliers, pressure groups, and the society has been considered as a source of company's sustainability of competitive edge in the global arena. This aspect contributes to the shareholder value creation in the long-run. Question C.1.1. to C.7. were designed to investigate how the surveyed companies recognized the rights of their stakeholders.

OECD Principles 3: Role of StakeholdersRights Recognition



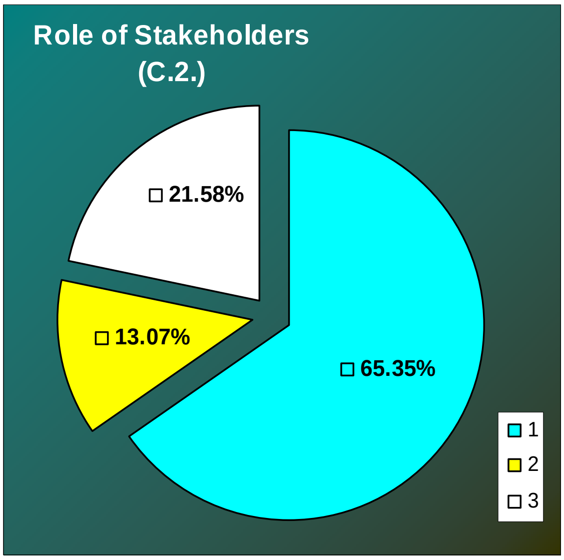
C.1.1. Does the company explicitly mention the benefits package to its employees?

C.1.2. Does the company explicitly mention programs to develop and train employees?

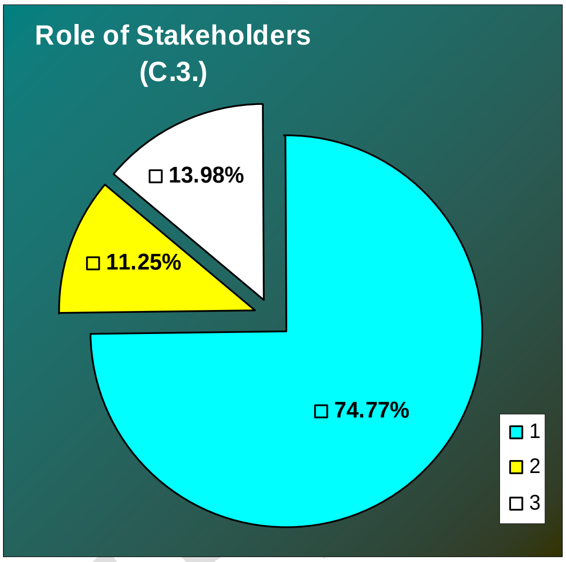
Questions C.1.1. and C.1.2. were meant to assess how the surveyed companies treated their employees. As shown by results of Question C.1.1., only 29.79 per cent of surveyed companies provided a comprehensive benefits package for their employees, while 26.14 per cent of them only provided a partial package. The majority of companies, however, did not provide any benefits package for their employees. Such companies received a poor score in this respect.

We also found that the majority of surveyed firms did not explicitly mention programs to develop their employees. Only 38.30 of the companies provided comprehensive training programs were 38.30 per cent, while 20.67 per cent of them provided some incidental programs.

OECD Principles 3: Role of Stakeholders – Rights Recognition



C.2. Does the company explicitly mention the role of customers?

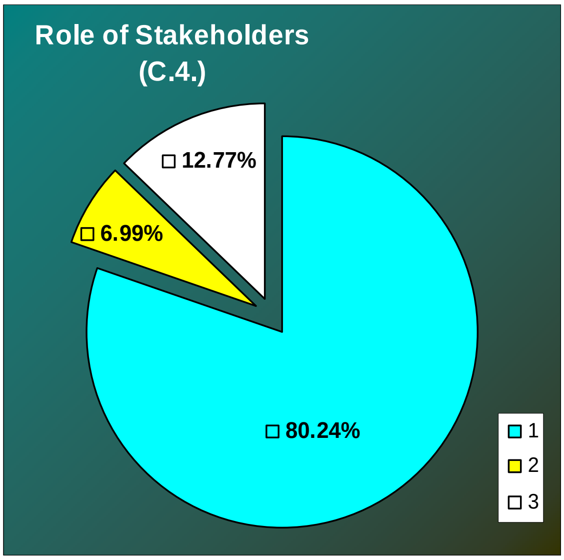


C.3. Does the company explicitly mention the role of suppliers?

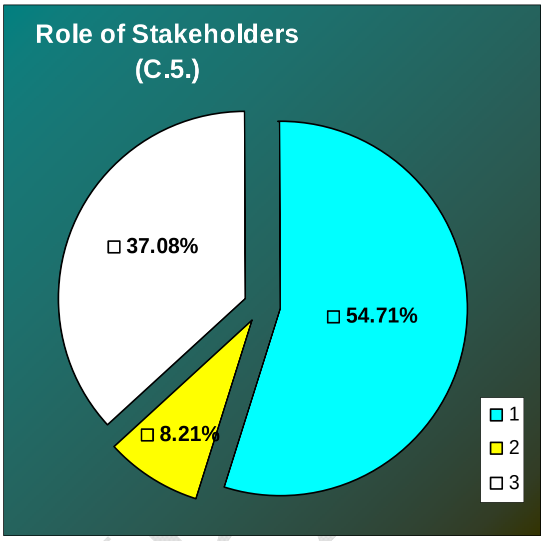
The majority of surveyed companies (65.35 per cent) did not explicitly mention the roles of customers in their strategic directions. Such companies received a poor score. 21.58 per cent of the companies received a good score because they developed comprehensive programs to improve their customers' satisfaction and loyalty, while 13.07 per cent of them, which provided superficial programs, received a fair score.

The majority of surveyed companies (74.77 per cent) received a poor score because they did not explicitly mention the roles of their suppliers. 13.98 per cent of the companies, which provided a comprehensive coverage of the roles of their suppliers, received a good score, while 11.25 per cent of them received a fair score because they only provided a superficial coverage.

OECD Principles 3: Role of Stakeholders – Rights Recognition



C.4. Does the company explicitly mention the obligations of its shareholders?

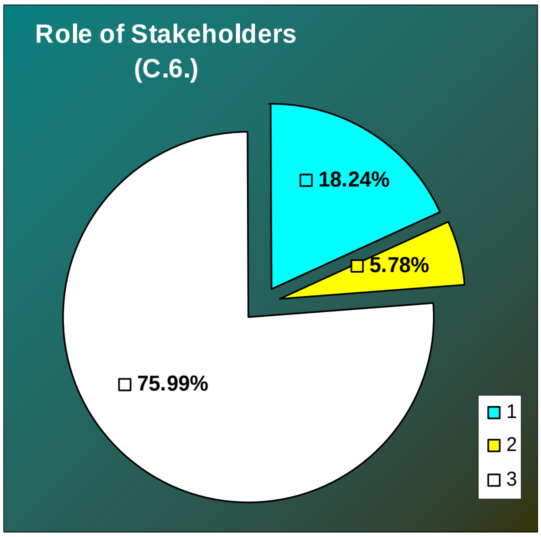


C.5. Does the company explicitly mention its obligations to the society?

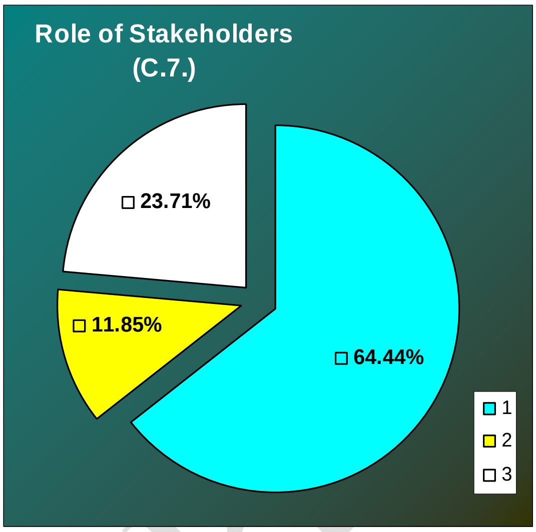
We found that the majority of surveyed companies (80.24 per cent) did not explicitly specify the obligations of their shareholders. Such firms were therefore rated poor in this respect. 12.77 per cent of the companies, which explicitly mentioned the obligations of their shareholders, received a good score, while, 6. 9 per cent received a fair score in this respect.

As shown by the results from Question C.5., 54.71 per cent of surveyed companies received a poor score because they did not explicitly mention their obligations to the society. 37.08 per cent of the companies, which explicitly mentioned their obligations, received a good score, while 8.21 per cent, which mentioned some of their obligations, received a fair core.

OECD Principles 3: Role of Stakeholders – Rights Recognition



C.6. Does the company explicitly mention its obligation to creditors?



C.7. Does the company explicitly mention environmental issues in its public communication?

It seemed that creditors were the most important one with respect to the roles of stakeholders (question C.6). We found that the majority of surveyed firms (75.99 per cent), received a good score in this respect, 5. 78 per cent received a fair score, and 18.24 per cent received a poor score.

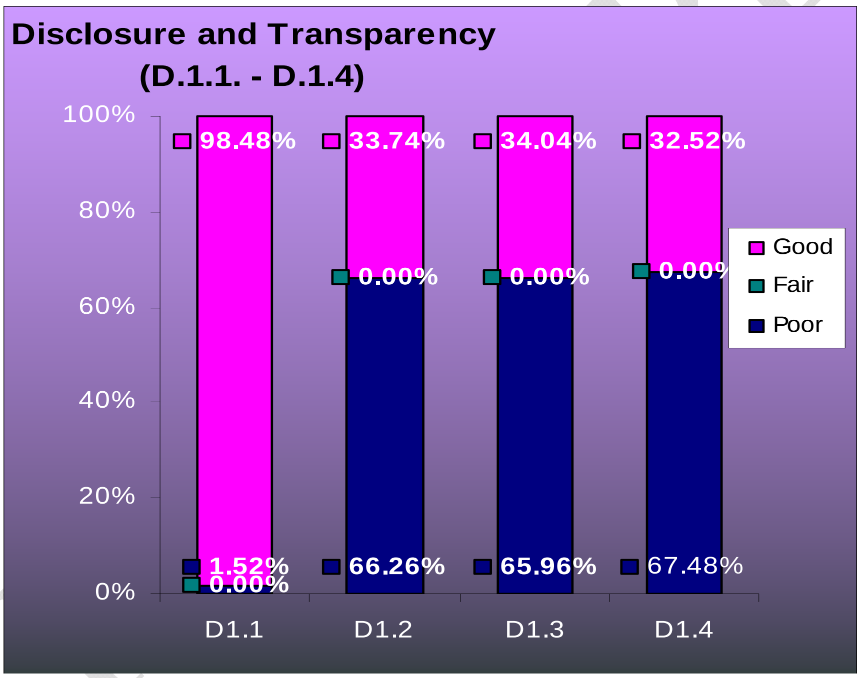
The environmental issues still remained a problem for the surveyed companies. 64.44 per cent of the companies received a poor score in this respect, 23.71 received a good score, and 11.85 per cent received a fair score.

D. Disclosure and Transparency

The overall mean score for the Disclosure and Transparency aspect was 66.64 per cent; the minimum score was 43.75per cent and the maximum score was 98.96 per cent. Although the score was not bad, given that nowadays firms have more channels to communicate and given that the demand for more voluntary information from outside investors and other parties keeps increasing, the score should have been higher.

In general, all the firms provided information required or encouraged to be disclosed by Bapepam. However, the other types of information that might be relevant to the stakeholders but are not required were insufficiently disclosed. The average score for required or encouraged disclosure (Questions: D1.1; 2.1; 2.2; 2.3; 2.5; 3; 5; 6; 7.1; and 8, 11) was 90.1 per cent, while the average score for voluntary disclosure was only 54.3 per cent. The mean score for voluntary disclosure implied that on average more firms received a 'poor' score rather than a 'good' score. The following section discusses in detail the results for each question.

OECD Principles 4: Disclosure and TransparencyOwnership Structure



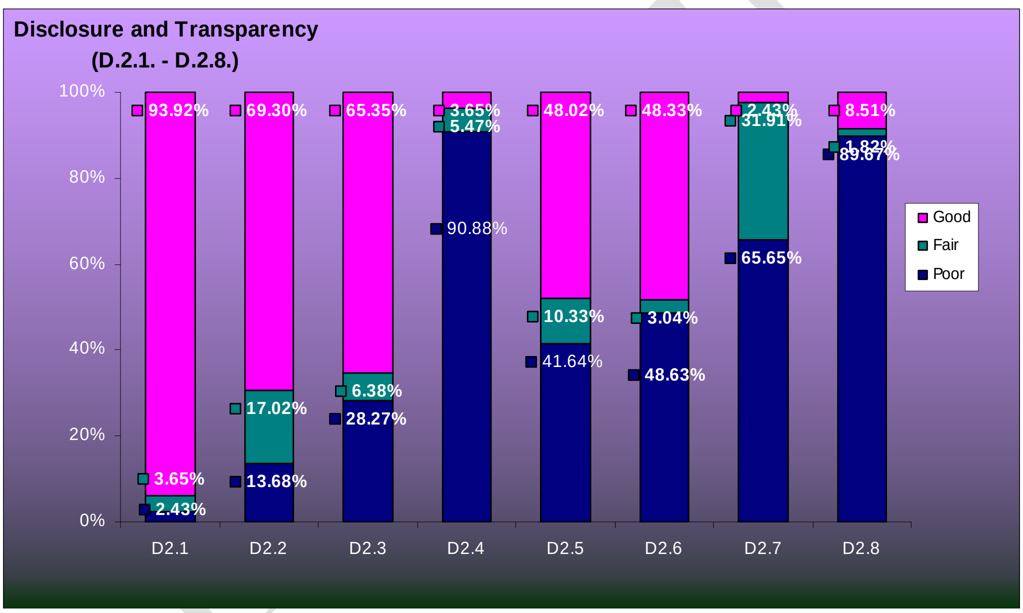
D.1. Does the company have a transparent ownership structure?

- D.1.1. Is a breakdown of shareholdings provided?
- D.1.2. Is it easy to identify beneficial ownership?
- D.1.3. Are commissioner shareholdings disclosed?
- D.1.4. Are director shareholdings disclosed?

D.1. Ownership Structure

Disclosing the detail of ownership structure is very important in countries (including Indonesia) whereby shares ownership by public investors is relatively small. We found that almost all companies provided the breakdown of shareholdings and complied with the requirements set by Bapepam. However, the majority of the firms (66per cent) did not disclose the beneficial ownership and the share ownership by commissioners and directors. Thus, overall, the disclosure of information about the detail of the ownership structure among publicly listed companies in Indonesia was relatively insufficient.

OECD Principles 4: Disclosure and Transparency – Annual Report



D.2. Assess the quality of annual report in each of the following areas (***D.2.1 – D.2.8***),:

- D.2.1. Financial performance
- D.2.2. Business operations and competitive position
- D.2.3. Board members background
- D.2.4. Basis of the board remuneration
- D.2.5. Operating risk
- D.2.6. Identification of independent directors
- D.2.7. Disclosure of individual directors' remuneration
- D.2.8. Board meeting attendance of individual directors

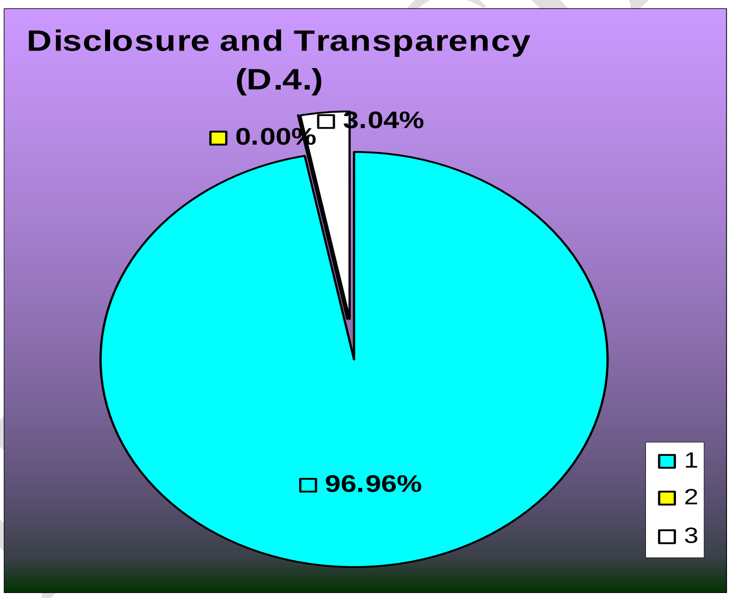
D.2. Annual Report

The annual report represents the primary medium of communication from companies to investors and other parties. The stakeholders utilize information in the annual report to evaluate the firm performance and, more importantly, to assess the boards' qualification and accountability. The assessment is necessary since the stockholders and other parties delegate the overseeing function to the board of commissioners and the managerial function to the board of directors. As such, the annual report ought to contain not only information about a firm but also the qualification, the activities and the remuneration system of the boards.

The disclosures related to the firm background and performances were relatively good. Almost all firms (more than 90 per cent) provided information related to the financial performance; the majority of the firms (almost 70 per cent) also disclosed the operation and the competitive edge of the firms, but less than half of the firms discussed their operating risk. Given the ever increasing business uncertainties nowadays, the information on operating risk is very relevant in evaluating the overall risk of the firm. With the increasing awareness among the companies about the importance of risk management, we believe that the disclosure of information about the operating risk will improve in the future.

The surveyed firms had a tendency to limit the disclosures of information about their board members just to required information. The majority of the firms (almost 70 per cent) provided the background of the board members, while surprisingly, only less than 50 per cent of the them provided information on independent directors of the firms. The minority shareholders and other stakeholders need to know who independent commissioners/directors of the firms are since these parties are supposed to protect the interest of the firm and not the interest of the major shareholders.. Almost all firms (more than 90 per cent) did not provide any information on board remuneration and activities (proxied by numbers of meeting). Disclosing individual directors' remuneration is quite sensitive Indonesia because of the large remuneration gap between the top management and lower level unskilled employees. It is feared that disclosing their remuneration may result in increasing tension between the top management and the employees. In any case, this lack of information makes it difficult for the stakeholders to evaluate the boards' accountability and thus we concluded that the disclosure of information about the boards' accountability was insufficient.

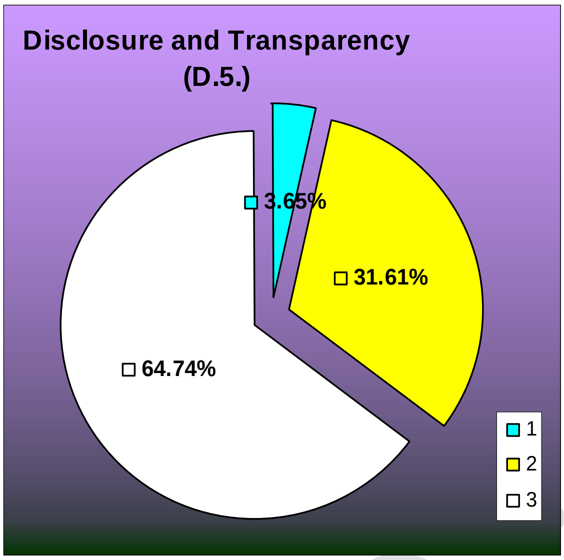
OECD Principles 4: Disclosure and transparency – Annual Report



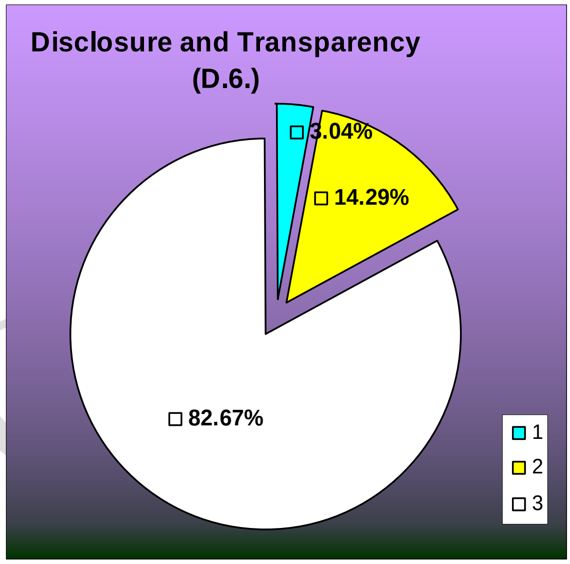
D.4. Does the company have a specific policy requiring the director to report the transactions of company shares?

Almost all companies insufficiently disclose whether or not they have a specific policy requiring a director to report the transactions of company shares. There are several possible accounts for this. First, companies have the policy but fail to disclose it to the public. Second, director of the companies do not own shares and thus it is not relevant for companies to set up the policy. Third, companies do not have the policy even though the directors own company shares. The third one is the most risky viewed from the perspective of investors because it indicates that the companies do not have any control over insider trading and may not able to prevent directors from being involved in insider trading. Such a situation is unfair to the shareholders.

OECD Principle 4: Disclosure and transparency – Financial Statement



D.5. Does the company perform an annual audit using independent and reputable auditors?



D.6. Are there any accounting qualifications in the audited financial statements apart from the qualification on uncertainty of situation?

D.3. Financial Statements

Questions D.5, D.6, D.8 and D.10 are related to financial statements and thus are discussed together.

Bapepam requires that a financial statement be audited by external auditors recognized by it. Some auditors are those that do not have any international affiliation. We found that 65 per cent of the firms were audited by internationally affiliated external auditors while the rest by local external auditors. To ensure the independence of external auditors, Bapepam limits the number of years that a public accounting firm can audit its client. The maximum period is five year, and afterwards a firm has to switch to another public accounting firm. This regulation may explain why, compared to other countries, in Indonesia there are a large number of firms audited by local auditors.

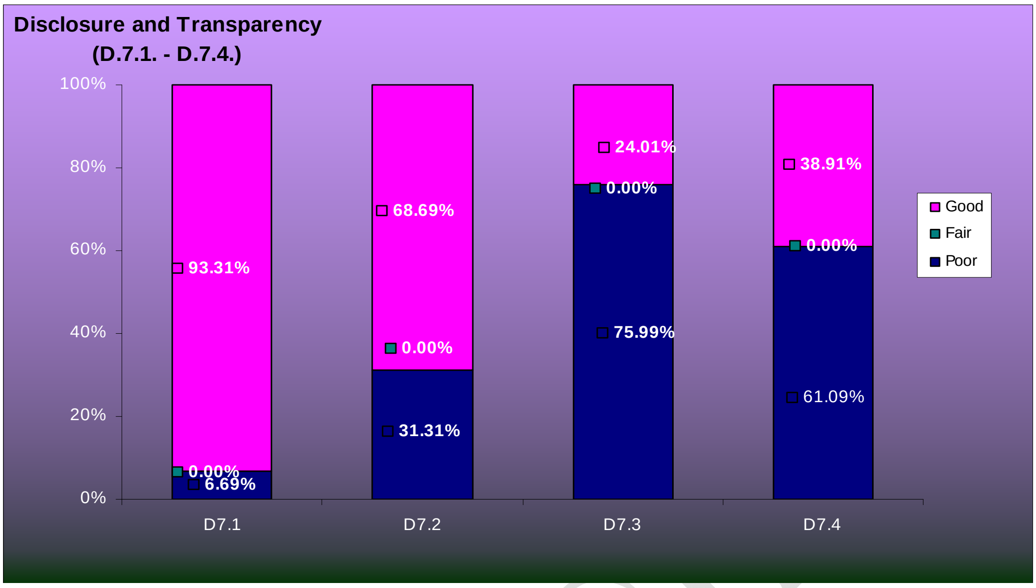
With regard to the audit opinion, more than 80 per cent of the firms received an unqualified opinion without any qualification, while more than 14 per cent of them received an overall unqualified opinion with some qualifications. Such a good result should be expected because firms may prefer to comply with the auditors' suggestion to make some audit adjustments rather than not complying, as the latter may result in a qualified opinion that will affect the credibility of the financial statements.

Almost all companies disclosed their financial statements on time, which according to the rule set by Bapepam is 3 months after the end of year. Bapepam may impose monetary sanctions for those that are late and in addition, the public in general take note of companies that are late and in some cases penalize these companies. For example, a business magazine every year provides awards to those companies considered to do well with respect to their financial performance as well as stock market performance. One criterion used to select the nominated firms is that the firms have to submit their financial report on time to Bapepam. This may explain why almost all firms submited their financial statements on time.

D.4. Access To Information

With regard to Question D.10, financial statements of almost all companies are accepted by Bapepam without any required revisions. This may suggest that at least from the regulator's perspective, there was no questionable information in the financial statements.

OECD Principles 4: Disclosure and Transparency – Access to Information



D.7. Does the company offer multiple channels of access to information, Include (***D.7.1 – D.7.4***):

D.7.1. Annual report

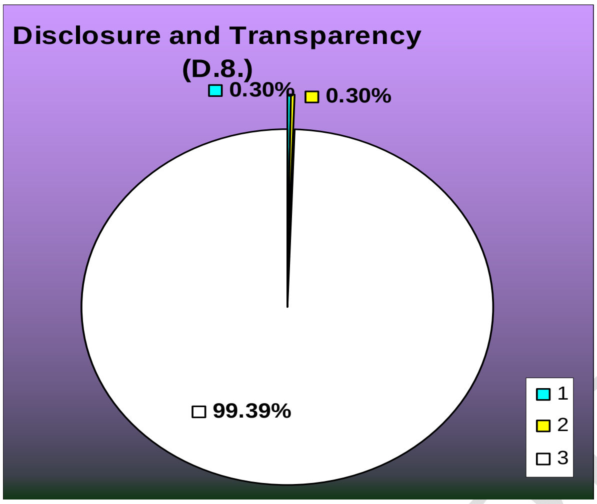
D.7.2. Company website

D.7.3. Analyst briefing

D.7.4. Press conference/press briefing

As part of the disclosure principle, companies have to offer multiple channels of access to information. The use of multiple channels will enable stakeholders to conveniently and easily access information about the companies. We found that almost 94 per cent of surveyed companies published an annual report. This is to be expected since Bapepam requires that listed firms publish an annual report., However, the voluntary use of other channels was not yet optimally utilized. For example, only 68 per cent of the firms had company website. Given that nowadays the most convenient way to obtain information is through the internet and given that the cost of developing and maintaining a website is relatively low, the finding that more than 30 per cent companies did not have a website suggests that such companies might not have been aware of the importance of being transparent to the public.

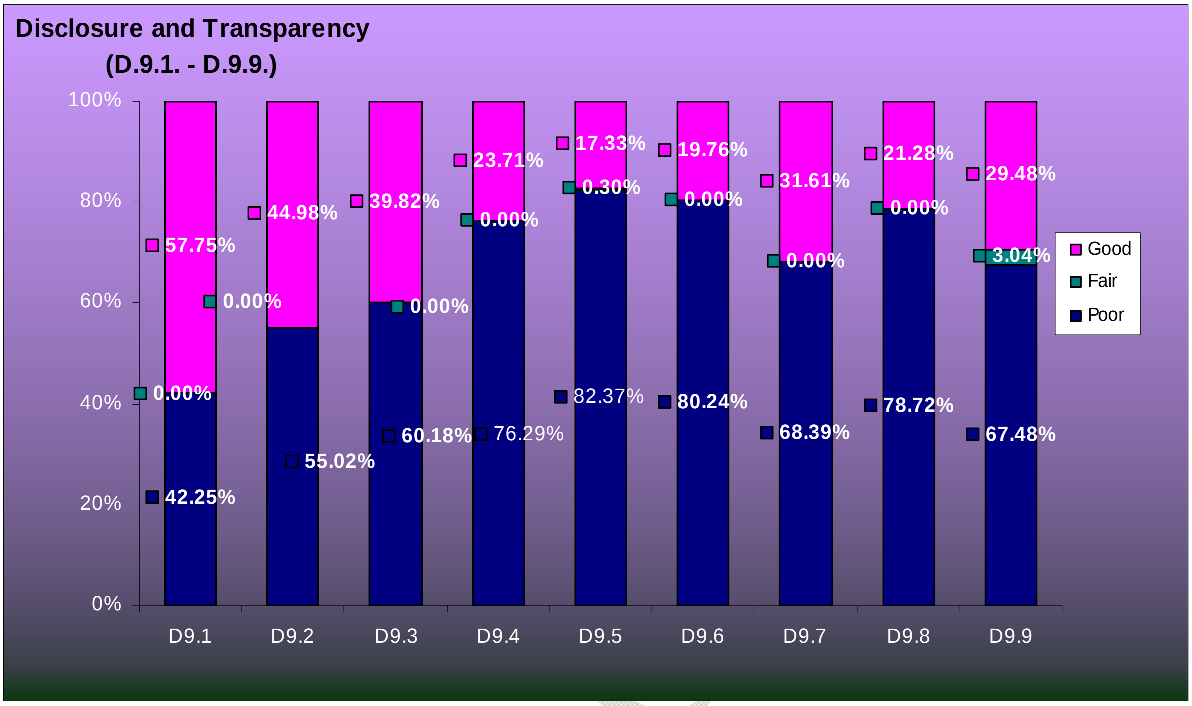
OECD Principles 4: Disclosure and transparency Access to Information



D.8. Is the financial report disclosed in a timely manner?

Furthermore, only a quarter of the firms were known publicly to have conducted an analyst briefing, while less than 40 per cent were found to have given press conferences. Thus, the finding that firms tended to use only mandatory channels for information access implies that public access on information is relatively limited, thereby resulting in a relatively high degree of information asymmetry between the companies and the public.

OECD Principles 4: Disclosure and transparency – Access to Information



D.9. Does the company have a website disclosing up-to-date information, Include (***D.9.1 – D.9.9***):

D.9.1. Business operation

D.9.2. Financial statement

D.9.3. Press release

D.9.4. Shareholding structure

D.9.5. Organization structure

D.9.6. Corporate group structure

D.9.7. Downloadable annual report

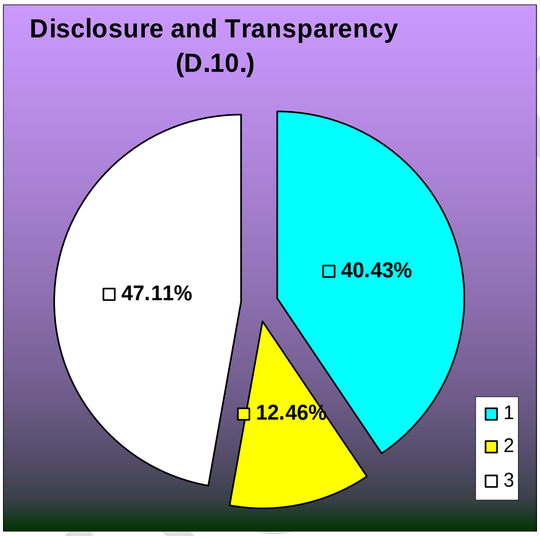
D.9.8. Notice to call shareholders' meeting

D.9.9. Website available in both Indonesian and English

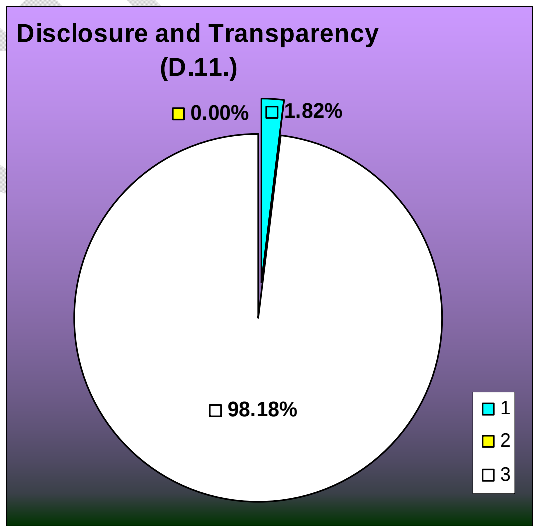
Question 9 assessed information contained in the company website. Since 31 per cent of the firms did not have a company website, they received a poor score in this respect. The unavailability of company websites also explained why the overall score for this question was low. We found that the information disclosed in the website were mostly about business operation and financial statement.

Some companies (about 40 per cent) used their websites to issue the press release. A few companies (less than 40 per cent) disclosed information on the shareholding, organization, and corporate holding structures. Surprisingly, only 21 per cent used their websites to announce the shareholders' meeting, which may have affected the level of attendance of shareholders (especially the attendance of minority shareholders). Finally, only 30 per cent of the companies made their websites available in English. This is hard to understand, considering the fact that foreign investors make up quite a large portion of share ownership at the Jakarta Stock Exchange.

OECD Principle 4: Disclosure and transparency – Access to Information



D.10. Does the company provide contact details that are easily accessible to outside investors?



D.11. Was there any record of sanctions by BAPEPAM for financial statements that were not revised?

To ensure transparency, companies need to provide contact details that are easily accessible to outside investors. Less than half of the firms provided such contact details. 12.5 per cent of the firms provide the name of a contact person but the contact information was missing. More than 40 percent of them did not provide any contact details. This finding suggests that the awareness of companies to have more open communication with outside investors was relatively low.

D.5. Comparison to 2004

The overall average disclosure score in 2005 (66.64 per cent) was lower than that in 2004 (75 per cent). In all types of information, the scores in 2005 were lower than those in 2004. However, the firms studied in 2004 consisted of big firms that belonged to the LQ-45 Index, while those studied in 2005 included almost all firms listed in the stock exchange. Since the firm size positively affects the disclosure score, the results in 2004 tend to be biased upward. Furthermore, the list of items of disclosure for the year 2005 and 2004 was not exactly the same. Due to these two factors, the results in 2005 cannot be directly compared to those in 2004.

E. Responsibility of the Board

The fifth OECD principle addresses the responsibility of the boards (directors and commissioners). Since the boards, especially the board of commissioners, in a dual tier system such as in Indonesia act as representatives of shareholders to protect the interest of shareholders and management, they do have the vital role in the corporate governance framework. It is stated in the OECD principles that the boards should act on a fully informed basis, in good faith, with due diligence and care, and in the best interest of the firm and shareholders. The boards should also apply the high ethical standard and able to exercise an objective independent judgment. Their key functions include, among others, reviewing the company's strategic direction, assessing company's governance practices, electing and compensating directors, monitoring the process of disclosure and transparency, etc.

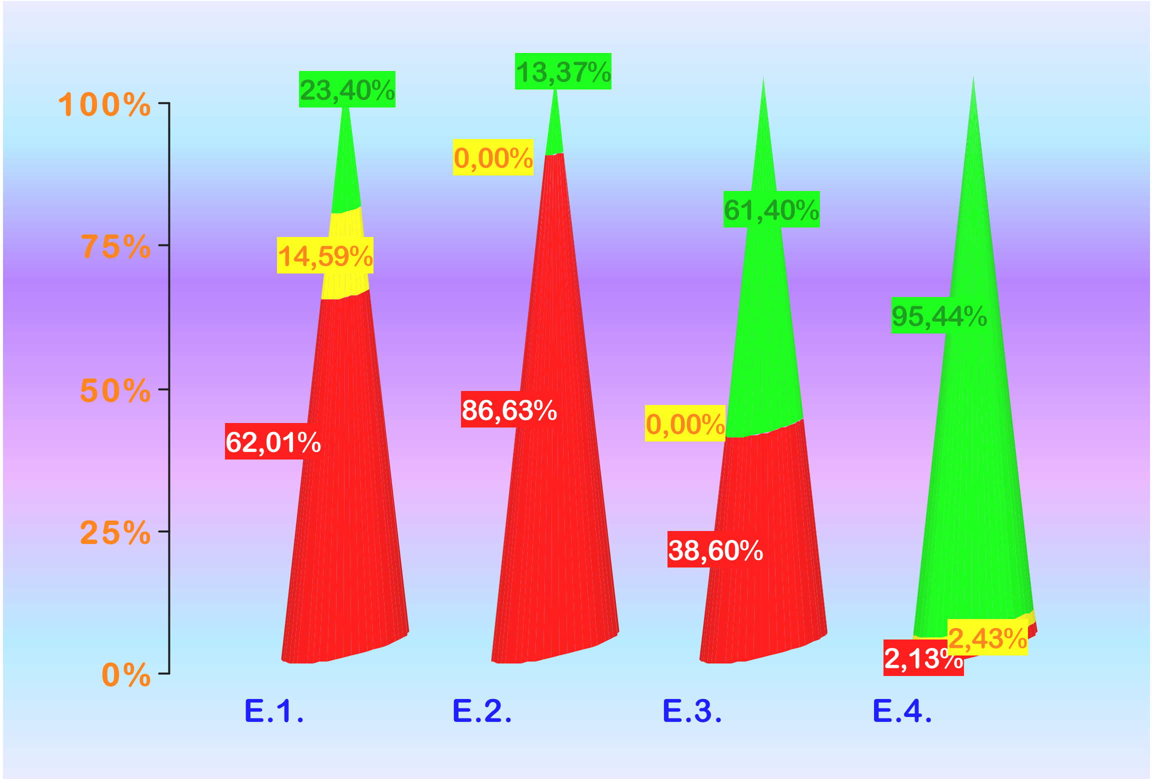
The performance of surveyed companies on Responsibility of The Board practices reached 52.32 per cent, slightly below the overall mean which reached 61.25 per cent. Of the five (5) principles of the OECD International Standard Code of Practices in Good Corporate Governance, the Responsibility of The Board practices was the worst, in addition to The Rights of Shareholders which reached 51.23 per cent. To interpret the relationship between the two, we could say that the low score in Responsibility of the Board correlated with the low score in Rights of Shareholders. Responsibility of The Board Practices would need to be improved to reduce agency problems in the surveyed companies. The highest score was 92.86 per cent and the lowest was 31.75 per cent for this aspect.

Questions E1-E26 assessed the responsibilities of the board of directors and commissioners and the leading roles that the board plays in overseeing and enhancing corporate governance practices. E1-E4 assessed the board's effectiveness in monitoring and controlling the firm, the first three (3) variables looked into the acceptance of Good Corporate Governance principles by the corporations in the form of the availability of the Governance Charter. Question E-4 measured the compliance level of the surveyed companies on the JSX/SEC(BAPEPAM) rules and regulation over the last three years.

E.1. Monitoring/Control

With respect to Question E.1., 62.01 per cent of surveyed firms received a poor score, meaning that the majority of them had not yet established rules of corporate governance that clearly articulate the responsibility of the board and the company's value systems. 14.59 per cent of the companies received a fair score, meaning that the corporate governance policies and rules were either not fully disclosed or the responsibility of the board were not clearly articulated. Only 23.40 per cent of firms received a good score, meaning that these companies had established rules of corporate governance that clearly articulate the responsibility of the board and the company's value systems. Such good firms came from Banking, Insurance, and Multi-finance industries (35.07 per cent). Their good score seemed to correlate with the availability of the written corporate governance rules that clearly describe the value system and the board responsibility in their companies.

OECD Principles 5: Board Responsibilities –Monitoring/Control



E.1. Does the company have its own written corporate governance rules that clearly describe its value system and board responsibility?

E.2. Does the board of commissioner provide the code of ethics or the code of appropriate business conduct to all directors and employees to ensure that they are aware of and understand it?

E.3. Does the company have a statement of corporate visions or missions?

E.4. Does the JSX/SEC (BAPEPAM) have any evidence of non-compliance of the company with JSX/SEC(BAPEPAM) rules and regulation over the last three years?

With respect to Question E.2., only a few surveyed companies (13.37 per cent) received a good score, meaning that their board of commissioners provided the code of ethics or the code of appropriate business conduct to all directors and employees to ensure that they are aware of and understand it. The majority of surveyed companies (86.63 per cent), however, received a poor score. The majority of surveyed companies that received a good score were Banking, Insurance, and

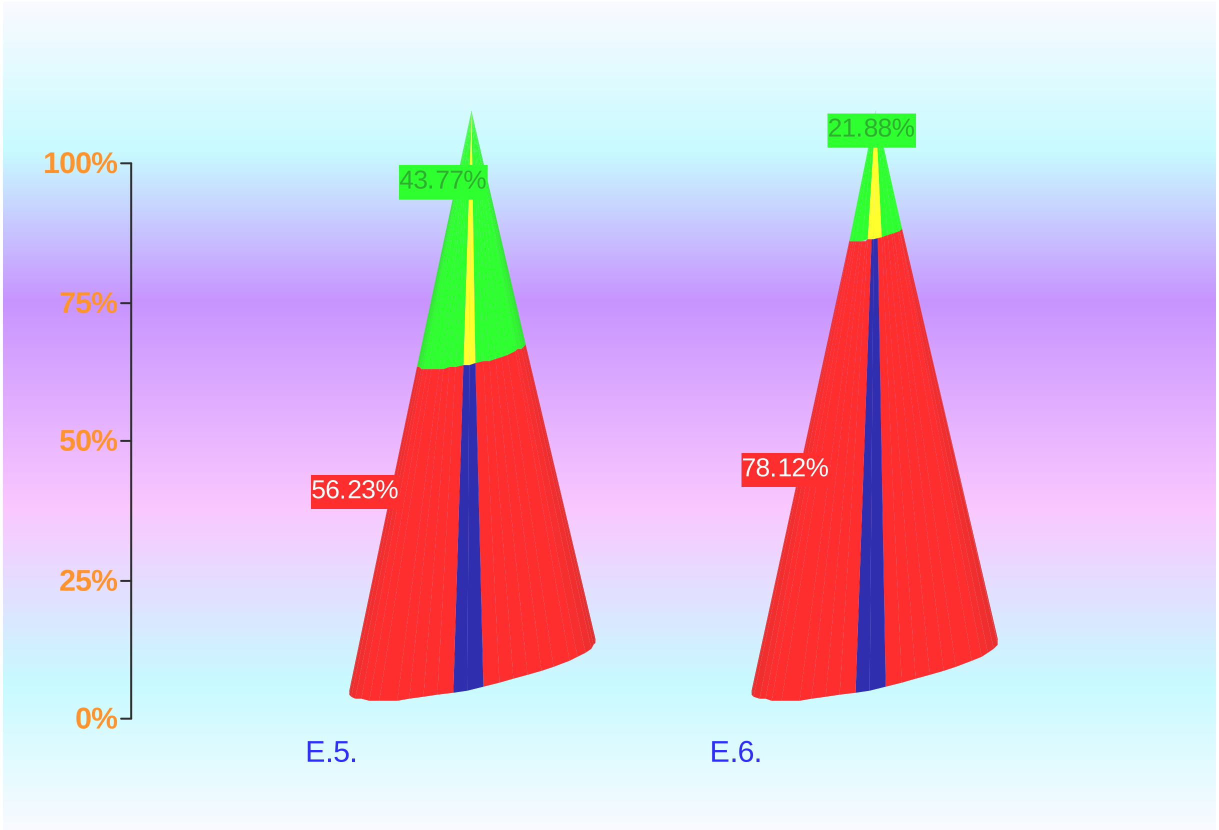
Multi-finance industries (34.09 per cent). The results suggest that the Board of Commissioners of Indonesian Publicly listed companies need to play a more active role because the OECD International standard of practices on Good Corporate Governance requires that the board apply high ethical standards. In other words, the Board of Commissioners need to “work at the board” not “sit at the board”.

A notable number of firms (61.40 per cent) had a statement of corporate visions or missions, while the rest (38.60 per cent) did not. .

With respect to the non-compliance with JSX/SEC rules and regulations over the last three years (i.e., Question E.4.), it is quite surprising that the majority of surveyed firms (95.44 per cent) never experienced non-compliance. This result was better than that in the previous study that included LQ-45 firms where 88.50 per cent of them received a good score. 2.43 per cent of the companies received a fair score in this respect, while 2.13 per cent of them received a poor score.

Questions E.5. and E.6. assessed whether or not the surveyed companies have an internal audit operation that was established as a separate unit in the company and to whom the internal audit function reported. With respect to Question E.5., we found that 43.77 per cent of the surveyed companies had an internal audit operation that was established as a separate unit in the company to accommodate the best practices of Good Corporate Governance monitoring and control. However, the majority of them (56.23per cent) still needed to improve their internal audit operation. With respect to Question E.6., only 21.88 per cent of the firms received a good score, while the majority of them (78.12 per cent) had no clear information as to whom the internal audit function reported. The Governance charter should include the internal audit tasks and organization to make sure the monitoring and control of the firms as one of the board responsibilities.

OECD Principles 5: Board Responsibilities – Monitoring/Control



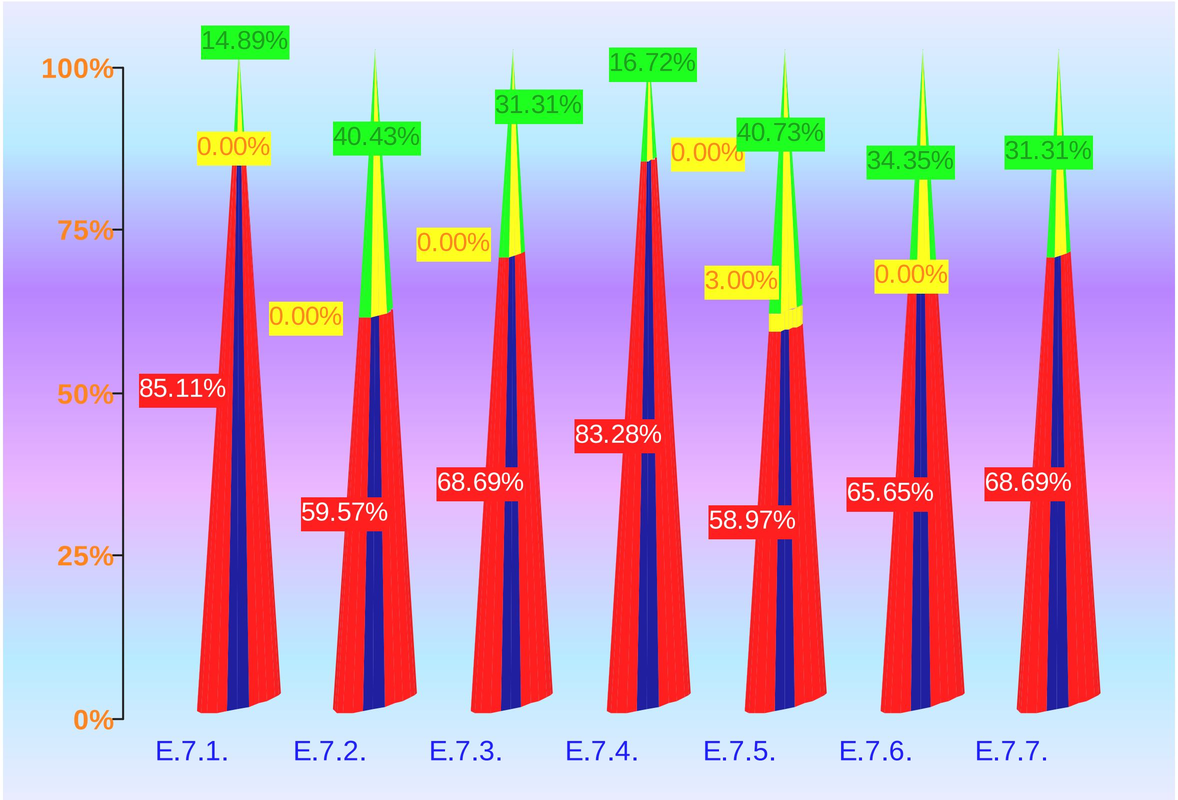
E.5. Does the company have an internal audit operation established as a separate unit in the company?

E.6. Please identify to whom the internal audit function reported?

The next questions examined the quality of the audit committee report in the annual report. They asked whether or not the report contains appropriate information for the consumption of shareholders as well as other stakeholders.

With respect to Questions E.7.1. – E.7.7., we found that the quality of the audit committee report in the annual report of the surveyed firms were all below 40.73 per cent. Therefore, the majority of the firms need to improve the quality of their audit committee report.

OECD Principles 5: Board Responsibility – Monitoring/Control



Assess the quality of the audit committee report in the annual report, which includes the following items:

E.7.1. Attendance

E.7.2. internal control

E.7.3. management control

E.7.4. proposed auditors

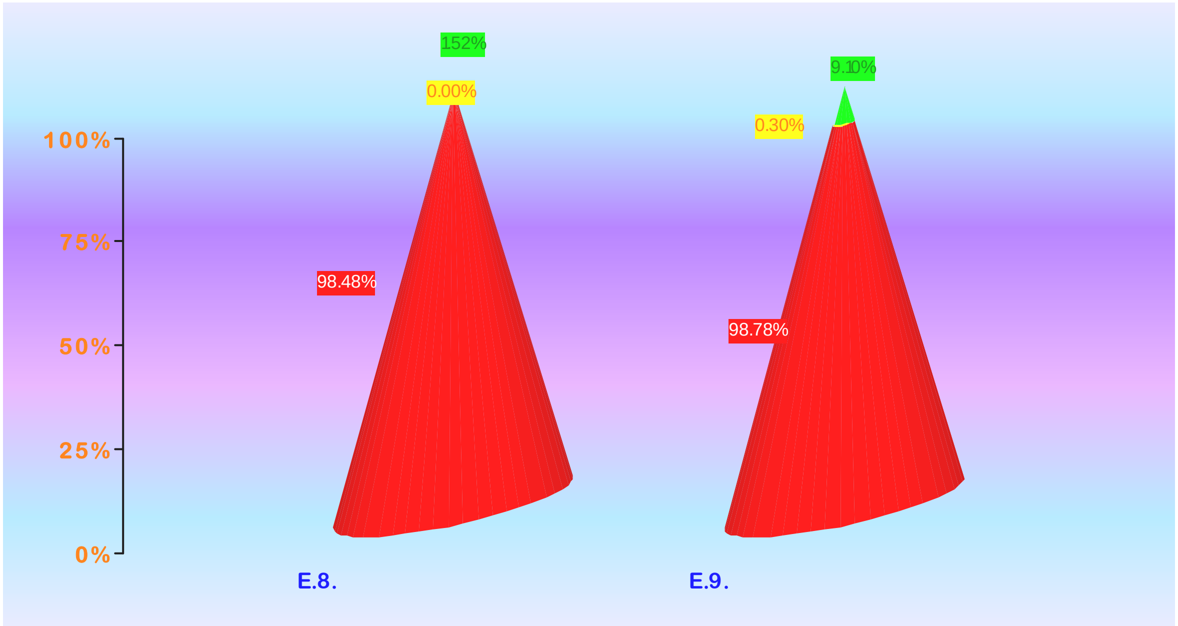
E.7.5. financial report review

E.7.6. legal compliance

E.7.7. conclusion or opinion

Re the assessment of the quality of the audit committee report, we found that the attendance variable received the poorest score. In this respect, only 14.89 per cent of surveyed firms received a good score, while the majority of them (85.11 per cent) received a poor score. A better performance was in the quality of internal control and Financial Report review, where the firms who earned the good score were 40.43 per cent and 40.73 per cent respectively. However, in overall the majority of the companies earned a significantly poor score on all variables in the assessment of quality of the audit committee report: *attendance, internal control, management control, proposed auditors, financial report review, legal compliance, conclusion or opinion* at *85.11 per cent, 59.57 per cent, 68.69 per cent, 83.28 per cent, 58.97 per cent, 65.65 per cent, and 68.69 per cent* respectively.

OECD Principles 5: Board Responsibilities – Monitoring/Control



Assess the board responsibilities variable in terms of the following:

E.8. Does the company provide orientation for newly-appointed directors ?

E.9. Have board members participated in corporate governance training?

Questions E.8. and E.9. assessed the firms' commitment in improving the competence of their board members. With respect to Question E.8., only 1.58per cent of the surveyed firms provided the orientation for their newly-appointed directors to improve their competence and to make the succession process go well. Quite a similar result also applied to Question E.9. In this respect, 98.78per cent of the surveyed companies had never sent their board members to any corporate governance training. Since the board members must have three important characteristics, namely competence, integrity, and motivation (C-I-M),[1] as elaborated by Dr. Gunther of McKinsey, it is imperative that the firms improve the competence of their board members by giving them an orientation and send them to attend a corporate governance training.

> "As fiduciaries who represent a corporation's shareholders, corporate directors have duties of care and loyalty. [We] affirm the value of ongoing director education in fulfillment of these duties. Furthermore, [we] strive to ensure that their actions and decisions meet the highest standards of law and ethics. Through this commitment, [we] serve the general public's need for corporate integrity."
>
> *National Association of Corporate Directors* [2]

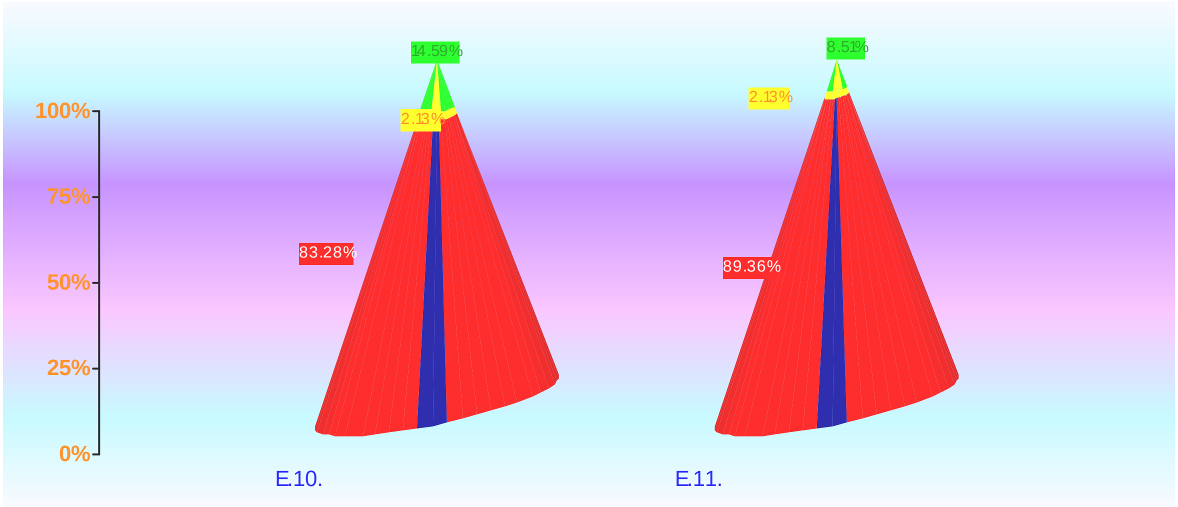
> "The objective of director development is to create a situation for directors where professional and personal growth can occur. This learning situation is likely to involve the acquisition and the increase of knowledge, experience and skills. It may also enable personal qualities to mature."
>
> *Institute of Directors, UK*

---

[1] *Prof. Gunter Dufey Corporate Governance & Financial Reporting Centre University of Michigan & Nanyang Technological University on Corporate Directors & Commissioners Forum 2006 at ShangriLa Hotel-Jakarta 2006*

[2] Global Corpoarte Governance Forum (GCGF)

OECD Principles 5: Board Responsibilities – Monitoring/Control



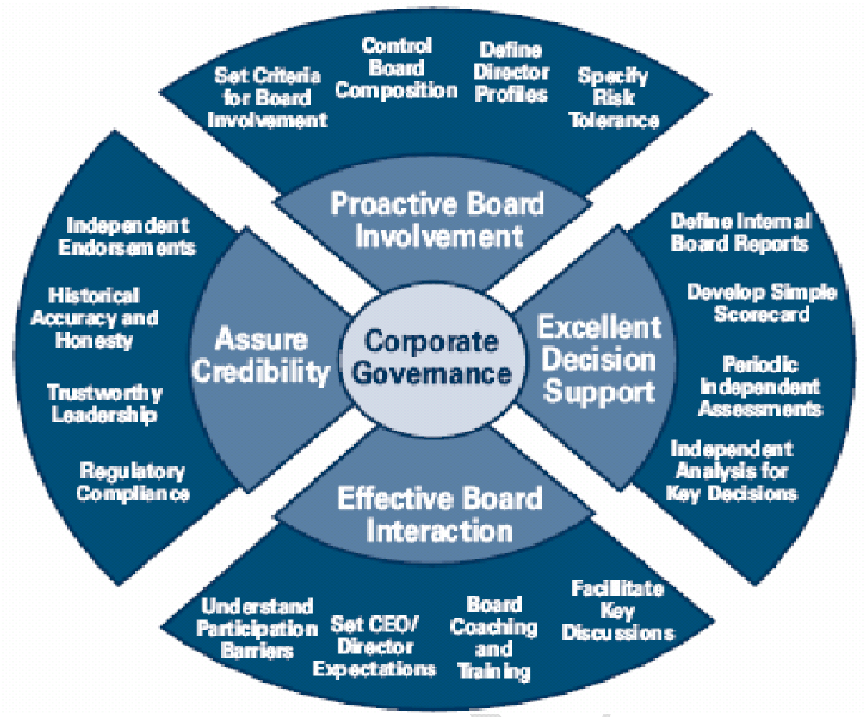
Assess the board responsibilities in terms of the attendance to meetings:

E.10. How many meetings were held in the past year?

E.11. What is attendance record of the board members during the past 12 months?

Questions E.10. and E.11. assessed the board responsibility with respect to the attendance to meetings. The majority of surveyed companies received a poor scored in these two respects, i.e., 83.28 per cent and 89.36 per cent respectively. The firms would therefore need to improve on these two measures by requesting the commitment of their board members in attending the firms' meeting so that they are familiar with the firms' situation and are able to respond to any crisis and make decisions quickly and responsibly as specified in *"TEN (10) Boardroom Challenges"* presented in the OECD ASIA Round Table Meeting in Bangkok last year (13-15 Sept 2006). The NACD framework advocates two out of four independent variables to ensure the implementation of Good Corporate Governance, namely *proactive board involvement*, and *effective board interaction* which serve as the important variables in creating an *excellent decision support* and assuring the *board credibility*.[3]

[3] NACD

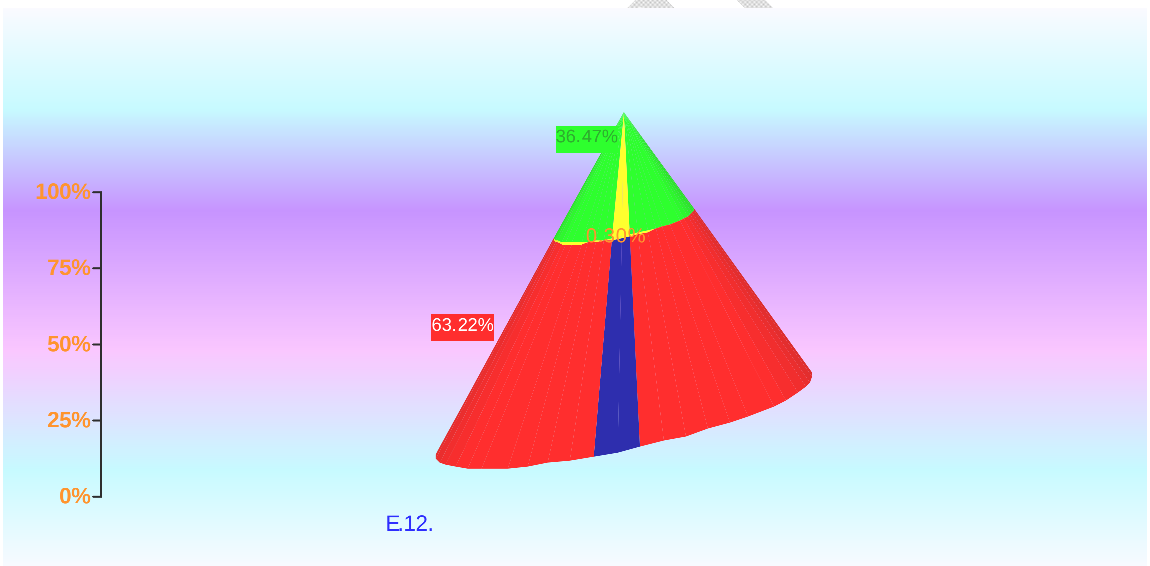


The Role and Board responsibilities in Risk Management provide *Strategic Risk oversight, Stewardship,* and *to link governance to value* through the inception of Best Risk Management policy and practices. The NACD Blue ribbon commission has further mentioned that the board's role is quite simple: *to provide risk oversight, making sure that management has instituted process to identify, and bring to board's attention the major risks that the enterprise faces. It also entails the continual re-evaluation of the monitoring process and the risks with the help of the board and its committees*.[4] The Board is responsible for protecting the company's assets and reputation and promoting the shares value by taking prudent risks, viewing risk on an enterprise-wide basis by understanding the nature of risks inherent in the business, setting up proactive controls for those risks and considering responses for any crisis, and participating in the setting up of a *risk management policy.*

[4] NACD Blue Ribbon Commission on Risk Oversight, Nov 2002

With respect to Question E.12., only 36.47 per cent of the surveyed companies received a good score for providing the risk management policy, while the majority of the firms (63.22 per cent) received a poor score because they did not provide any risk management policy in their annual report. Forty three out of a hundred and twenty companies (35.83 per cent), which received a good score, belonged to highly regulated industries, such as banking, insurance, and multi-finance. It seems that the imposition of regulatory framework by the regulator is indeed necessary to foster the implementation of good principles of risks management.

OECD Principles 5: Board Responsibilities – Monitoring/Control

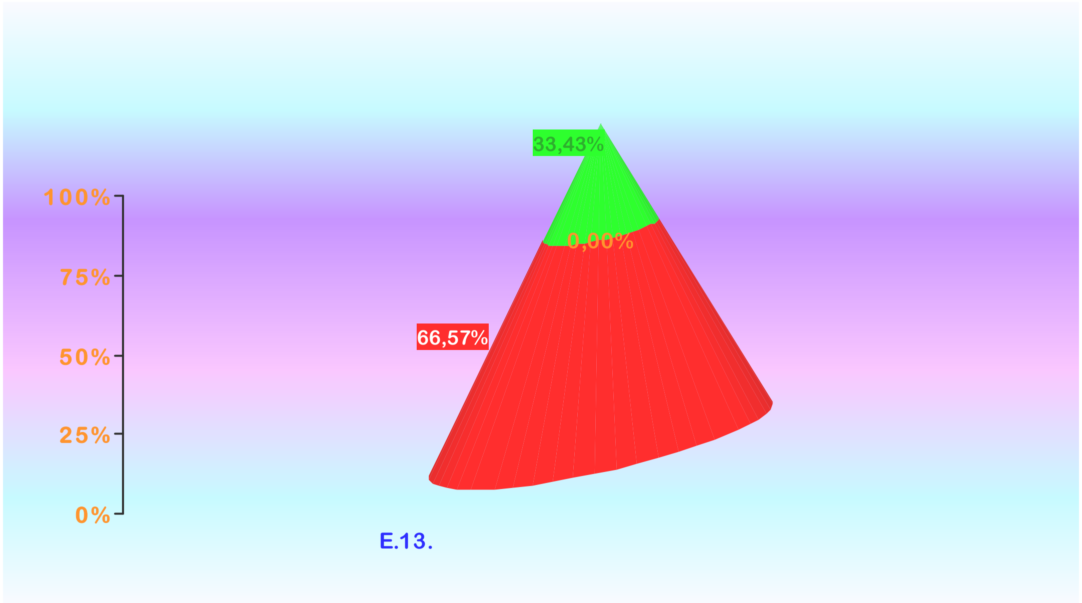


Assess the board responsibilities in terms of the implementation of good principles of risks management:

E.12. Does company provide a risk management policy?

The result derived from Question E.13. has implications for the board effectiveness, which eventually might affect the implementation of corporate governance practices. The result of the assessment showed that the majority of surveyed companies had not clearly distinguished the roles and responsibilities of the BOC and BOD. That is, 66.57 per cent of the firms received a poor score since they did not have a clear governance charter that distinguishes the roles and responsibilities of the BOC and the BOD. The rest of them (33.43 per cent) received a good score for distinguishing the roles and responsibilities of the BOC and the BOD.

OECD Principles 5: Board Responsibilities – Monitoring/Control



Assess whether the board roles and responsibilities have been clearly defined in the governance charter:

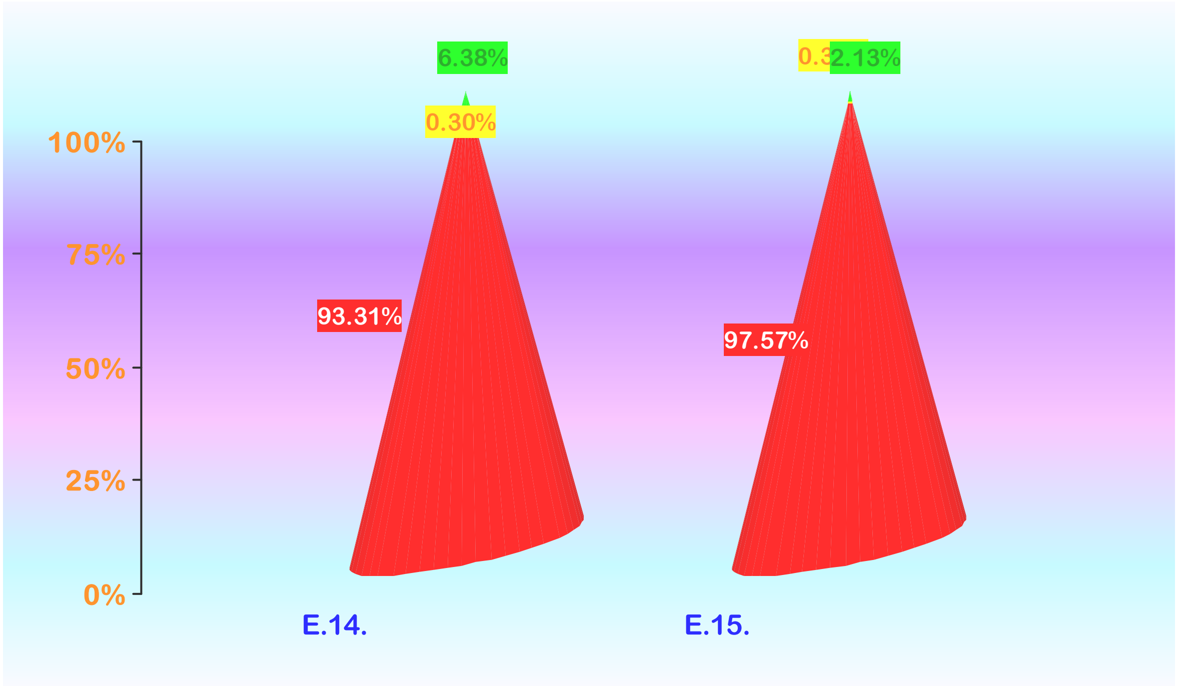
E.13. Does the company clearly distinguish the roles and responsibilities of the BOC and the BOD?

The BOC and the BOD have a number of responsibilities such as *monitoring, overseeing, custodianship, determining the overall strategy and direction, and setting up statutory compliances)*. The board of commissioners (BOC) is to oversee the board of directors (not the company) and the president of the commissioners is responsible for evaluating the performance of the board of Commissioners and for acting as spokesperson of the BOC.

E.2. Board Performance Evaluation

The next series of questions (E.14. and E.15.) were designed to evaluate the board performance of the surveyed companies.

OECD Principles 5: Board Responsibilities – Board Performance Evaluation



E.14. Does the BOC conduct the annual performance assessment of the BOD ?

E.15. Does the board conduct the annual self-assessment ?

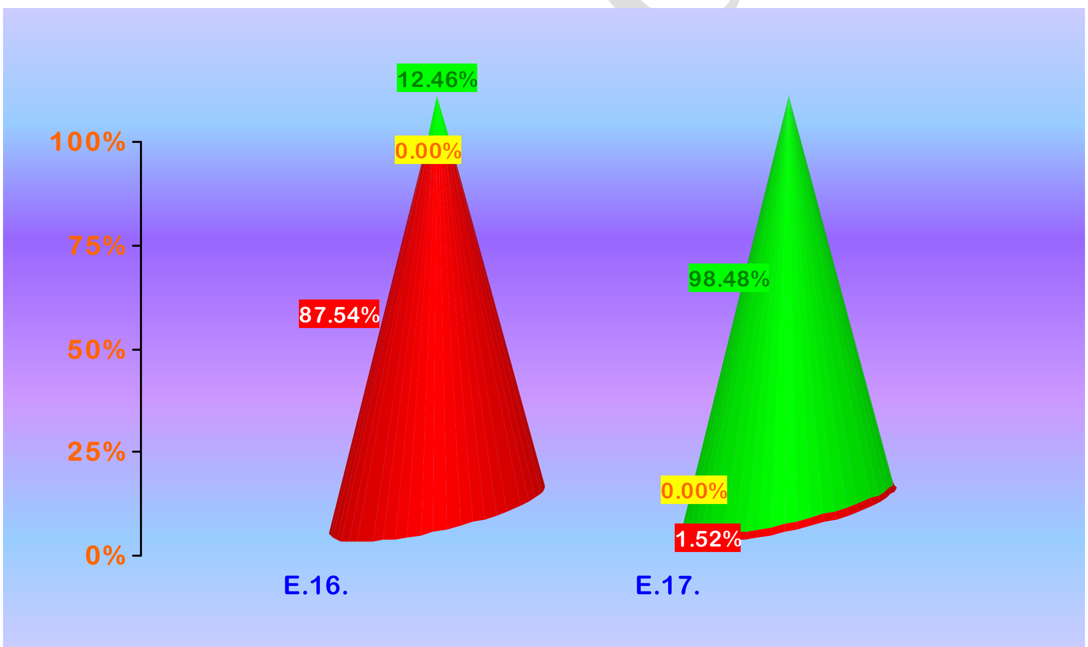
To have an effective board and to ensure the best implementation of Good Corporate Governance require the following: *the right people, the right culture, the right issues, the right information, the right process and the right follow-through.* However, the most crucial factor that determines to the board effectiveness is the first one, i.e., *the right people*. Without it, things can go wrong. To improve of the quality of the board members, a performance evaluation or assessment needs to be implemented, The evaluation can be conducted effectively with the right combination of the following factors: *Timing, Content, Process,* *and Personnel*. Typically, a governance committee designs an initial set of measurable objectives.

With respect to Questions E.14. and E.15., we found that the surveyed companies received a poor score, namely 93.31 per cent for E.14. and 97.57 per cent for E.15. Out of the total 329 surveyed companies, the firms that received a good score in these two respects were only twenty one (6.38 per cent). Eight of these firms belonged to banking, insurance, and multi-finance industries.

E.3. Conflict Of Interest

Questions E.16.- E.20. were designed to assess the potential conflict of interests between the members of board of commissioners, board of directors, and company's objectives.

OECD Principles 5: Board Responsibilities – Conflict of Interest



E.16. Is the chairman an independent commissioner?

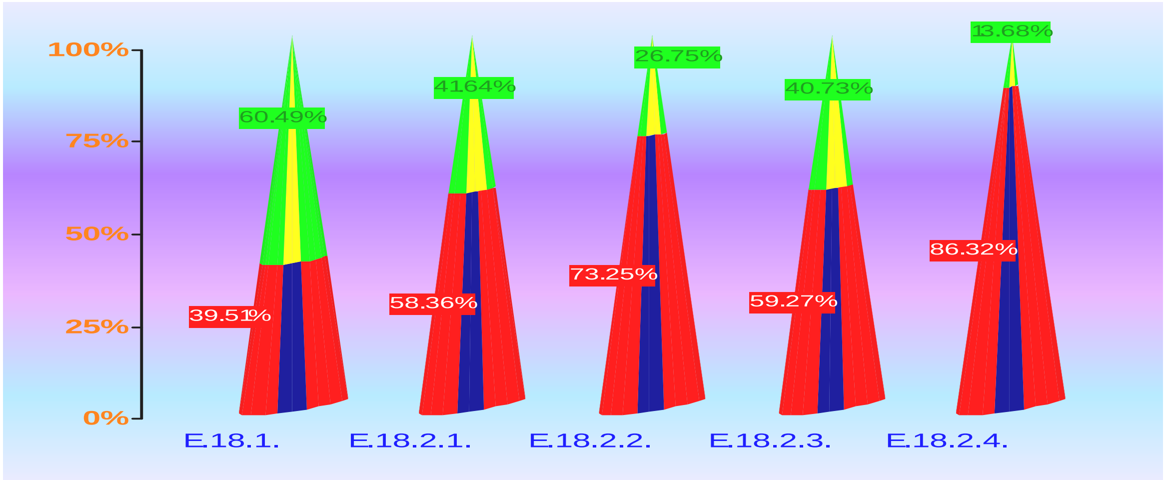
E.17. Is the chairman also a CEO?

According to the OECD principles, the board should prevent the potential conflict of interests by monitoring the performance of the company's management. The implication of this is that there must be a sufficient number of independent commissioners and there is separation of roles between the chairman and the CEO of the company. Furthermore, from the perspective of good corporate governance, the chairman must act as an independent commissioner.

With respect to Question E.16., we found that the board practices of the surveyed firms as measured by the chairman as an independent commissioner were still insufficient for being characterized as good corporate governance practitioners. As the figure indicates, 87.54 per cent of observed companies received a poor score, and only 12.46 per cent received a good score. With respect to Question E.17., almost all surveyed companies gave outstanding performance, that is, all companies received a good score. However, the result was to be expected due to the Indonesian law which prohibits the dual structure of the board composition.

As stated previously, the board independence is a requirement for the board in order to be able to exercise its fiduciary duties to the company and to the minor shareholders effectively. .

OECD Principles 5: Board Responsibilities – Conflict of Interest



E.18.1. Does the board appoint an independent audit committee with independent members?

E.18.2.. If yes, are the following items (E.18.2.1 – E.18.2.4) disclosed?:

- E.18.2.1. Charter/role and responsibilities
- E.18.2.2. Profile/qualifications
- E.18.2.3. Independence
- E.18.2.4. Performance/Attendance

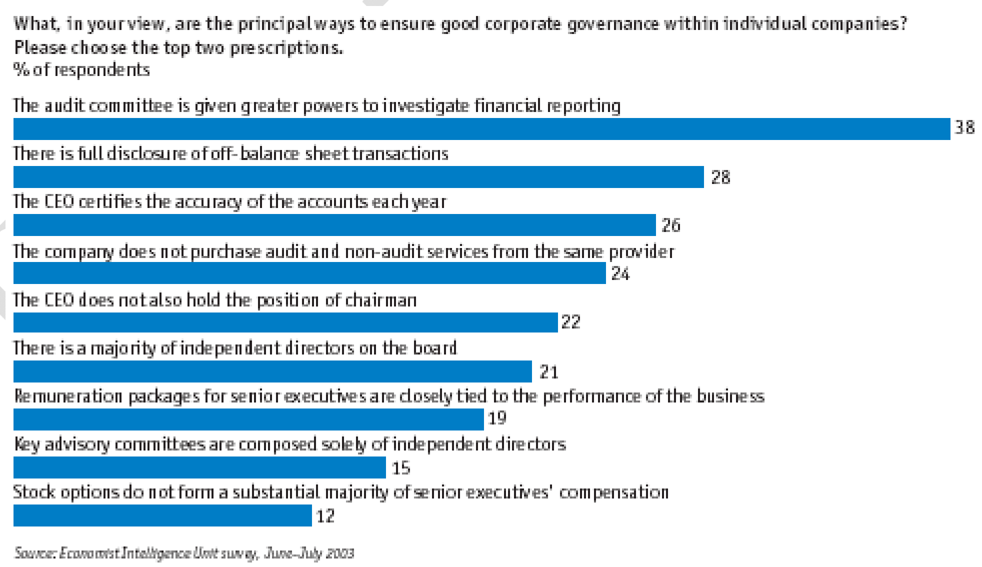
With respect to Question E.18.1., we found that that the majority of surveyed companies (60.49 per cent) had established their independent audit committee staffed with independent directors. However, 39.51 per cent of them received a poor score for not establishing their independent audit committee, thereby violating the publicly-listed companies' law which requires the establishment of an independent audit committee.

With regards to Questions *E.18.2.., E.18.2.2.*, *and E.18.2.3.*, we found that the majority of surveyed companies received a poor score, namely 58.36 per cent, 73.25 per cent, 59.27 per cent, and 83.25 per cent respectively.

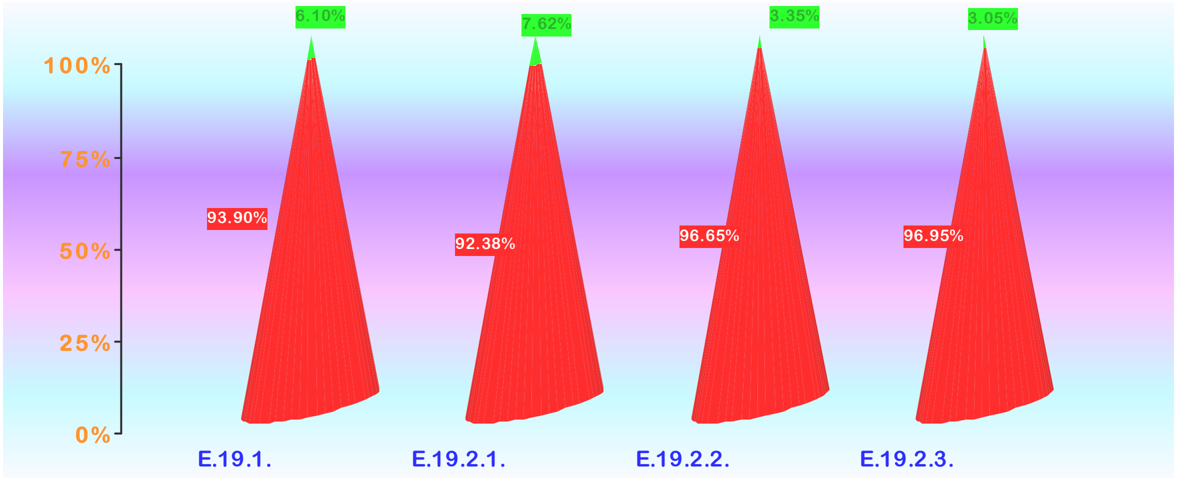
With respect to Question E.19.1., only a small number of surveyed companies (6.10per cent) received a good score, meaning that these companies appointed a compensation committee, chaired by an independent commissioner, with most or all of the committee members being non-executive directors. The rest of them received a poor score. Quite a similar result also applied to Questions E.19.2.1, E.19.2.2., and E.19.2.3. That is, in three respects, the majority of surveyed companies received a poor score, namely 92.38 per cent, 96.65 per cent, and 96.95 per cent respectively.

This Commission recommends a compensation philosophy and related practices that reflect the principles of independence, fairness, long-term shareholder value, link to performance, and transparency.

NACD Blue Ribbon Commission



OECD Principle 5: Board Responsibilities – Conflict of Interest



E.19.1. Does the board appoint a compensation committee, chaired by an independent commissioner, with most or all of the committee members being non-executive director

E.19.2.. If yes, are the following items (E19.2.1 – E.19.2.3) disclosed?:

E.19.2.1. Charter/roles and responsibilities

E.19.2.2. Independence

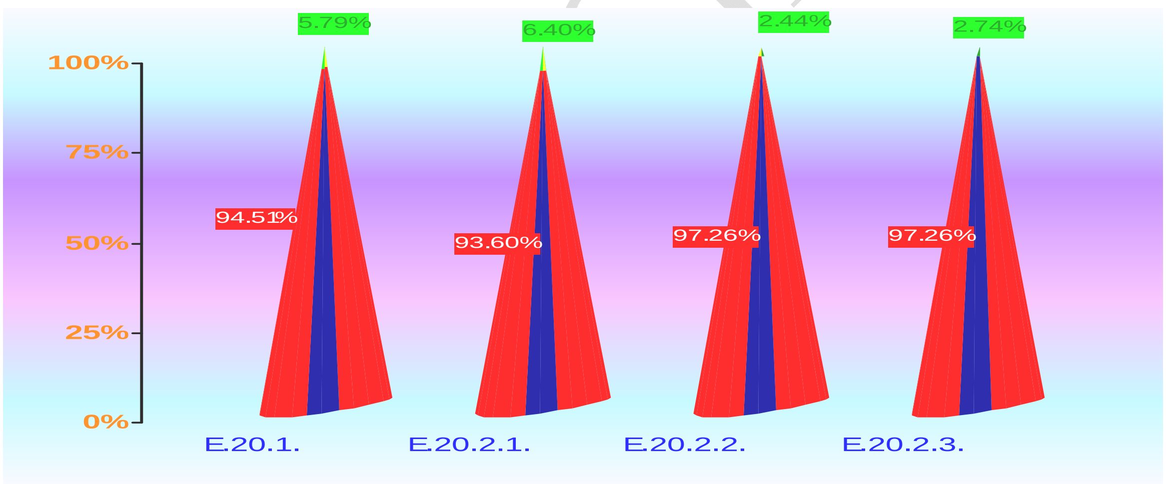
E.19.2.3. Performance/attendance

The compensation committee determines the compensation policy, reviews the CEO's goals and performance, and evaluates the CEO compensation such as salary, incentive and equity-based awards, compensation for elected officers and directors, etc.

Starting from 2002, Indonesian Security & Exchange Committee (SEC) - Bapepam has been actively involved in promoting the implementation of Good Corporate Governance principles. . As an effort to boost the implementation of Good Corporate Governance Principle, the draft of the capital market law amendment contains a provision which requires issuers and public companies to appoint independent commissioners, independent directors, audit committees, and corporate secretaries. Most of the issuers listed in the JSX had already appointed independent commissioners and audit committees to comply with the law. However, as for the compensation committee, the result was what we saw in the previous description.

With respect to Question E.20.1., we found that only a small number of surveyed companies (5.79 per cent) received a good score, meaning that these firms appointed a nomination committee, chaired by an independent director, with the majority or all of the committee members being non-executive directors. The rest received a poor score. Quite a similar result also applied to Questions E.20.2.1, E.20.2.2., and E.20.2.3. That is, in three respects, the majority of surveyed companies received a poor score, namely 93.60 per cent, 97.26 per cent, and 97.26 per cent respectively.

OECD Principles 5: Board Responsibilities – Conflict of Interest



E.20.1. Does the board appoint a nomination committee, chaired by an independent director, with most or all of the committee members being non-executive directors?

E.20.2.. If yes, are the following items (E.20.2.1 – E.20.2.3) disclosed?:

- E.20.2.1. Charter/roles and responsibilities
- E.20.2.2. Independence
- E.20.2.3. Performance/attendance

In the compulsory two-board system, the majority owner or the chosen relative usually occupies the post of executive president. Majority owner may choose a non-related executive to chair the Executive Board and/or the Supervisory Board, but the chosen professional must have demonstrated an unquestionable loyalty to the majority owner…**(Dr. Djisman Simanjuntak - IICD)**[5]

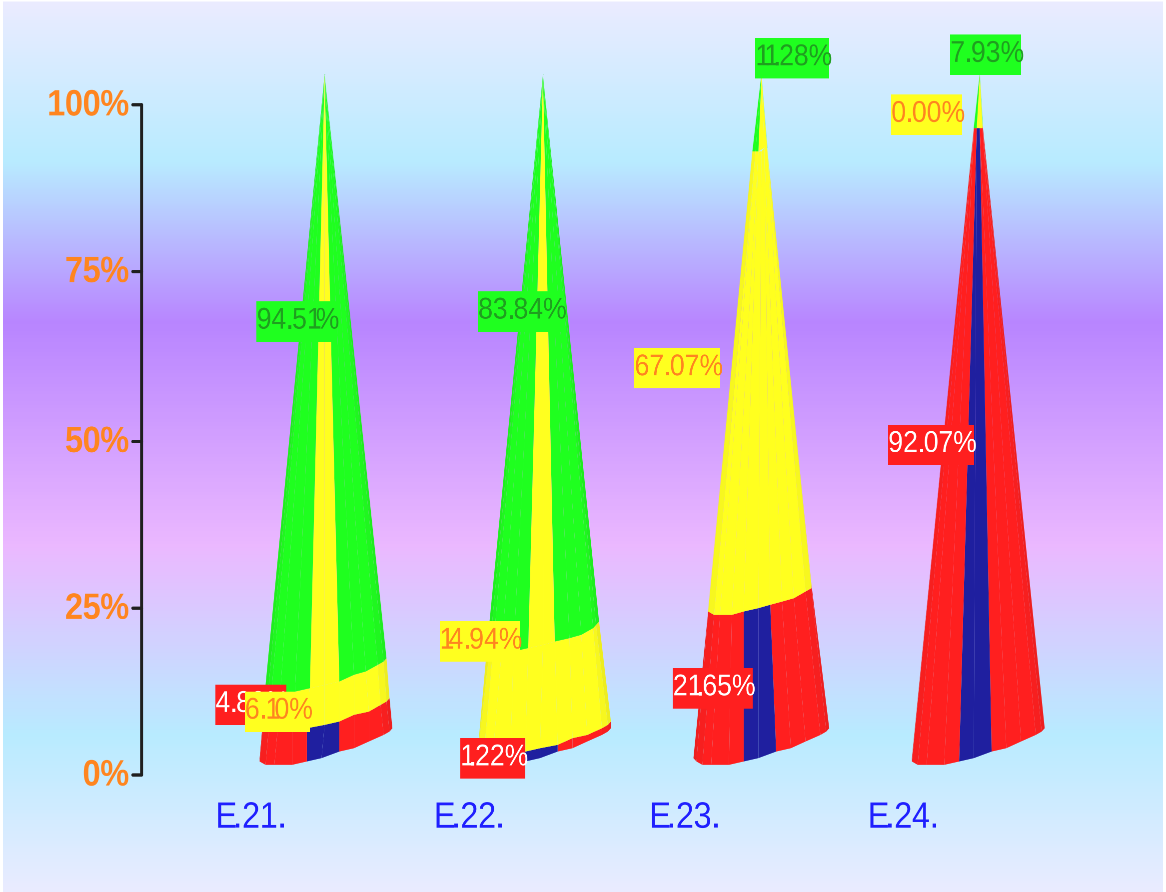
In the section that follows, we describe the assessment for the composition of the board of commissioners (Questions E.21. – E.24.)

E. 4. Board Composition

Research shows that the size of the board will affect the corporate performance. In Indonesia, the board size is small, i.e., consisting of 2-4 BOC and 4-5 BOD on average. In the USA, which adopts the single board system, the number of executive and non-executive directors within one company could reach 12-17 people, while in Australia the average is 6,5 people. A board that is too big or too small will affect the corporate performance, so the most appropriate size of board members needs to be determined to obtain an optimal function. Unfortunately, there is no exact formula that can be used to determine the size of the board.

[5] Dr. Djisman S. Simanjuntak: " GCG in POST CRISI Indonesia

OECD Principles 5: Board Responsibilities – Board Composition



E.21 What is the size of the board of commissioners?

E.22. How many board members are non-executive directors?

E.23. Within the board of commissioners, how many of them are independent commissioners?

E.24. E.20 Does the company state in its annual report the definition of independent commissioners?2.2.

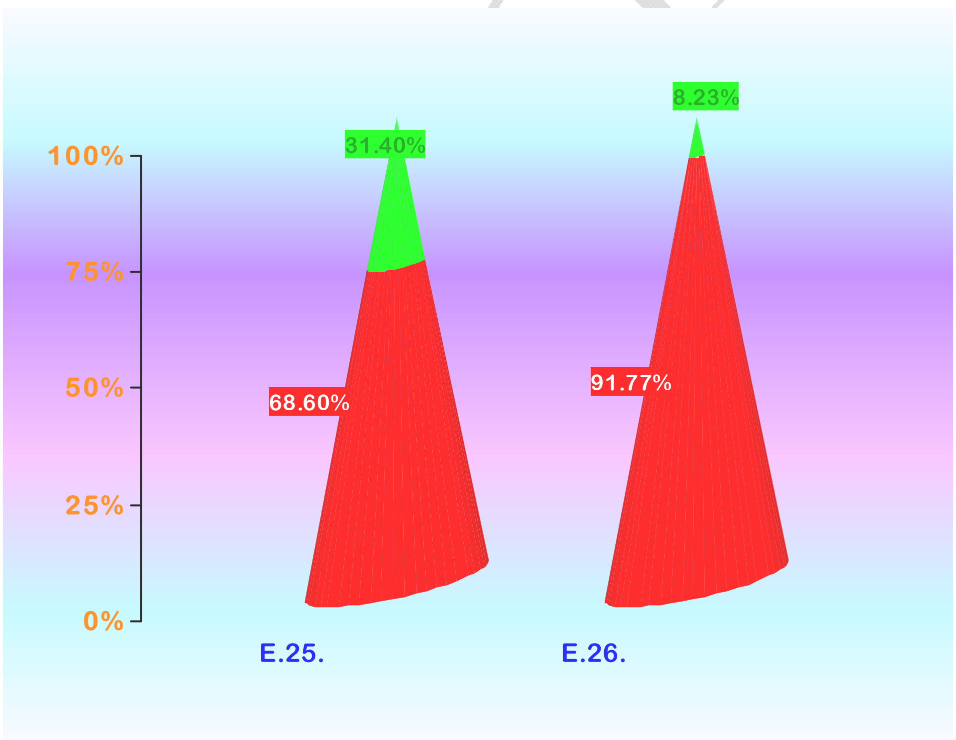
With respect to Questions E.21. and E.22., we found that the majority of surveyed companies (94.51 per cent and 83.84 per cent respectively) received a good score, meaning that such companies had a good size of commissioners/non-executive directors. However, with respect to Question E.24., we found that the majority of surveyed companies (67.07 per cent) received a poor score due to the small number of independent commissioners they had, while the rest (11.28

per cent) received a good score. With respect to Question E.25., we found that the majority of the firms (92.07 per cent) did not provide the definition of "independent" commissioners in their annual report. Only a handful of companies (7.93per cent) received a good score in this respect.

E.5. Communication and Bonus

The next questions, E.25. and E.26., were originally meant to be placed at the *Monitoring/Control* and *Conflict of Interests* sections respectively. However, the terms were more suitably included in the *Communication and Bonus* section.

OECD Principles 5: Board Responsibilities – Communication and Bonus



E.25. Does the company have a separate board of commissioner's report describing their responsibilities in reviewing the firm's financial statement?

E.26. The company provides an option scheme to encourage the top management with an exercise period over three years and an exercise price above the market value

With respect to Question E.25., we found that that the majority of firms (68.60 per cent) received a poor score, thereby indicating that the majority of the firms did not have a separate board of commissioner's report describing their responsibilities for reviewing the firm's financial statement.

The majority of the surveyed firms (91.77 per cent) also received a poor score for Question E.26., because most of them did not provide an option scheme that encourages top management performances. We also found that 8.23per cent out of 48.15 per cent of the companies that received a good score were from the services industries. Such industries showed the need for the availability of the punishment and reward mechanism in order to succeed in a fiercely-competitive market.

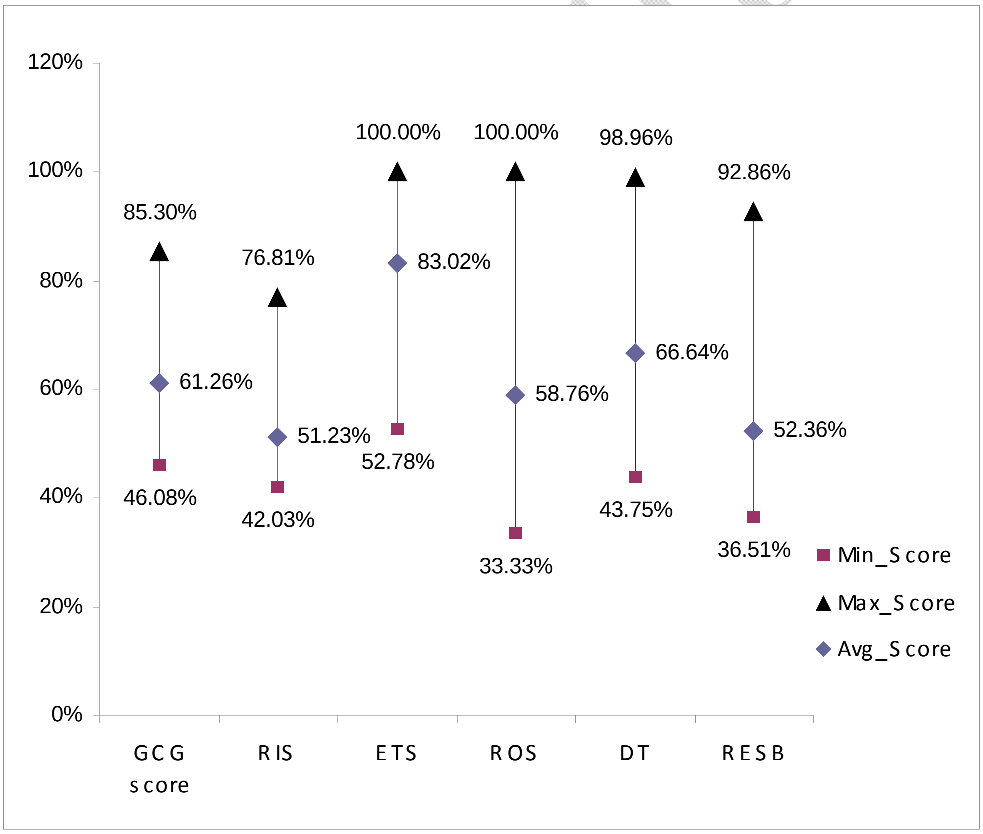
IV. ANALYSES

A. Corporate Governance Performance

A.1. Overall Performance

It is worth noting that the main purpose of this corporate governance scorecard assessment is meant to improve good corporate governance practices in Indonesia by providing a comprehensive picture of the practices by the Indonesian public-listed companies. Figure 1 shows the corporate governance performance in terms of the five OECD principles and overall mean scores (Avg Score).

Figure 1: Corporate Governance Performance



The overall mean score for all public-listed companies was 61.26 per cent. On average, the surveyed companies complied with the regulatory requirements. In this respect, some companies achieved the highest score (85.30 per cent) and some of them obtained the lowest score (42.08 per cent).

If we consider all the OECD principles on good corporate governance, we can see that the implementation of the rights of shareholders was the worst (mean score = 51.23 per cent), followed by the implementation of responsibility of the boards (mean score = 52.36 per cent). The role of stakeholders was also not well implemented by the surveyed firms (mean score = 58.76 per cent). The second principle, i.e., equitable treatment of shareholders, and the fourth principle, i.e., disclosure and transparency, were implemented above the overall mean score.

When comparing the corporate governance scores in 2005 with those in 2004, it can be stated that there was a slight decrease in corporate governance performance, i.e., from 67.37 per cent in 2004 to 61.26 per cent in 2005 with respect to the overall mean score. However, it should be noted that there are significant differences between the two studies:

a. The 2005 study used a more stringent instrument consisting of 117 assessment items compared with 86 items in the 2004 study.

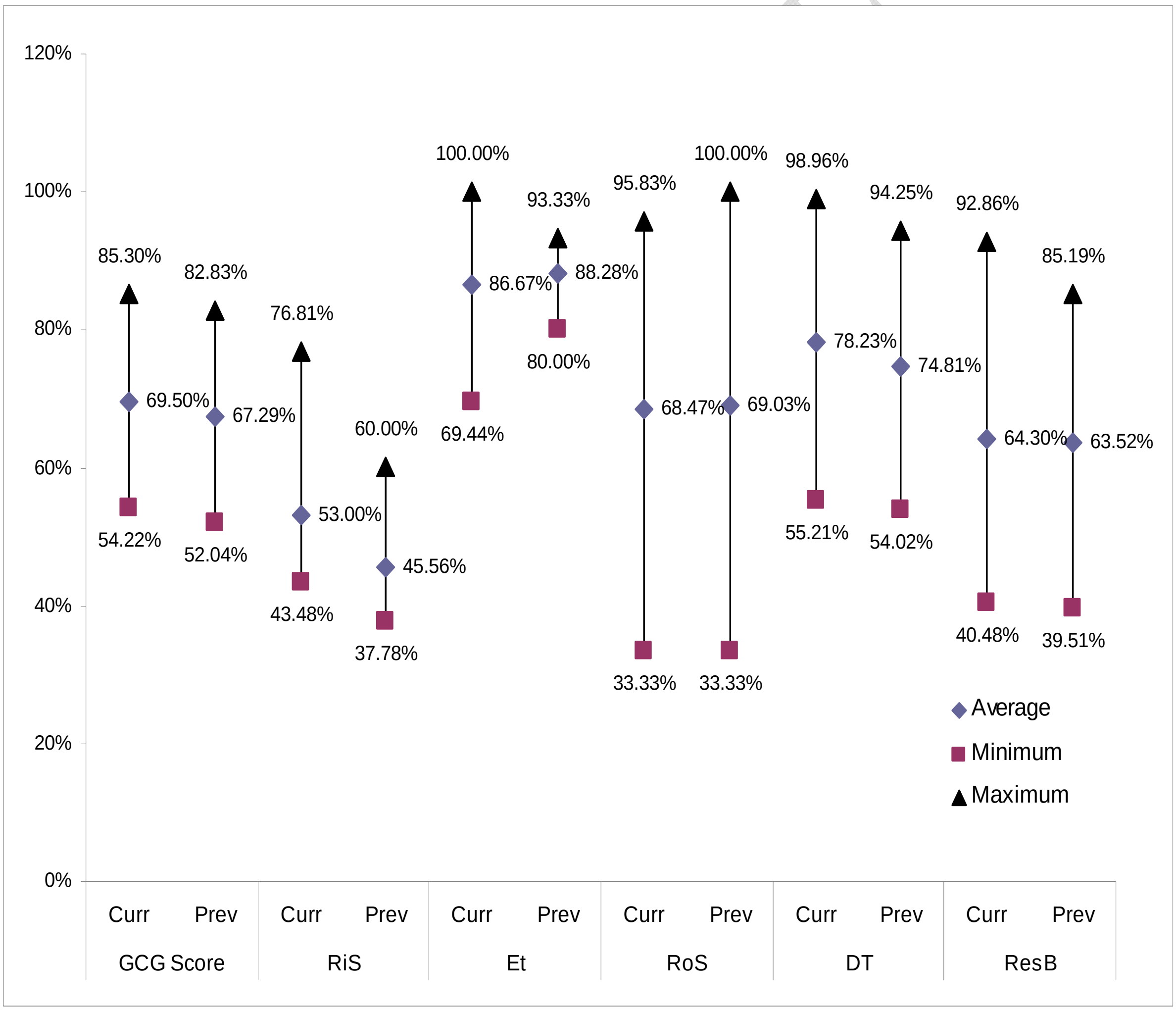
b. The 2005 study involved all public-listed companies, including the low- performance firms, while the 2004 study only involved 61 leading public-listed companies.

It should also be noted that the 2005 assessment study provided a more realistic picture of corporate governance performance of the Indonesian public-listed companies.

A.2. Performance Comparison for Sixty Leading Companies

A better implementation of corporate governance practices was shown by sixty leading companies, as shown in Figure 2. The overall mean score of 2005 study for sixty leading companies was 69.50 per cent. There was a slight improvement when compared with the overall mean score of the 2004 assessment study for the same companies, which reached 67.29 per cent. A significant improvement in the rights of shareholders indicated that investors in these leading companies were better informed compared with those in the previous study. Improvement also occurred in the other two pillars of good corporate governance, namely disclosure and transparency and board responsibility.

Figure 2: The 2004 and 2005 Studies Comparison (N = 60)



Note: One out of 61 companies in the 2004 study was not included in the 2005 study. This explains why the number of firms to be compared was 60 and the overall mean score for 2004 study was 67.29 instead of 67.37.

B. Corporate Governance and Economic Performance

To analyze the relationship between the corporate governance and the company performance, we used the Spearman correlation test. In this test, the corporate governance score was translated into a dummy variable, i.e., 1 for high score and 0 for low score. The overall mean score was used as a critical point to determine high versus low scores. The scores above and equal to the overall mean score were categorized as high and scores below the overall mean were treated as low.

The company economic performance was measured by Tobin's Q. Tobin's Q, used to measure the market performance of company's outstanding stocks, represents the ratio between the market value of equity plus firm debt divided by the book value of total assets. The association between the corporate governance score and the market valuation (Tobin's Q) is summarized in the table below:

Correlations

			GCGPERF	TOBINS
Spearman's rho	GCGPERF	Correlation Coefficient	1.000	.187**
		Sig. (2-tailed)	.	.001
		N	329	329
	TOBINS	Correlation Coefficient	.187**	1.000
		Sig. (2-tailed)	.001	.
		N	329	329

**. Correlation is significant at the 0.01 level (2-tailed).

The correlation between the corporate governance score and Tobin's Q was very weak (r = 0.187) since the significant correlation was at the 0.01 level. This weak correlation, however, provided a signal for the importance of good corporate governance since the investors were willing to pay a premium for well-managed corporations.

C. *Industry Analysis*

As shown in Table 4 below, the corporate governance score varied with respect to the types of industry assessed. The mining industry reached the highest score (i.e., 72.38 per cent), followed by the banking industry, which reached 70.70 per cent. Other firms, which performed above the overall mean score (i.e., 61.62 per cent), included pharmaceutical industry, retail industry, and telecommunication and IT industry. The majority of industries performed below the overall mean performance. We also found that the majority of surveyed firms (56.84 per cent) performed below the overall mean score and only 43.16 per cent of them performed above the average.

Table 4: Corporate Governance Score In Terms of Industry types

Industrial Type	Mean Score	Min. Score	Max. Score
Agribusiness	59.29 %	46.27 %	69.63 %
Banking	70.70 %	58.21 %	83.65 %
Chemical	57.60 %	46.08 %	66.86 %
Financial investment	60.17 %	47.04 %	76.57 %
Food	57.26 %	48.07 %	70.46 %
Insurance	58.52 %	52.80 %	63.95 %
Mining	72.38 %	52.66 %	85.30 %
Packaging	59.79 %	56.23 %	65.19 %
Pharmaceutical	62.21 %	50.75 %	75.76 %
Property & Construction	60.19 %	48.60 %	78.03 %
Pulp	58.40 %	48.99 %	63.87 %
Retail	61.65 %	53.97 %	70.73 %
Steel	57.26 %	52.91 %	62.59 %
Telecommunication & IT	64.22 %	54.15 %	80.38 %
Textile	58.01 %	53.27 %	64.45 %
Trading	57.86 %	48.20 %	72.20 %
Transportation	60.11 %	54.50 %	65.62 %
Wood	63.39 %	54.24 %	71.20 %
Others	60.40 %	47.47 %	78.10 %

It is worth noting that high performance was usually associated with highly-regulated companies, such as banks and state-owned enterprises (SOEs). We found that such companies received a higher score than the non-highly-regulated companies, i.e., the majority of them performed above the overall mean score, as shown in Table 5.

Table 5: Corporate Governance Score for banks and SOEs

CG Score	Banks N = 23	SOEs N = 15	Total Firms N = 329
Above Overall Mean Score	21	14	142
Below Overall Mean Score	2	1	187

Note: The Overall Mean Score for 329 companies was 61.62 per cent

Table 5 indicates that 21 banks (i.e., 91.30 per cent) and 14 SOEs (93.33 per cent) performed above the overall mean score (i.e., 61.62 per cent) compared with 43.16 per cent for all companies. A similar result was also found in the 2004 assessment study in which the majority of the banks and SOEs performed above the overall mean score.

When comparing the banking corporate governance performance in two consecutive studies for the same banks (i.e., nine banks), we found that there was an improvement in their performance, i.e., from 74.91 per cent to 78.00 per cent, as seen in Table 6 below.

Table 6: Did Banks Improve Their Corporate Governance performance?

Year Of Study	Number of Companies	Corporate Governance Score
2004	9	74.91
2005	9	78.00

Note: There were only nine companies in the first scorecard assessment (2004)

The top twenty performers in 2005 were also dominated by Banks and SOEs, as shown in Table 7. Seven out of twenty companies (or 35 per cent of the top twenty companies) were banks, while eight out of twenty companies (or 40 per cent) came from state-owned enterprises. The top twenty companies in 2004 also represented the top twenty companies in 2005.

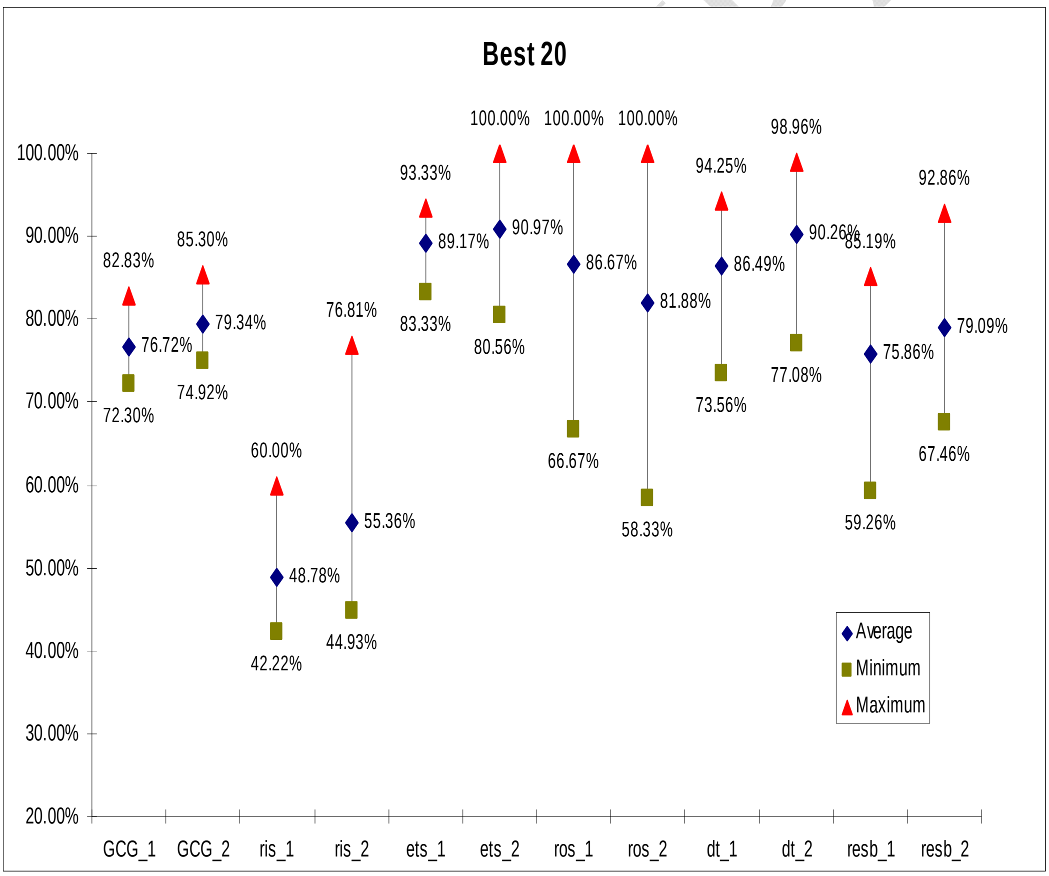
Table 7: The Top Twenty Companies (2004 vs 2005)

2005 Study		2004 Study	
Company Name	**CG Score**	**Company Name**	**CG Score**
Aneka Tambang	85. 30 %	Bank Rakyat Indonesia	82.83 %
Medco Energi International	84.60 %	Indosat	81.00 %
Bank NISP	83.65 %	Perusahaan Gas Negara	79.06 %
Bank Niaga	83.06 %	Astra International	78.63 %
Tambang Batubara Bukit Asam	81.37 %	Aneka Tambang	78.51 %
Bank Danamon	80.76 %	PT Timah	78.11 %
Telekomunikasi Indonesia	80.38 %	Telkom Indonesia	77.08 %
Bank Rakyat Indonesia	80.14 %	Tambang Batubara Bukit Asam	77.05 %
Indosat	80.01 %	Bank Central Asia	77.01 %
Bank Mandiri	79.68 %	Unilever Indonesia	76.38 %
Bank Central Asia	79.52	Medco Energi International	76.05 %
Astra International	78.10	Semen Gresik	75.73 %
Adhi Karya	78.03	Trimegah Sekuritas	75.63 %
Apexindo Pratama Duta	77.36	Adhi Karya	75.63 %
Citra Marga Nushapala	77.07	Bank Danamon	75.09 %
Adira Dinamika Multi Finance	76.57	Bank Mandiri	75.08 %
Kimia Farma	75.76	Bank Niaga	74.88 %
Bank Permata	75.45	Bank International Indonesia	74.23 %
Bakri Sumatra Plantation	74.98	International Nickel Indonesia	74.14 %
International Nickel Indonesia	74.92	Bumi Resources	72.30 %

Table 7 above also reveals that there was improvement with respect to the scores achieved by the top twenty companies for each rank in 2005 compared with that in 2004. Antam, for instance, in which occupied the first rank in 2005, achieved 85.30 per cent, while Bank Rakyat Indonesia, which occupied the first rank in 2004, reached 82.83 per cent.

The improving performance with respect to the overall and individual OECD principles, except for the role of stakeholders, was also shown by the top twenty companies, as shown in Figure 3.

Figure 3: 2005 Vs 2004 Top Twenty Performance by Overall and Individual OECDPrinciples

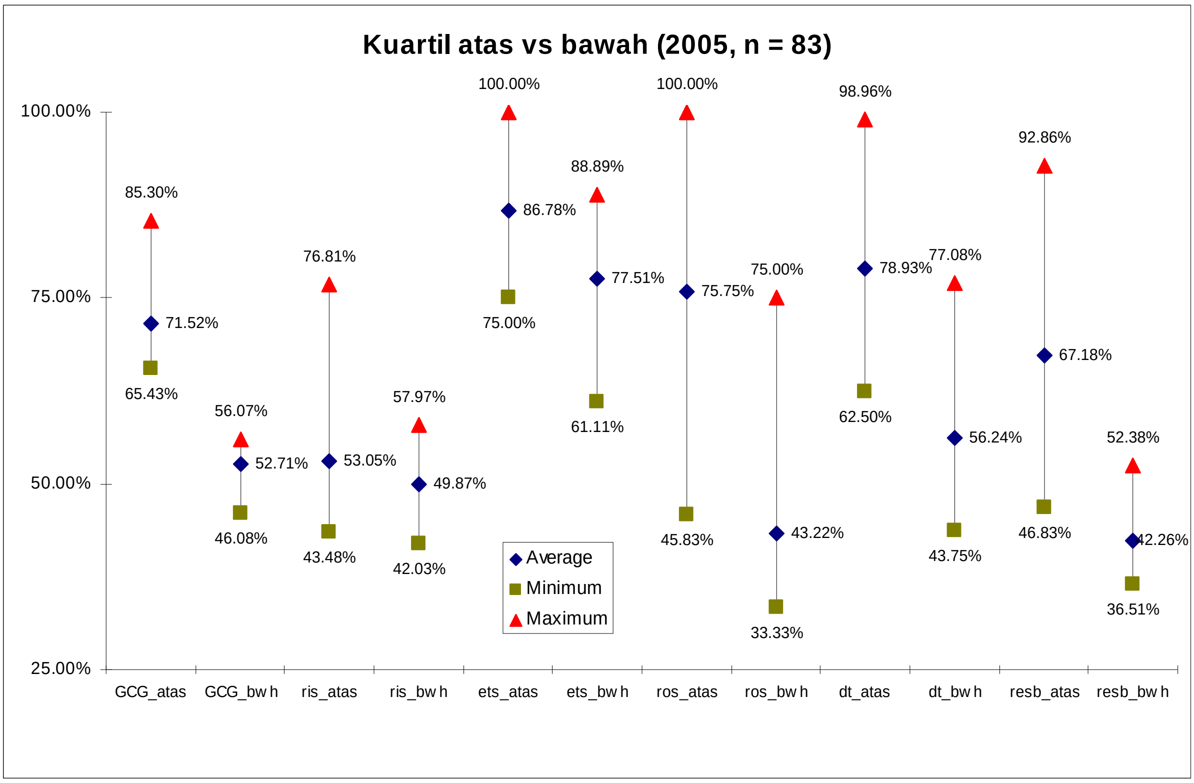


Overall, the corporate governance score attained by the top twenty companies increased from 76.72 per cent to 79.34 per cent (overall mean score). The overall minimum and maximum scores also increased, as shown in Figure 3. In 2005 study, the performance of rights of shareholders increased 6.58 per cent, equitable treatment of shareholders increased 1.80 per cent, role of shareholders decreased 4.79 per cent, disclosure and transparency increased 3.77 per cent, and responsibilities of the board increased 3.23 per cent. Although the performance of stakeholders' role decreased in 2005, the percentage was still much better than the performance of shareholders' rights. However, the performance of stakeholders' rights might improve in the future because of the presence of a new company law that requires firms which exploit natural resources to implement corporate social responsibility.

Top and Bottom Quartile

The corporate governance performance between the top-quartile and the bottom-quartile firms was significantly different both in terms of the overall performance and the individual OECD principles performance, as seen in Figure 4. Overall, the corporate governance performance of the top quartile firms reached 71.52 per cent, which was far above the bottom quartile firms that reached only 52. 07 per cent. Except for the equitable treatment of shareholders, the other four individual OECD principles were performed below the minimum regulatory requirement (i.e., below 60.00 per cent). This means that the bottom-quartile firms had not shown enough commitment to implement good corporate governance practices. Why was the performance of equitable treatment of shareholders of the bottom-quartile firms far above the other principles? One possibility was that the majority of questions related to the OECD principles (i.e., 8 out of 12 questions) were of regulatory types. The voluntary-related items, however, were poorly performed. A special attention needed to be given to the bottom-quartile firms in order to improve their corporate governance performance. In this respect, the IICD can provide assistance to such companies if they are committed to good corporate governance practices.

Figure 4: The Top-Quartile Vs the Bottom-Quartile Performance



Note: GCG_atas = Top Quartile; GCG_bwh = Bottom Quartile

D. IDEA Net Comparison

Table 8 below shows the comparison in corporate governance performance between Indonesia and Thailand.

Table 8: Indonesia Vs Thai Comparison of Corporate Governance Score

Description	Indonesia			Thailand		
	Mean	Max.	Min.	Mean	Max.	Min.
Overall	61.26	85.30	46.08	68.8	92.2	45.1
Rights Of Shareholders	51.23	76.81	42.03	65.8	97.4	37.0
Equitable Treatment	83.02	100.00	52.78	74.5	97.4	51.3
Role of Stakeholders	58.76	100.00	33.33	43.2	100.0	0.0
Disclosure & Transp.	66.64	98.96	43.75	83.1	97.1	48.0
Board Responsibility	52.36	92.86	36.51	53.5	92.0	22.6

Overall, the performance of corporate governance in Thailand was slightly better than that in Indonesia (i.e., the overall mean score in Indonesia was 61.26 per cent and 68.8 per cent in Thailand). There were two major factors responsible for better implementation of corporate governance in Thailand. First, Thailand had been able to better identify areas for improvement based on its experience from four consecutive studies, while Indonesia had only conducted two consecutive studies. Second, Thai companies received a big support from the Stock Exchange and the Securities and Exchange Commission of Thailand, and an endorsement from the National Corporate Governance Committee of Thailand.

V. CONCLUSIONS AND RECOMMENDATIONS

A. Conclusions

a. Rights of Shareholders

1. In spite of improvement in the implementation of the rights of shareholders by surveyed companies compared to that found in previous study, the shareholders still need to be well-informed about their rights. The surveyed companies did not clearly define and appropriately disclose the shareholders' rights. Some implications of these inappropriate practices might be as follows:

   a. It is hard to see how shareholders could participate effectively at annual general meetings. The surveyed companies did not pay a particular attention to the shareholders' rights and the situation was worsened by the absence of CEO, Chairman of BOC, and Chairman of other committees.

   b. The interests of the directors (BOD and BOC) might prevail when the shareholders were not facilitated and not well-informed about their basic rights. It seems that the shareholders were treated as the residual claimants of the companies. Such improper behaviors might result in excessive executive compensation, the absence of effective exercise of BOC's fiduciary duties in protecting shareholders, etc.

2. The unavailability of information about the AGM minutes provided a significant contribution to the poor implementation of rights of shareholders. Although BAPEPAM (SEC of Indonesia) requires that the report of the AGM results be

submitted to the commission, but minutes of meetings were not publicly available.

b. Equitable Treatment of Shareholders

1. The highest score among the five OECD principles on good corporate governance attained by subject companies was one on the principle of equitable treatment of shareholders. Although there was a slight decrease in the performance, we believed that it was caused by the use of a more stringent instrument and the inclusion of the low-performance companies.

2. An interesting finding of this study was that the excellent performance on certain assessment items might be attributed to of the existing laws and regulations. The majority of the assessed items, such as share vote, insider information, related-party transactions, sanctions, and proxy voting, were highly regulated either by the corporate law, BAPEPAM, or the Central Bank of Indonesia and other regulatory bodies. In the meantime, the items which had to be voluntarily implemented were poorly performed.

c. Role of Stakeholders

There was a tendency that the boards of surveyed companies acted for their own interests. This tendency seemed to be confirmed by the performance results of the role of stakeholders. Similar to what happened with the rights of shareholders, the surveyed companies tended to ignore the rights of other stakeholders. Simply complying with the law, for example providing the rights of employees as required by the law, seemed to be a common practice. In other words, it appeared that the laws and regulations had a more profound impact rather than the benchmarking against the best practices.

d. Disclosure and Transparency

1. To obtain an overall picture of the level of disclosure with respect to types of information and accessibility of information, the present study classified the questions into several groups, ,i.e., disclosure related to the financial information, the business and its operation, the ownership structure, the boards' accountability, and the accessibility of information. The average scores for each group in descending order are as follows:

Type of Information	Avg Disclosure Score	Avg Mandated Disclosure Score	Avg Voluntary Disclosure Score
1. Financial	89.9 %	95.3 %	63.2 %
2. Accessibility of information	63.5 %	95.5 %	58.9 %
3. Business and Operation	63.5 %	77.0 %	54.4 %
4. Ownership Structure	63.0 %	99.0 %	54.0 %
5. Boards' accountability	56.0 %	79.0 %	52.1 %

Overall, the disclosure related to the financial performance was the only type of information that was rated good, while the disclosure related to other types of information were rated fair or less than fair. The boards' accountability received the lowest score. The fact that the score was much lower than 66.7per cent implied that on average more firms received a poor score rather than a good score in this category. When each category was broken down into mandatory or encouraged information to be disclosed and voluntary disclosure, the mean scores for mandatory or encouraged disclosure were much higher than those for voluntary disclosure. The results also indicated that the high score for financial disclosure was due to the mandatory disclosure of financial information.

2. We found that the regulation on mandatory disclosure had a significant impact on the level of disclosure. The current study employed data or information in year 2005. In that year, the regulation on disclosure, especially in the annual report, was based on rule no. 38/PM/1996 set by Bapepam. Mandatory disclosure according to the rule was fairly limited to the financial performance (including financial statements), management discussion and analysis on financial performance, and significant changes during the year. The rule provided illustrative examples of information that can be disclosed. Disclosure requirement of the boards' accountability was very minimal.

e. Responsibility of Board

1. The Top average score (the highest 5per cent) of Responsibility of The Board practices of surveyed companies was 81.28per cent, which was dominated by the ***Banking industry*** *(9 out of 17 surveyed companies or 52.94 per cent Top Ratings)*, while the bottom average score (the lowest 5per cent) of Responsibility of The Board practices of surveyed companies was 38.42per cent, dominated by the *Manufacturing* ***industry*** *(5 out of 17 surveyed companies or 29.41 per cent Bottom Ratings).*

2. The boards of commissioners of surveyed companies had not been effective in monitoring and controlling the top management's actions. This contributed to the poor performance of shareholders' rights because the BOC were not fulfilling their primary fiduciary duty in protecting shareholders. The major factors affecting this ineffective monitoring and control can be attributed to the following:

a. Lack of standard principles (corporate governance and ethical standards) as guidance in implementing good corporate governance practices.

b. Lack of orientation and corporate governance-related training programs for directors and commissioners.

c. Although BAPEPAM requires that the audit committee be established in each company, it has not contributed much to the improvement of the board performance in fulfilling its key functions. The absence of other key committees, such as compensation and nomination committees in the majority of companies had also weakened the effectiveness of the board.

f. Overall Corporate Governance Performance

1. Laws and regulations played significant roles in encouraging companies to improve their good corporate governance practices. This was confirmed by the performance of highly-regulated companies, such as SOEs and banks.

2. Regulatory- or non-regulatory-types of questions in the assessment also affected the scores attained by the surveyed companies. For example, a question related to the committee audit (which is mandatory) resulted in a better score compared with a question related to compensation and nomination committees (which is voluntary).

3. The size of the firm, in terms of assets, seemed to correlate with the practices of corporate governance.. The high performers in corporate governance practices were commonly big companies. This empirical fact may be attributed to the costs of implementing the practices that only big companies can afford.

4. Overall, the orientation of corporate governance practices of surveyed firms was still directed at the compliance with laws and regulations. However, the awareness to implement best practices voluntarily was on the rise, at least as practiced by the leading corporations.

B. Recommendations

1. To improve shareholders' rights practices, firms were requested to pay a special attention on some items raised in the questionnaire, such as individual board remuneration; shareholders' rights to elect board members individually; appointment of directors, commissioners, and external auditors; dividend policy; director's comment and opinion for the AGM agenda; voting methods; opportunity that allow shareholders to raise questions at the AGM; and attendance of CEO, chairman, and chairman of committees. The majority of the firms received a poor score for these items because of the unavailability of information. This performance can be attributed to the absence of requirements by BAPEPAM to include the items in the annual report (although the companies were required to submit a report on the results of the AGM).

   As a guide to improve the performance of these items, certain companies that received a good score were mentioned in this study so they can be used as a benchmark. Companies such as Antam, Medco Energy, Bank Niaga, Bank Mandiri, Bukit Asam, Telkom, Bank BRI serve as good examples for their performance in the disclosure of individual board remuneration. Antam and Metco Energy received a good score with respect to the attendance of their CEO, Chairman, and Chairman of committees at the AGM. Bank Niaga effectively used its website in informing voting procedures to their shareholders and other interested parties.

2. Insider information can be prevented by improving the performance of equitable treatment of shareholders. Some companies such as Bank NISP, Bank Niaga, Indosat, Astra International, Bank Danamon, Apexindo Pratama, Medco Energy, and Antam have a stated policy concerning the use of insider information. These high-performance firms can be used as a model. In the meantime, allowing the minority shareholders to have a say on the board compensation is more challenging to implement. BAPEPAM or the Central Bank of Indonesia (for banking industry) can play a critical role by requiring the firms to establish such policy.

3. The performance of stakeholders' role such as commitment to employees, customers, suppliers, shareholders, society at large, and environmental issues can actually be improved. Firms which showed low performance in these practices can gradually improve their practices by first identifying their major stakeholders and trying to meet their claims, before expanding to other stakeholders. Antam and Apexindo Pratama have shown their full commitment to their stakeholders, while some other companies provided appropriate commitment. Benchmarking practices against the high-performance firms are highly recommended. Requiring public-listed companies to establish CSR policies and tightly monitoring of its implementation by BAPEPAM is another strategic approach to improve the practices.

4. In 2006 Bapepam issued a new rule on the annual report disclosure (Kep 134/BL/2006). under this new rule, the extent of mandatory disclosure is much broader than that in the old rule. For example, the rule requires that firms report the activities of the board of commissioners and directors. However, some types of disclosure, for example disclosures

related to beneficial ownership and boards' remuneration, are still missing.. To think positively, we expect that under this new rule, the average level of disclosure for listed firms will increase more significantly in year 2006 than 2005. To further improve the level of disclosure, we also recommend that Bapepam expand mandatory disclosures, especially those related to boards' accountability, ownership structure, and require listed firms to have company websites. The voluntary implementation of best practices of disclosure is also highly recommended as exemplified by Antam, Bank NISP, Indosat, Bank Mandiri, Bank BRI, Astra International, Bukit Asam, Telkom, Bank Danamon, Medco Energy, Bank Central Asia, and Bank Niaga.

5. Firms which have established the corporate governance and ethical standards tended to received a good score in their corporate governance. Astra International, Bank NISP, Medco Energy, and other companies serve as good examples in this respect. Some of them went even further by making their own corporate governance rules and standards in accord with international standards. Therefore, we recommend that to corporate governance standards be established and implemented consistently.

6. The director's competence does have its life cycle. The effectiveness of the board can be improved by participating in corporate governance-related training programs. There is some evidence that the firms which adopted director training programs performed much better than those that did not. The corporate governance practices in Thailand also provide a good example by requiring directors of publicly-listed companies to be certified.

7. Mandatory committees beyond the audit committee, such as compensation and nomination committees, could play a vital role in improving the effectiveness of the board. However, all these committees must have the capacity to provide an objective and truly independent point of view of the work of the board.