



2005 Policy Dialogue on Indonesia  
*CORPORATE GOVERNANCE*

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The World Bank

Session 3

Report on the Observance of Standards and Codes (ROSC),  
Corporate Governance Country Assessment, August 2004

Bali, Indonesia

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## Regional Context

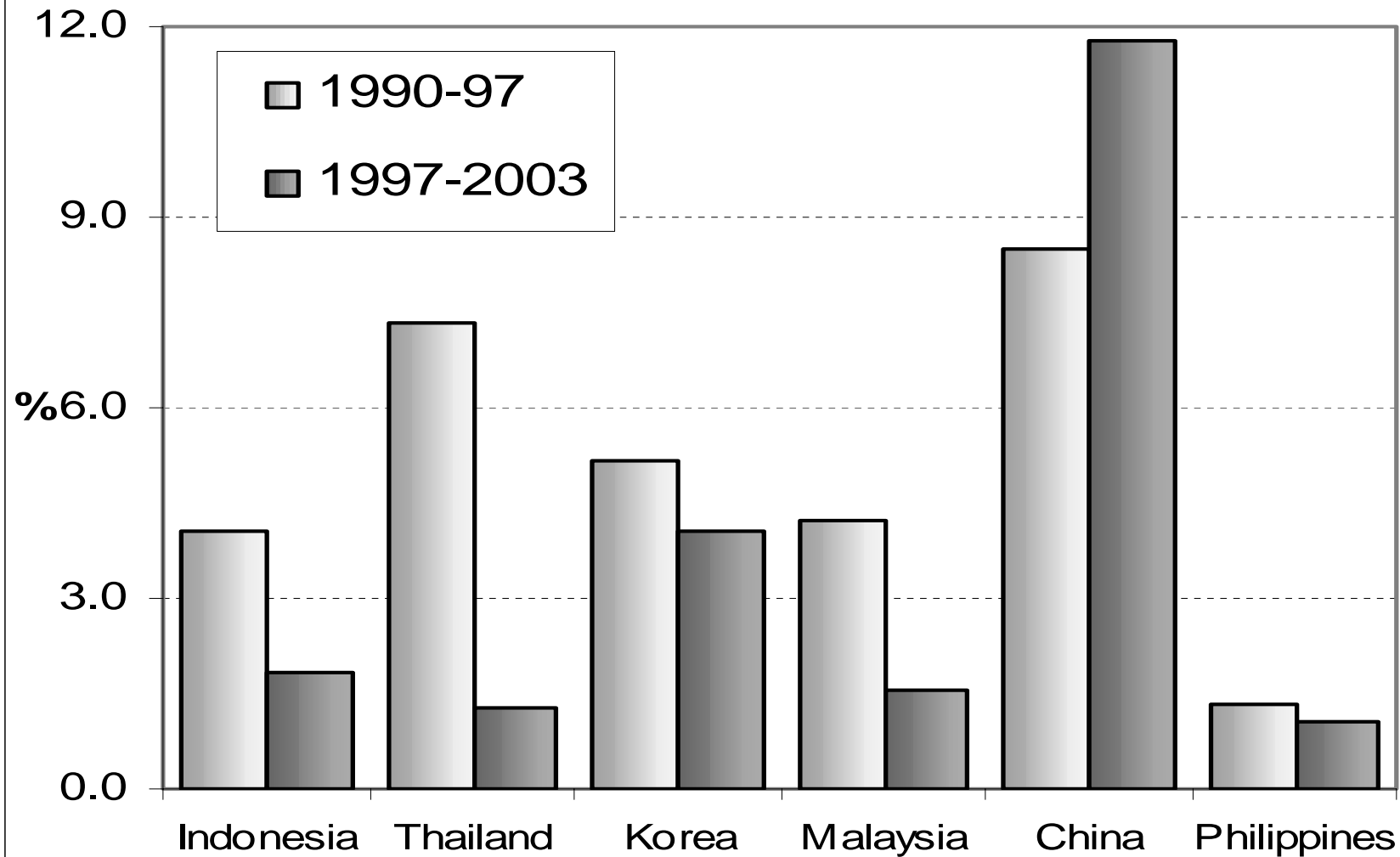
- All countries in East Asia, particularly higher income countries, are moving forward in reforming corporate governance as part of improving their competitiveness
- As countries move toward convergence of basic principles of corporate governance (accountability, transparency and the rule of law), it makes it easier to integrate their capital markets at the regional level

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## Regional Context (cont)

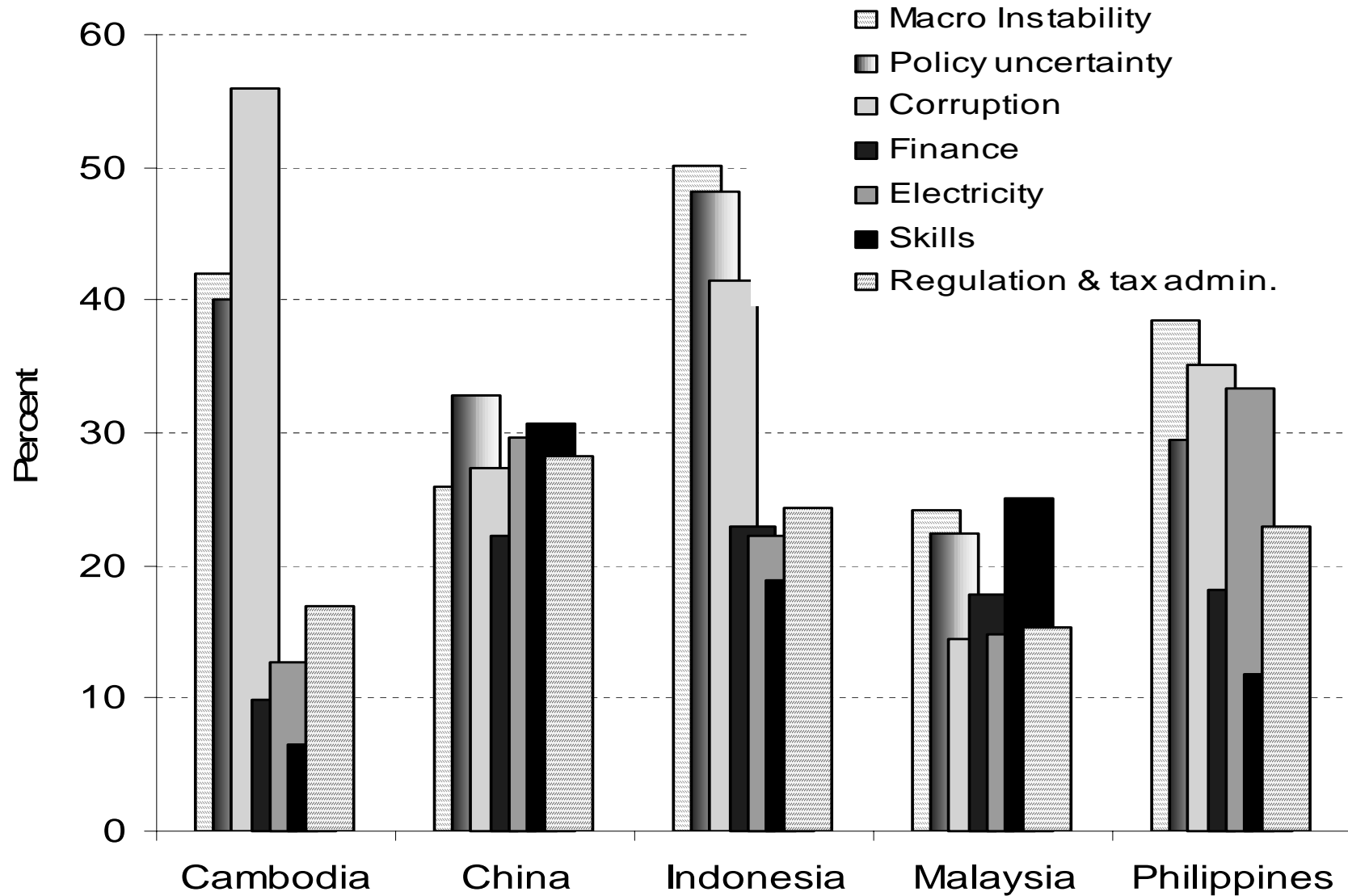
- Good governance influences the environment in which firms operate
- Corporate governance is an important element of good governance and should be promoted as part of a larger reform agenda
- Corruption often increases uncertainty of the business environment, has a major impact on cost of doing business.

**Figure 1: Growth in Physical Capital Per Worker (% per year)**



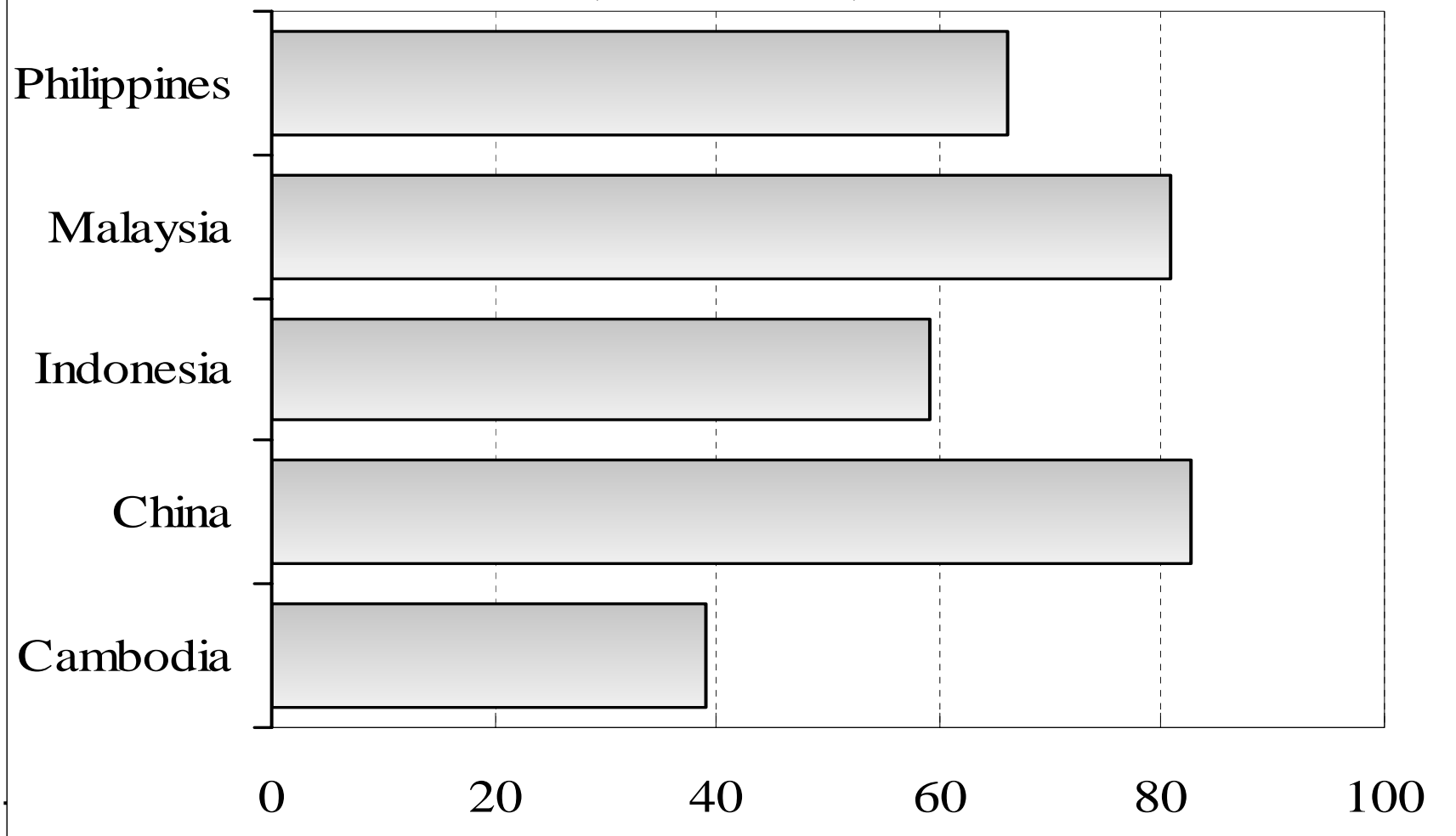
*Source: Bosworth and Collins (2003); World Bank calculations.*

Fig. 2 Major investment climate constraints



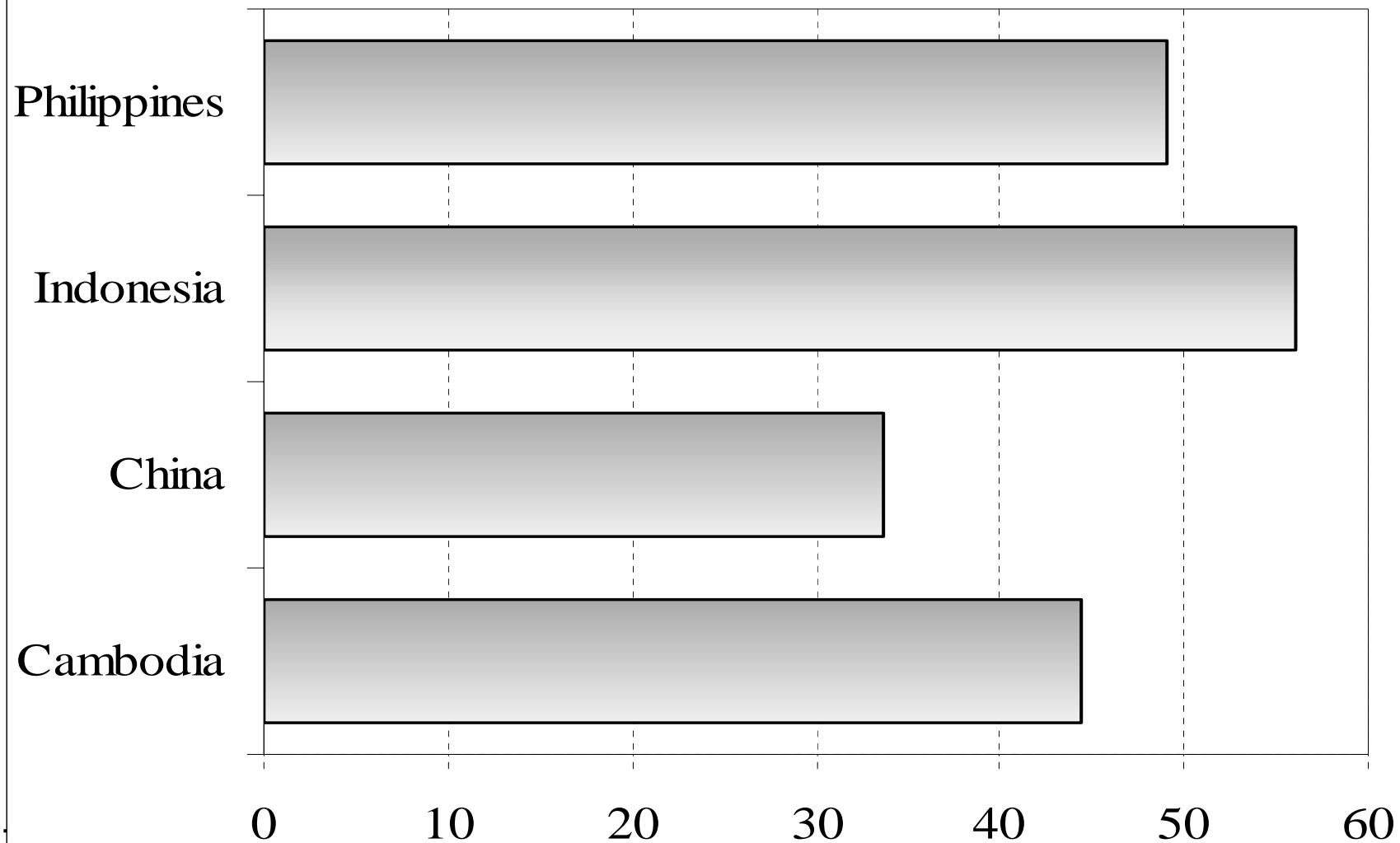
Source: Investment Climate Assessments, World Bank.

**Fig. 3: Confidence that courts will uphold property rights**  
(% of firms)



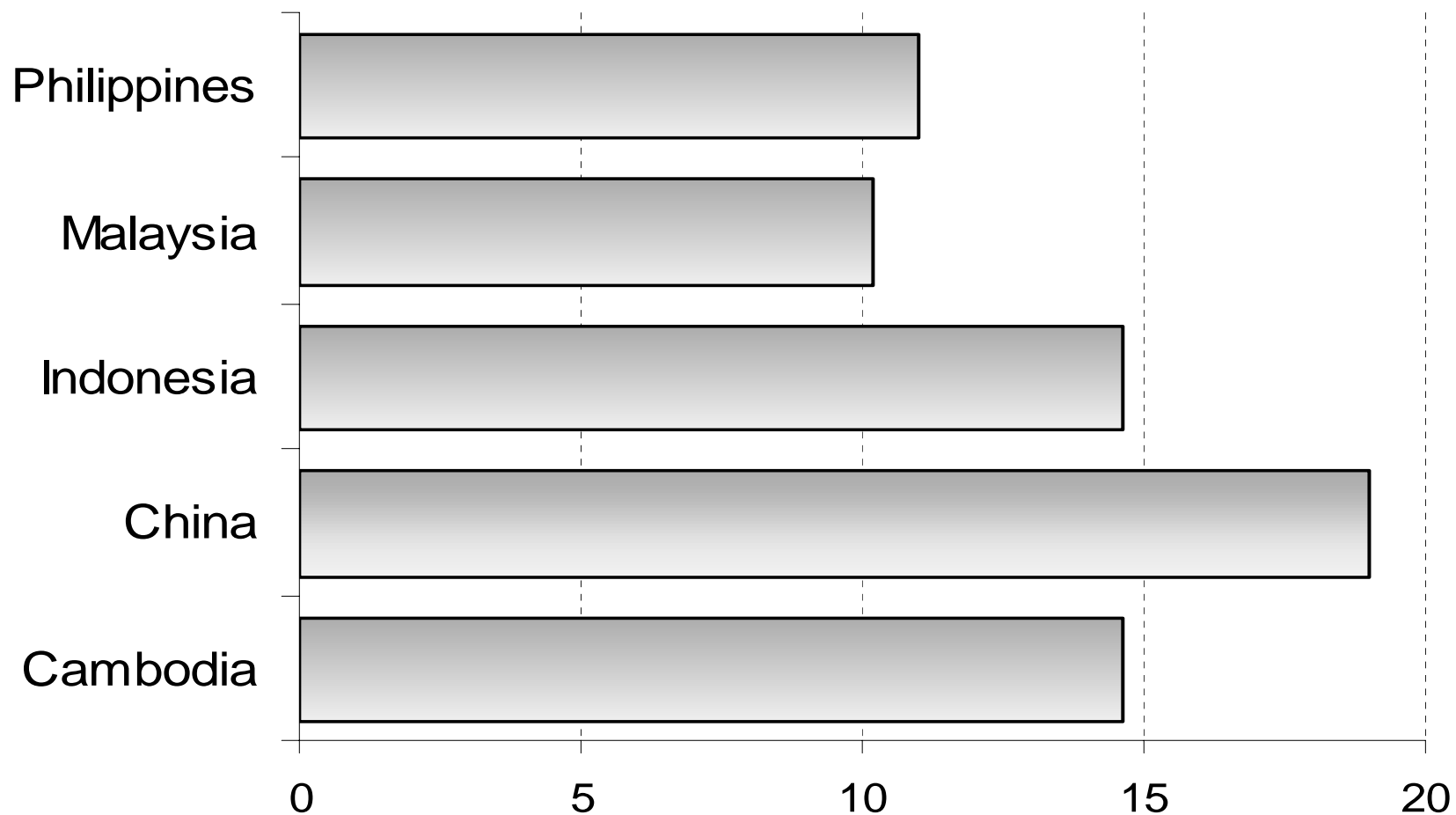
Source: *Investment Climate Assessments, World Bank.*

**Figure 4: Firms that believe interpretation of regulations is unpredictable (%)**



Source: Investment Climate Assessments, World Bank.

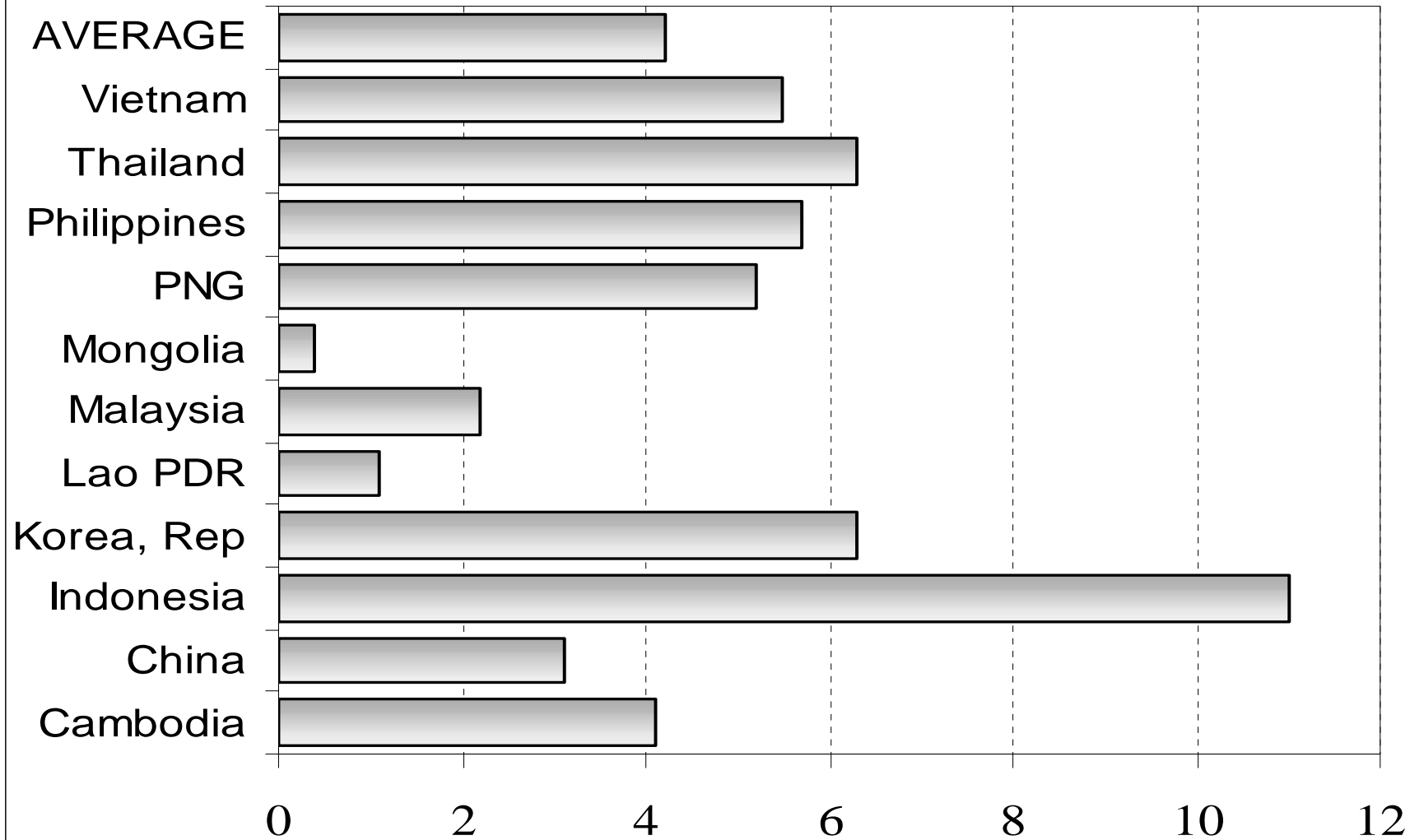
**Figure 5: Share of Management's time spent dealing with officials (%)**



*Source: Investment Climate Assessments, World Bank.*

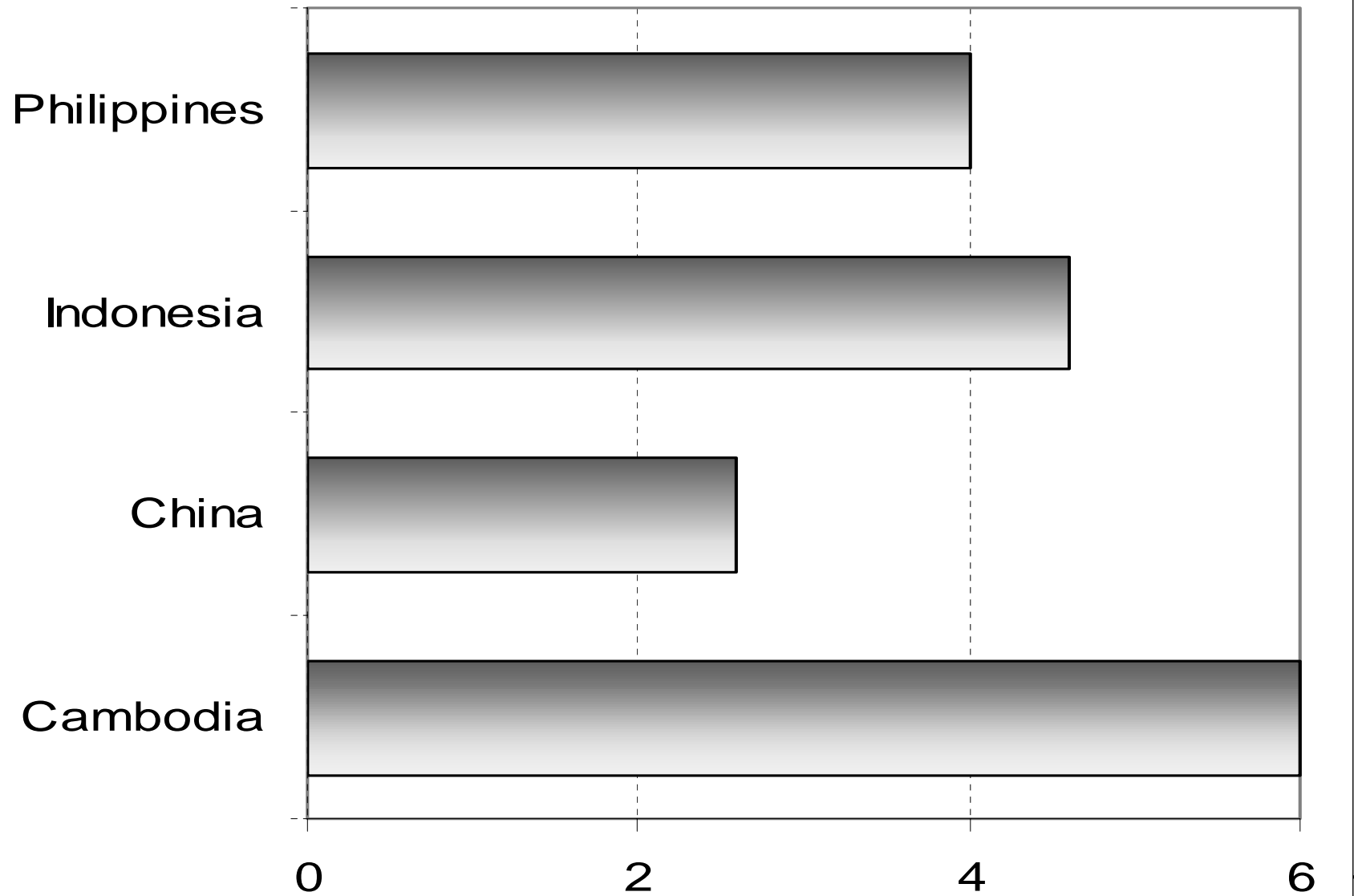


**Figure 6: Cost of registering a property as  
% of property value**



Source: Investment Climate Assessments, World Bank.

**Fig. 7: Bribe as Share of firm's sales (%)**



Source: *Investment Climate Assessments, World Bank.*

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# Corporate Governance Country Assessment (ROSC)

- Since 2000 Indonesia has taken significant steps to address weaknesses in its corporate governance framework
- Indonesia now has an elaborate system of formal corporate governance rules
- Equity market as percentage of GDP remains small
- Major challenges remain

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# Context

- Corporate sector is characterized by:
  - Companies with concentrated ownership
  - Controlling shareholders
  - Business culture known to be relationship-based rather than rule-based
  - Enforcement is weak and level of sanctions for violations of laws and regulations may not be adequate

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# Assessment

- Principle-by-principle assessment using OECD principles as benchmark is, in general, partially observed
- While the legal and regulatory framework complies with the OECD principles, practices and enforcement diverge

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# Key Recommendations

- Strengthen the role of Bapepam as the securities regulator
- Strengthen enforcement of laws and regulations
- Clarify in company law the fiduciary duties of directors and commissioners for violation of securities law

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## Key Recommendations (cont)

- Consider addressing accountants' legal liability with respect to third parties in the draft public accountants' law
- Improve transparency and reliability of financial reports and adequacy of disclosure
- Adopt fully international accounting and auditing standards
- Make accessible on company website annual reports and other relevant company information

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## Key Recommendations (cont)

- Strengthen process for nomination and selection of independent commissioners
- Improve effectiveness of audit committees
- Further enhance minority shareholder rights
- Intensify training of directors and commissioners, establish an accredited program



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# Conclusion

Improving corporate governance is a long term process and requires a collective effort by all market participants, including regulators, creditors, institutional investors, directors, commissioners, accountants, and shareholders.

Thank you