



CG FOCUS

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Strengthening Stakeholder Participation

The Financial Services Authority (OJK) of Indonesia has introduced Regulation Number 21/POJK.04/2015 concerning the Implementation of the Corporate Governance Guideline for Public Companies. The Circular Letter Number 32/SEOJK.04/2015 (hereinafter ‘the CG Guideline’) requires companies to engage with stakeholders to ensure the company’s long-term sustainability. Stakeholders include all shareholders (including minority shareholders), employees, suppliers, customers, creditors, and others affected by company activities. This note provides guidance based on OJK recommendations and some leading international practices.

Other regulations applying to the BoC and BoD

In Indonesia, other regulations and company documents may apply to company relations with stakeholders. These must be complied with as appropriate and include (but are not limited to):

- Law No. 40/2007 on Limited Liability Company;
- Law No. 8/1995 on Capital Market;

- The individual company’s Articles of Association (AoA).

Improving corporate governance through stakeholder participation

Stakeholders play an important role in evaluating, monitoring, and urging companies to adopt good corporate governance practices, thereby contributing to their long-term sustainability. Principle 7 of the CG Guideline recognizes the importance of engaging stakeholders, incorporating their interests, and protecting their rights in building competitive and profitable companies. To accomplish this, companies should identify their key stakeholders, understand their interests, and establish policies and practices for their participation in company activities. It is equally important to ensure that stakeholders have sufficient information on company policies and access to redress mechanisms to report any violations of these policies.

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Principle 7: Improving Corporate Governance Through Stakeholder Participation.

Rec. 7.1: Public companies have a policy to prevent insider trading

Rec. 7.2: Public companies have an anti-corruption and anti-fraud policy

Rec. 7.3: Public companies have a policy on supplier selection and capacity improvement

Rec. 7.4: Public companies have a policy to fulfill creditors' rights

Rec. 7.5: Public companies have a whistle-blowing policy

Rec. 7.6: Public companies have a policy to provide long-term incentives to directors and employees

7.1 Policy to prevent insider trading

Insider trading can disadvantage investors/minority shareholders who trade without access to the information available to insiders and can also result in insiders pitting their own self-interests against those of the company. Careful handling of material non-public/confidential information and mechanisms to discourage its misuse by corporate directors, officers, and others who have access to inside information are important elements of an effective corporate governance regime. It is illegal for a person who has inside information to trade using that information as defined in the Capital Market Law.

Public companies should minimize the occurrence of insider trading through preventive policies, for example with a clear separation of confidential data/information from public data/information as well as a proportional and efficient division of responsibilities for information management. Transparency regarding insiders dealing in shares is an important part of the protection of minority shareholders who may not have access to insider information. The company's insider trading requirements may be a stand-alone policy or may be incorporated in a code of ethics/conduct applying to the BoC, BoD, senior managers, and employees of the company. Public companies should therefore:

- Develop and publicly disclose a formal, written policy defining company requirements for confidentiality and the management of confidential or privileged information. The policy should include a clear procedure to allow stakeholders to report any contraventions to the policy that come to their notice.

- The policy should describe the accountability mechanism, including who is responsible for preventing information from leaking outside of the company, ensuring information is not misused, and overseeing and reviewing the existing procedures.
- Establish mechanisms to ensure oversight and enforcement of self-dealing rules starts with a company's BoC, BoD, and management.
- Contents of the policy should include:

» A definition of confidential/privileged information as any information related to the company's business that may significantly influence the market price of the company's shares, investors' decisions to buy, sell, or maintain them, or investors' decision as to the exercise of their rights.

» A requirement for all insiders (including BoC and BoD members, senior managers, and controlling shareholders) to always act honestly, with integrity, and in the best interests of the company.

» Full disclosure of all interests of company insiders including shareholdings and shareholdings of their related parties, related persons, and any entities associated with the insiders or over which they may influence or exercise investment decisions.

- » Prohibition of trading on non-public material information, or forbidding anyone to benefit from his/her possession of privileged information.
- » Prohibition of sharing such information with others, except as required by their professional duties and law.
- » Prohibition of recommending to others that they purchase or sell affected securities.
- » Requirement to obtain board permission prior to trading from all those who have or are assumed to have access to inside information.
- » Announcement of all shares trading to the regulator and to the public at large by those perceived to be insiders as soon as the transaction occurs.
- » Introduction of 'black out' periods¹ whereby those with inside information may not trade in company shares.
- » Disclosure of company processes and sanctions for breaches of the policy.
- » Provision of a list of non-exclusive examples that would normally fall into the realm of confidential/privileged information.

The base expectation is that all commissioners and directors have a duty to always act honestly, with integrity, in good faith, and in the best interests of the company. Commissioners and directors should be – and be perceived to be – above reproach in all their actions.

The Code of Ethics/Conduct or policy should include programs and procedures intended to prevent corruption, kickbacks, fraud, and bribery within public companies and to ensure all company personnel, including commissioners, directors, and management, understand the requirements of the policy. The scope of the anti-corruption policy should reflect prevention against all forms of corruption, which include the act of illegally giving to or receiving benefits (monetary and in-kind) from other parties. Public companies should therefore:

- Develop, adopt, socialize, and provide training around a formal, written anti-bribery policy/code which also includes gifts, hospitality, donations and similar benefits, and facilitation payments. The policy should clearly define behavior expectations from all company personnel.
- The policy shall apply to all personnel, be published on the company's website, and include encouragement for stakeholders to report any contravention to the policy that comes to their notice.
- The language shall be simple, concise, and easily understood by all commissioners, directors, and employees and promoted to internal parties within the company as well as external parties that deal with the company.
- The policy should contain a top level and visible commitment to an unequivocal state of 'zero tolerance' and absolute prohibition of any bribery or corrupt activities. Training on the policy's requirements shall be provided regularly to all personnel.

7.2 Policy on anti-corruption and anti-fraud measures

An anti-corruption and anti-fraud policy is beneficial to ensure that business activities are conducted legally, prudently, and in accordance with the principles of good corporate governance. This policy can be incorporated as a part of a code of ethics/conduct, or as a stand-alone policy.

¹ A 'black out' period is a time when trading is limited for certain insiders during periods when they are presumed to be in possession of privileged information (e.g., immediately prior to quarterly earnings announcements).

- The policy’s effectiveness shall be subject to regular evaluation and the results reported to the BoC. All waivers of the policy’s provisions shall be reported immediately to the BoC.
- The policy shall be regularly reviewed, revised, updated, and endorsed by the leadership team and shall include a process for reporting suspected misconduct (see whistle-blowing policy).
- The policy shall include that company personnel:

- » Conduct regular risk assessments of company exposure to fraud, bribery or corruption risks.
- » Implement an anti-fraud and anti-corruption due diligence process for recruitment as well as for suppliers, agents, distributors, and other intermediaries. Any contracts made by the company shall include anti-bribery terms.
- » Implement financial, procurement, and other commercial controls to minimize bribery risks for the organization.
- » Provide a reporting mechanism to escalate concerns around bribery.
- » Ensure processes are in place to investigate cases of alleged bribery and for appropriate action to be taken following the results of the investigation.
- » Keep accurate and detailed records of the company’s approach to bribery.
- » Will not put themselves in a position that will create conflicts of interest or a perception of being conflicted. They should behave in an exemplary way so as to sustain public trust, be professional, be accountable for their actions and decisions, and not bring disrepute on the company.
- » Confirm annually in writing that they understand the policy and will abide by its provisions.

Examples of good anti-fraud and anti-bribery and corruption measures can be found in the *OECD Guidelines for Multinational Enterprises* and in the *UN Global Compact*. Material in this newsletter has been sourced from the UK Institute of Business Ethics’ Business Ethics Briefing, Issue 27, October 2012, Anti-Bribery and Corruption Standards and Frameworks, available at www.ibe.org.uk. An example of an anti-bribery and anti-corruption policy may be found at www.aurizon.com.au.

7.3 Policy on supplier selection and capacity improvement

A policy on supplier selection is useful to ensure that companies are procuring high quality goods and services at competitive prices. Meanwhile, supplier capacity improvement policy is important to guarantee an effective and efficient supply chain, which will significantly influence the quality of the company’s output. The implementation of this policy can guarantee the continuity of the company’s critical supplies, both quantitatively and qualitatively.

The policy should cover criteria for supplier selection, a transparent procurement mechanism, supplier capacity improvement, and the fulfillment of suppliers’ rights. Ethical compatibility is also important and should include due diligence processes on values and standards, on treating customers fairly, and on financial and non-financial risks.

A policy on supplier selection should include:

- » A statement of mandatory requirements for suppliers including compliance with all laws, standards, and rules.
- » A requirement for company employees and suppliers to adhere to the company’s code of ethics/conduct, including prohibition of bribery or collusion between company employees and suppliers, transactions that are conflicted, and a commitment to cease dealings with suppliers that transgress legal or company standards.

- » A commitment to supplier information confidentiality and to the proper handling of complaints.
- » An accreditation/screening process for regular suppliers of goods and services, contract review and approval processes and required information from vendors, and delivery and invoicing specifications.
- » Supplier review for fair, transparent, and reasonable employment; healthy work environment; and health, safety, and environmental practices.
- » A supplier training program to develop understanding of the firm's requirements and support for skills, knowledge, and systems to ensure those requirements are met. The training should include ethics, management systems, labor standards, environmental standards, health, safety, and workplace matters. Such training should also recognize any specific industry standards/code of practices.
- » The application of a supplier policy should include regular assessment and monitoring of suppliers as well as their relationships with the company's employees.
- » General purchasing policies including details of responsible individual or department, basic guidance on professionalism and business practices, internal controls, the parameters of open and competitive selection processes, and the requirement to protect the company's reputation.
- » Authority levels and required processes and documentation for purchasing.
- » A statement of the responsibilities of a purchasing department and of a requisitioning department.
- » A process to report breaches of company supplier requirements.

An example may be found in the Responsible Sourcing Policy of Unilever at www.unilever.com

7.4 Policy to protect creditors' rights

Policy on the fulfillment of creditors' rights can be used as a guideline in dealing with creditors. The policy, which is intended to safeguard creditors' rights and maintain creditors' trust towards the company, should take into account factors that need to be considered before entering into a loan agreement and follow-up actions to fulfill the company's obligation towards its creditors.

A policy to ensure respect for creditors' rights should include:

- » A commitment to mutual respect based on fairness and truthfulness in all dealings (no coercion or unnecessary litigation) and a regular and timely consideration of creditors' rights by the debtor.
- » A commitment that creditors shall enjoy all rights and interests provided for in laws, regulations, and rules, including in creditor contracts.
- » The provision to creditors of material information in relation to their rights and interests and co-operation with creditors when they seek access to information to protect their interests.
- » A commitment to making timely payments according to agreed terms and conditions and to not undertake transactions that may harm creditors' rights or interests.
- » A commitment to confidentiality in creditor dealings and to timely resolution of complaints and disputes.

7.5 Policy on whistle-blowing

A whistle-blowing policy that has been developed properly will provide assurance and guarantee the

protection of a whistle-blower or witness of a violation committed by the company's employees and/or management. The implementation of a whistle-blowing policy will have an impact on the formation of good corporate governance culture.

A whistle-blowing policy should cover the types of reportable violations, reporting mechanisms/procedures, whistle-blower protection and guarantee of confidentiality, complaints handling, complaints manager, and results/follow-up of the complaints handling.

Good practices for a whistle-blower policy include:

- » The company's commitment to receiving and responding to a whistle-blower in a timely manner and to maintaining fairness and confidentiality to all parties.
- » The purpose of the policy and clarity as to whom it applies, which should include all full-time and part-time directors and staff, company suppliers, and contractors.
- » Guidance on what kinds of conduct to report, which should exclude/distinguish staff grievances.
- » Clarity as to the person or persons (internal or external to the company) who may receive the report and the role, if any, of the company's Whistle-blower Protection Office.
- » A statement on the expected investigative process after a report has been filed and the time frame in which to expect this process to commence. The investigative process should be objective, fair, reasonable, and appropriate for the reported conduct.
- » A statement of protection for the whistle-blower according to any applicable law against any disclosure of identity, disclosure of records, reprisal, retaliation or harassment, and protection of the whistle-blower's right to information and feedback on the progress of the investigation.

- » A statement about the protection and commitment to reliable confidentiality for any person alleged to have behaved improperly.

An example may be found from the Wesfarmers Ltd. website, www.wesfarmers.com.au

7.6 Policy on long-term incentives for directors and employees

Long-term incentives are predicated upon the achievement of long-term performance objectives of the company, which is reflected in the growth of the company's share value or other performance targets. A long-term incentive program is useful to encourage loyalty and provide motivation to the company's directors and employees to increase their productivity and performance, contributing to the company's long-term growth.

A long-term incentive policy (LTIP) shows a real commitment from the company to reward its employees in the long-term and should be structured and aligned with the company's long-term objectives. The policy, which can be included in the company's existing remuneration policy, should include its objectives and purposes as well as requirements and procedures for employee participation, and take into account conditions and risks borne by the company.

Long-term incentive plans should include:

- » Objectives that focus the work behavior of the covered employees on the desired performance, assist in the retention of executives and other key employees, and link achievement of long-term business strategies with the awards.
- » Various awards may be used, such as stock options, performance shares, and restricted stock plans, and should be chosen to suit the individual business. For example, a high growth company may prefer an employee stock option plan to help attract and retain talent while keeping fixed costs low. A mature company may prefer a performance share plan to drive and reward employee performance.

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» Criteria for LTIPs should be clear, be outcome based, and have set performance metrics that are achievable and meaningful for awards. One common metric is total shareholder return (TSR), which is return to investors/shareholders which may come as a result of capital gains through share price increase and/or through dividends.

» Personnel included in the LTIP should be carefully considered. LTIPs should not include too many people and focus on key personnel who can directly influence company performance.

» Any LTIP policy should clearly state the terms/definitions it uses, the type of plan it is, size of awards, participants, required documentation, key provisions and performance hurdles, any restrictions in dealing in awarded shares, leaver provisions, forfeiture provisions, the status of the plan if there is a change of control (takeover, reconstruction or winding up), how awards may be varied, conditions for vesting, exercise or clawback, and an explanation of the capacity for the company to change or terminate the plan.

» It is required in some jurisdictions and a common practice in many other jurisdictions to seek shareholder approval for LTIPs.

» For clarity, it is useful to include in the LTIP policy an example of how the plan may apply to a senior member of the staff.

An example may be found at www.phillips.com

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Contact us:

Chris Razook
Corporate Governance Lead
crazook@ifc.org

Mohsin Ali Chaudhry
Corporate Governance Officer
mchaudhry1@ifc.org

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