ACCELERATING CORPORATE GOVERNANCE REFORM IN THAILAND:THE BENEFITS OF PRIVATE REFORM MECHANISMS

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I. INTRODUCTION

When the Asian financial crisis hit Thailand in July 1997, speculators around the world originally viewed the blow to one of Southeast Asia's most promising "Tigers"[1] as a "currency crisis."[2] Only one year prior to the crisis, the International Monetary Fund (IMF) placed Thailand on its watch list due to its alarming current account deficit of 8% of GDP, its high foreign debt of 51% of GDP, and its 20% increase of short-term debt to foreign debt ratio.[3] During the months leading up to the crisis, foreign banks, which had previously saturated the economy with short-term foreign currency credit, discovered a mortifying legal loophole. Under Thai law, debtors were able to avoid loan payments indefinitely,[4] leaving foreign banks with no recourse to seize assets placed as collateral for defaulted loans.[5] Due to this disturbing insight, foreign creditors and investors quickly scrambled to get out of a country[6] that had not encountered "a single year of negative economic growth" since the late 1950s.[7]

Viewed superficially, this is how the Asian financial crisis came about. Once scholars delved deeper, however, they learned that behind the opacity

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[1] *See* Scott B. MacDonald, *Transparency in Thailand's 1997 Economic Crisis: The Significance of Disclosure*, 38 ASIAN SURV. 688, 689 (1998).

[2] *See* William H. Overholt, *Thailand's Financial and Political Systems: Crisis and Rejuvenation*, 39 ASIAN SURV. 1009, 1010 (1999).

[3] Deunden Nikomborirak & Somkiat Tangkitvanich, *Corporate Governance: The Challenge Facing the Thai Economy* 5 (1999) (paper submitted for Org. for Econ. Co-operation & Development Conference on Corporate Governance in Asia: A Comparative Perspective, Mar. 3-5, 1999), *available at* http://www.oecd.org/dataoecd/7/12/1931476.pdf (last visited Nov. 23, 2005); Asia Point Network, *Thailand and the IMF*, Jan. 30, 1998, http://www.asienhaus.org/asiancrisis/thai_imf.htm (short-term debt worried the IMF because it was unlikely that Thailand could repay its short-term loans if recalled).

[4] *See* Overholt, *supra* note 2, at 1011.

[5] *See id.* at 1012.

[6] *See generally id.* ("Banks realized simultaneously that (1) an impending bubble burst was endangering a wide range of even the most prestigious Thai companies; (2) a lack of transparency in company accounts under prevailing Thai regulations obscured the real financial status of their customers; and (3) Thai bankruptcy law failed to protect creditors. A massive exodus of foreign bank loans and fixed-income investors from Thailand ensued, triggering the country's historic financial crisis.").

[7] *Id.* at 1009.

of Thailand's financial sector, business was conducted with little regard to the technicalities of law. Instead, "relationship-capitalism," resulting from an Asian business culture that relied upon long-standing relationships between elite family firms and government officials, made up the corporate landscape.[8] In such an environment, it was not uncommon for government ministries to grant exclusive licenses to certain family firms,[9] for these firms to further monopolize the market by creating informal alliances with other families, and for banks to grant loans to such influential firms without evaluating the debtors' ability to pay back their loans.[10] Business was conducted without independent supervision by any of the traditional regulatory parties and thus, the corporate governance of many firms and banks was called into question.

Thailand's financial crisis resulted from "unsound macroeconomic policies and imbalances," as well as the "overutiliz[ation] [of] short-term foreign currency-denominated loans,"[11] rather than from a weak corporate governance system. The crisis, however, revealed serious flaws within Thailand's corporate governance practices that were previously overlooked. Some attribute the extraordinary financial exposure of Thailand and its neighboring nations to a financial and corporate culture infused with a lack of transparency and disclosure.[12] Such a claim reflects a country's business culture and also speaks to the effectiveness of a country's rule of law. Economist Scott MacDonald explains that countries with poor transparency mechanisms lack "trust in the [legal] system to uphold contracts, enforce regulation, and ultimately establish and maintain a level playing field."[13] According to the Organisation for Economic Co-operation and Development, ensuring the proper level of disclosure and transparency within the corporate sector is one of the cornerstones to creating a sound corporate governance framework.[14] As two prominent scholars, Andrei Shleifer and Robert Vishny, explain, "Corporate governance deals with the ways in which suppliers of finance to corporations assure themselves of getting a return on their investment."[15] The reason that corporate governance has become such an important reform concept is because, in the aftermath of the crisis, it is increasingly important for crisis-hit countries to restore investor confidence in the country's markets by ensuring both domestic and foreign investors that they will receive the proper return on their capital investments. In the long run, an effective

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[8] *See* Arthur M. Mitchell & Clare Wee, *Corporate Governance in Asia Today and Tomorrow*, 38 INT'L L. 1, 3-4 (2004).
[9] *See* Kevin Hewison, *Pathways to Recovery: Bankers, Business, and Nationalism in Thailand*, in CHINESE ENTERPRISE, TRANSNATIONALISM, AND IDENTITY 234, 237 (Edmund Terence Gomez & Hsin-Huang Michael Hsiao eds., 2004).
[10] *See* MacDonald, *supra* note 1, at 690.
[11] Piman Limpaphayom, *Thailand*, *in* CORPORATE GOVERNANCE AND FINANCE IN EAST ASIA: A STUDY OF INDONESIA, REPUBLIC OF KOREA, MALAYSIA, PHILIPPINES, AND THAILAND: VOLUME TWO (COUNTRY STUDIES) 229, 229 (2001), *available at* http://adb.org/Documents/Books/Corporate_Governance/Vol2/chapter4.pdf (last visited Mar. 24, 2005).
[12] *See* MacDonald, *supra* note 1, at 688.
[13] *Id.*
[14] ORG. FOR ECON. CO-OPERATION & DEV., OECD PRINCIPLES OF CORPORATE GOVERNANCE 24 (2004).
[15] Andrei Shleifer & Robert W. Vishny, *A Survey of Corporate Governance*, 52 J. FIN. 737, 737 (1997).

corporate governance system leads to greater competition amongst businesses, better corporate performance, and ultimately "overall economic growth and social welfare."[16] Thus, rather than focusing on the financial details of how to improve Thailand's corporate sector, this Note takes a broader approach by inquiring how Thailand may improve its corporate governance system through the creation of mechanisms for enhancing transparency.

Academics and practitioners studying the cause of the crisis identified two main attributes within Thailand's corporate sector that contributed significantly to the financial crisis.[17] These distinct factors are: (1) the concentrated ownership feature of large firms; and (2) an opaque corporate governance system that consists of inadequate market incentives and ineffective regulatory bodies.[18] Many studies on corporate ownership within countries worldwide question whether there is a possible link between having a large number of firms with high ownership concentration and having insufficiently developed corporate governance practices and legal institutions.[19] The curious relation between the two factors spawned a wealth of studies and, as a result, many scholars studying the transformation of corporate governance systems within developing Asian economies weighed the advantages of effecting change within the public sector through institutional and legal reforms, against private sector reforms such as changing firm ownership structures through greater diversification of shareholders.

The purpose of this Note is to present the two main faces that corporate governance reform may take, either public or private, and to analyze the likely success of each method in the legal, business, and political culture of a developing economy such as Thailand. Part II of this Note situates Thailand amongst the other East Asian nations and presents the possible benefits to Thailand in reforming its corporate governance regime. Part III discusses methods of public reform introduced by legal scholars, Thailand's own public reform efforts, and institutional change at the Thai Securities and Exchange Commission which serves as an example to analyze whether such public reform measures are sufficient for improving corporate governance. Part IV turns to the private sector and presents recent studies on the corporate ownership structure of Thailand's larger publicly traded non-financial firms. Part V concludes with an analysis of whether altering

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[16] Prasarn Trairatvorakul, *The Importance of Corporate Governance Reforms in the Recovery from Financial Crisis: Viewpoints from Thailand*, Nov. 9-10, 1998, http://wb-cu.car.chula.ac.th/papers/corpgov/cg071.htm.

[17] *See id.*

[18] *Id*.

[19] *See* Erik Berglöf & Stijn Claessens, *Corporate Governance and Enforcement* 2-4 (World Bank Pol'y Res., Working Paper No. 3409, Sept. 2004), *available at* http://econ.worldbank.org/files/38742_wps3409.pdf; Stijn Claessens, Simeon Djankov & Larry H.P. Lang, *The Separation of Ownership and Control in East Asian Corporations*, 58 J. FIN. ECON. 81, 107-09 (2000); Rafael La Porta, Florencio Lopez-de-Silanes & Andrei Shleifer, *Corporate Ownership Around the World*, 54 J. FIN. 471, 495-96 (1999) (explaining that to understand "corporate governance in most countries in the world, . . . to see how corporate governance is *changing or can be changed*, it is important to recognize how much an exception widely held corporations really are" or, alternatively, to investigate the ownership structure of firms).

the structure of concentrated ownership firms will accelerate the improvement of corporate governance practices at larger firms. Part VI ultimately purports that Thailand's corporate governance reform should emphasize the use of private actors rather than public ones and identifies specific enforcement mechanisms that will further develop the reform process. This Note argues that because Thailand's public sector is riddled with political and legal deficiencies that are largely cultural in nature, employing public mechanisms for change will delay corporate governance reform. The private sector, therefore, should play a key role in the implementation of promising corporate governance improvements. Although many legal scholars study corporate governance on a microscopic level, this Note does not attempt to focus on the "minutia of standards and practices of corporations."[20] Rather, it takes a broader stance on corporate governance reform in developing nations such as Thailand, where the greater problems are ineffective enforcement of the laws and weak institutional structures.

II. SITUATING THAILAND AMONGST OTHER EAST ASIAN NATIONS

A. WHY THAILAND?

After experiencing a tremendously successful history of economic growth, Thailand became the first victim of the East Asian financial crisis. Speculative attacks on its currency, the Thai baht (THB), devalued the baht from THB 24.53 = US$1 to a low of THB 53.74 = US$1 by January 1998.[21] The Thai stock market plunged by more than 65% in 1997 and the nearby economies of Indonesia, Malaysia, the Philippines, and South Korea quickly tumbled alongside Thailand's.[22] Aside from being the first casualty of the crisis, a review of Thailand's economic history reveals that the country has consistently been a particularly attractive investment ground for foreigners. Thailand's abundant natural resources and central location in the heart of Southeast Asia provided easy access to neighboring Indochina, Malaysia, Indonesia and South Asia.[23] Furthermore, as Japan developed into a more sophisticated economy, it looked to Southeast Asian nations to develop its heavy industries market.[24] Thailand's "skilled, literate, and comparatively cheap labor pool" provided one of the most practicable markets for Japanese direct investment.[25] Although Japan's entry into the

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[20] Mitchell & Wee, *supra* note 8, at 5 ("Good laws on the books do not immediately translate into good governance.").

[21] Overholt, *supra* note 2, at 1010. *See also* Nikomborirak & Tangkitvanich, *supra* note 3, at 5 (explaining that an additional reason for the devaluation of the baht and its illusory credibility can be attributed to the fact that during the period in which the Thai baht was pegged to the U.S. dollar, the baht appreciated approximately 17% against the dollar).

[22] Anya Khanthavit, Piruna Polsiri & Yupana Wiwattanakantang, *Did Families Lose or Gain Control?: Thai Firms After the East Asian Financial Crisis* 1 (Inst. of Econ. Res., Hitotsubashi U., Japan, Working Paper, 2003).

[23] *See* MacDonald, *supra* note 1, at 689.

[24] *See id.*

[25] *Id.*

Thai market only marked the beginning of a massive foreign direct investment inflow, many economists recognize that Thailand's steady success at attracting foreign investors is due to the fact that Thai laws are "less protectionist than its neighbors."[26] In the automotive industry, for example, economist William Overholt provides the following comparative description about Thailand:

> Thailand has succeeded primarily because it is less protectionist than its neighbors and provides a level playing field for foreign direct investors. Unlike Indonesia, the rules are clear. Unlike South Korea, foreigners are not deliberately driven out. Unlike Vietnam, there is no necessity to spend years building a consensus among government and party officials. Unlike Malaysia, Thailand does not insist that all key parts of the car be made at home. . . . Thailand's large, partially educated workforce can compete successfully against Malaysia's smaller one, Indonesia's largely uneducated one, and the highly skilled but very expensive one in South Korea.[27]

This "openness and [relative] fairness"[28] should continue to play an important role as investors abroad seek out emerging markets during the post-crisis era.

Another factor that makes Thailand attractive to investors emanates from the fact that Thailand is less susceptible to political upheavals than its neighbors.[29] At the time of this writing, however, some journalists suggest that Thailand's current political state may be a foreshadowing of future political turmoil to come.[30] Notwithstanding that fact, an additional reason to use Thailand in this study is because its civil legal system, though originating from the European models, is infused with common law elements borrowed from both England and the United States.[31] This hybridized legal system lends credence to the fact that Thailand is, once again, a middle figure amongst its neighbors because of its mixed legal structure. It is not decidedly civil, like the Indonesian system that is largely borrowed from the Dutch colonial model,[32] and it does not operate as a

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[26] Overholt, *supra* note 2, at 1019, 1026 (explaining that although Thai laws, compared to Singaporean or Hong Kong laws, technically place more restrictions on foreigners doing business or practicing law in Thailand, such laws are largely not enforced and can often be maneuvered around by seeking out senior officials).

[27] *Id.* at 1026.

[28] *Id.*

[29] *See id.* at 1009 ("Though as severe as the collapses occurring elsewhere in the world, Thailand's financial crisis avoided the economically destabilizing revolutions its counterparts experienced in the Philippines and Indonesia, and with reference to South Korean and other countries."). *But cf.* MacDonald, *supra* note 1, at 689 n. 3 (noting that Thailand's political stability is only relative since it has experienced its fair share of military coups). *See also* Overholt, *supra* note 2, at 1031 (reviewing Thailand's political history).

[30] *See Thaksin the Callous*, ECONOMIST, Oct. 30, 2004, LEXIS, News Library (reporting that the image of Thailand's Prime Minister, Thaksin Shinawatra, may be beginning to tarnish due to his aggressive actions against insurgents in southern Thailand).

[31] *See* John Fagan, *The Role of Securities Regulation in the Development of the Thai Stock Market*, 16 COLUM. J. ASIAN L. 303, 306 (2003).

[32] *See* Jeremy J. Kingsley, Note, *Legal Transplantation: Is This What the Doctor Ordered and Are the Blood Types Compatible? The Application of Interdisciplinary Research to Law Reform in the Developing World – A Case Study of Corporate Governance in Indonesia*, 21 ARIZ. J. INT'L & COMP. L. 493, 507 n.74 (2004).

predominantly common law jurisdiction like the past British colonies of Singapore, Hong Kong, and Malaysia.[33] This special characteristic of Thailand's legal system may become useful in understanding why certain institutions such as the Thai Securities and Exchange Commission, modeled after the U.S. Securities and Exchange Commission, still has difficulties in effectively enforcing its law.[34]

Thailand serves as a paradigm model for investigating corporate governance in relationship-based market systems because studies have revealed that Thai firms exhibit the greatest concentration of ownership and control.[35] This means that in large Thai firms, the owner and the manager are basically the same person. As explained by Rafael La Porta, Florencio Lopez-de-Silanes, and Andrei Shleifer, understanding ownership structures is an important piece of the puzzle in determining "how corporate governance is changing or can be changed."[36] Shleifer and Vishny further explain that concentrated ownership creates the undesired potential for large shareholders to expropriate capital owned by minority shareholders.[37] Whether or not this is true, Thailand serves as an appropriate model for studying the effects that concentrated ownership may have on the Asian corporate governance culture.

In addition to having the highest concentration of ownership and control, controlling shareholders of Thai firms reinforce their control over the company by direct ownership of company shares[38] and through "informal alliances" with other dominant family firms.[39] Family firms may also effectively control an entire group of firms by creating holding companies.[40] These holding companies are created to hold shares of affiliated or subsidiary companies within the family firm's group.[41] Family members are placed on the management boards of these firms and individual family members may also own outstanding shares of these affiliated companies.[42] Positioning family members and friends in controlling positions of subsidiary firms suggests that the control

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[33] *See* Chee Keong Low, *A Road Map for Corporate Governance in East Asia*, 25 NW. J. INT'L L. & BUS. 165, 167 (2004).
[34] *See* Fagan, *supra* note 31, at 307, 328 (Fagan later explains that criminal prosecutions under the Thai legal system and the current securities enforcement system are unsuccessful, in part, because "Thai judges are proscribed by civil law procedure from basing their rulings on past decisions or applying their personal knowledge and discretion to a case.").
[35] *See* Claessens et al., *supra* note 19, at 99-100 tbl.4 (showing that Thailand has the most concentrated cash-flow rights, the most concentrated control rights, and the highest ratio of cash-flow to voting rights. This means that, in Thailand, the owners of firms (those receiving cash-flow) tend to have the most control over the management of the firm's business (those receiving control rights)).
[36] La Porta et al., *supra* note 19, at 495-96.
[37] *See* Shleifer & Vishny, *supra* note 15, at 739, 758-61.
[38] *See* Khanthavit et al., *supra* note 22, at 5 (Thai firms' use of direct ownership contrasts with other East Asian nations' more common use of indirect ownership. According to one group of academics, "Direct ownership means that a shareholder owns shares under his own name or via a private company owned by him. Indirect ownership is when a company is owned via other public firms or a chain of public firms. This chain of controls is in the form of pyramidal structures and/or cross-holdings, which can include many layers of firms.").
[39] *See* Claessens et al., *supra* note 19, at 93-94.
[40] *See* Limpaphayom, *supra* note 11, at 242-43.
[41] *See id.*
[42] *See id.*

mechanisms used by Thai firms used or are still using "relationship capitalism" to further their enterprises. This may be due to the fact that businesses in Thailand are still primarily dominated by ethnic Chinese.[43] Chinese merchants who immigrated to Thailand practiced a "distinctive type of capitalism [exhibited by] [c]ontinuing control by members of entrepreneurial families, [and] a preference for personalized, long-standing, external networks based on trust and often leading to friendship." [44] This practice of "Chinese diaspora capitalism" may still be the norm amongst Thai firms. Since corporate governance reforms in Asia attempt to eliminate the potential for widespread cronyism and business transactions based on personal relationships, informal alliances and networks between family firms in the Thai business community may be undesirable or in need of alteration. It is therefore useful to study how one country with such a pervasive relationship-based culture may seek to eliminate or modify this practice in the private sector.

B. THE PLIGHT OF OTHER VICTIMS

While many East Asian countries around the region embarked on similar corporate governance reform measures, the impact that the Asian financial crisis had on each country varied considerably. Factors such as differences in each country's corporate governance standards, legal infrastructure, level of property right protection, institutional and regulatory effectiveness, and degree of concentrated ownership within firms contribute to the diversity of experiences in the region.[45] For example, Hong Kong, Malaysia, and Singapore maintain higher standards in their legal and corporate governance systems.[46] Studies indicate that this may be due to the fact that common law jurisdictions, rather than civil law systems, are better at providing investors with protection.[47] As a result, Hong Kong weathered the crisis comparatively well and is now able to focus on implementing specific educational and legislative means for enhancing shareholder protection.[48]

In countries with more developed legal systems, seriously contemplating mechanisms for eliminating conflicts of interest within institutions are viable goals. For instance, Hong Kong is trying to remedy the problem of conflicts of interest in the system employed by the Stock

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[43] *See* Fagan, *supra* note 31, at 332 ("A study by Andersen Consulting in September 2000 found that despite comprising 14% of the population, Chinese businesses command 81% of the market capitalization in Thailand.").

[44] Hewison, *supra* note 9, at 234, *quoting* Constance Lever-Tracy & Noel Tracy, *The Three Faces of Capitalism and the Asian Crisis,* 31-3 BULL. OF CONCERNED ASIAN SCHOLARS 1, 5 (1999).

[45] *See* Il Chong Nam, Yeongjae Kang & Joon-Kyung Kim, *Comparative Corporate Governance Trends in Asia, in* CORPORATE GOVERNANCE IN ASIA: A COMPARATIVE PERSPECTIVE 85, 88 (Org. for Econ. Co-operation & Dev. ed., 2001).

[46] *See id.*; Low, *supra* note 33, at 168 (Hong Kong, Malaysia, and Singapore share a common English law ancestry which explains why their duties and standards of care with respect to company directors may be quite similar).

[47] *See* Low, *supra* note 33, at 165.

[48] *See* J. Mark Mobius, *Corporate Governance in Hong Kong,* CORPORATE GOVERNANCE: AN ASIA-PACIFIC CRITIQUE 201, 201-02 (Low Chee Keong ed., 2002).

Exchange of Hong Kong (SEHK).[49] The problem stems from the fact that the SEHK is made up of brokers who collect transaction charges from all active trades made on the SEHK.[50] But like any other independent stock exchange such as the NYSE or NASDAQ, the SEHK also regulates the companies from which it is receiving steady revenues.[51] Conflicts of interest problems also exist in Thailand, but the likelihood of successfully remedying the problem appears to be quite bleak considering the lack of independence that the government has from the business sector. The current Prime Minster of Thailand, Thaksin Shinawatra, is the wealthiest man in Thailand and the head of the largest telecommunications conglomerate, Shin Corp, and has been labeled as possessing "manifestly pro-business tendencies."[52] Instead of promoting transparency and bolstering the regulatory power of institutions like the Thai Securities and Exchange Commission, the current administration seeks to endorse the deepening of the securities market by doubling the market capitalization of the Stock Exchange of Thailand over the next three years and by handing out tax incentives to prospective investors.[53]

At the other end of the casualty spectrum is Indonesia, which was one of the hardest hit countries of the Asian financial crisis.[54] Indonesia shares many of the same statistical figures as Thailand in regards to ownership and financial structures. First, the Jakarta Stock Exchange and the Stock Exchange of Thailand are relatively young establishments with only twenty-five years of institutional competence. In contrast, the SEHK has over one hundred years of institutional experience.[55] Second, both Indonesia and Thailand exhibit two of the most highly concentrated family control structures with the fifteen largest families controlling well over half of the corporate assets in one study.[56] As will be seen later, some scholars attribute highly concentrated ownership of large family firms as a possible reason for a country's lack of institutional development.[57] Third, in reviewing firm factors that increase incentives to expropriate, both Indonesian and Thai firms outscore their counterparts by exhibiting the highest concentration of cash-flow and control rights residing in the hands of their largest shareholders.[58] Lastly, because Indonesia and Thailand have

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[49] *See id.* at 217.
[50] *See id.*
[51] *See id.*
[52] *See* Fagan, *supra* note 31, at 327; Sean Hawkey, *Free Speech in Thailand: WACC Scholar Takes on Prime Minister and Media Giant in Freedom of Speech Case* 257 (Aug. 2004), http://www.wacc.org.uk/wacc/publications/media_action/257_aug_2004/free_speech_in_thailand_wacc_scholar_takes_on_prime_minister_and_media_giant_in_freedom_of_speech_case.
[53] *See* Hackley, supra note 52.
[54] *See* Benny S. Tabalujan, *Why Indonesian Corporate Governance Failed – Conjectures Concerning Legal Culture*, 15 COLUM. J. ASIAN L. 141, 142 (2002).
[55] *See* Claessens et al., *supra* note 35, at 90 tbl.2 (indicating that the SEHK was established in 1891, while the Jakarta Stock Exchange and the Stock Exchange of Thailand were established in 1977 and 1975, respectively).
[56] *Id.* at 108 tbl.9 (indicating that the top fifteen families in Indonesia and Thailand control 61.7% and 53.3%, respectively, of the total value of listed corporate assets that families control).
[57] *Id.* at 109.
[58] *Id.* at 99 tbl.4 (in Indonesia and Thailand, respectively, 25.61% and 32.84% of the cash-flow rights lay in the hands of the largest shareholders while 33.68% and 35.25% of the voting rights lay in the hands of the largest shareholders).

two of the largest proportions of family-held firms but the smallest proportion of widely held firms, the level of economic development in these countries may be falling behind that of other East Asian nations.[59] This finding resonates with the fact that the level of economic development tends to increase as the level of concentrated control in publicly traded companies decreases.[60] Although an Indonesian country study could have served this Note well in some respects, Indonesia would be a more cumbersome case study due to the recent political and social disruptions that were further amplified by the financial crisis.[61] After the resignation of President Suharto, who governed the country for over thirty years, Indonesia endured the passing of four presidents during the post-crisis period from 1998 to 2002.[62] Furthermore, Indonesia's "great diversity of traditions, population groups, and geography," as well as its hodgepodge of a legal system consisting of "Dutch colonial rule, *adat* laws, Islamic law/influences and national laws," adds to the complexity of its legal culture.[63]

III. PUBLIC REFORM EFFORTS

A. WHAT THE SCHOLARS SAY

Much of the literature on corporate governance reform in post-crisis Asia espouses the need for these countries to implement public sector reforms rather than squander their efforts at a comprehensive reform of current accounting standards and corporate laws. These scholars argue that institutional changes and public sector reforms are more necessary to effect change in crisis-hit countries.[64] Rather than transplanting a Western corporate governance system such as the complex Sarbanes-Oxley laws, advocates urge these developing economies to focus on the root of the governance problem, namely, institutional deficiencies and ineffective legal enforcement.[65] For followers of this doctrine, legal transplantations of complex Western corporate governance systems to Asian countries are especially questionable because they tend to overlook the legal, political, and social cultures of the recipient country.[66] In addition, the corporate governance laws of exporting countries, such as the United States, are still

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[59] *Id.* at 103-04 tbl.6 (indicating that at the 10% cutoff level of firm control, 68.6% of the Indonesian firms are family-owned and only 0.6% are widely held; whereas in Thailand, 56.5% of the firms are family-owned and 2.2% are widely held).

[60] *See id.* at 104.

[61] *See* Overholt, *supra* note 2, at 1024 (relating that the crisis mostly affected the average Thai person's income growth by a few years while the average Indonesian's experience was a "real risk to basic livelihood").

[62] *See* Tabalujan, *supra* note 54, at 142, 171 n. 1.

[63] Kingsley, *supra* note 32, at 506-07.

[64] *See* Mitchell & Wee, *supra* note 8, at 5. In this note, "public reform" includes changes made in public laws as well as institutional changes made in government agencies.

[65] *See id.* at 5-6.

[66] *See* Kingsley, *supra* note 32, at 497-98 ("Law reform cannot be a 'one-size-fits-all' approach; rather, a more indigenous and organic structure is required.").

developing and not yet fully established, causing such laws to be both "vague and ambiguous [in] nature."[67]

On the other hand, legal transplants may serve a real purpose when a "perception of legitimacy" is necessary to assure outsiders that certain market economies are safe to invest in.[68] In the past, legal transplants were oftentimes utilized when emerging countries, which lacked an effective legal framework, preferred "borrow[ing] legal structures from others rather than having to reinvent the wheel" themselves.[69] The debate on legal transplants will become more significant when this Note investigates whether structural changes within Thai corporations should adhere to certain Western dispersed ownership structures or retain their native large-blockholder trait.

B. WHAT THAILAND IS DOING

In the aftermath of the crisis, Thailand's financial sector promptly closed fifty-eight ailing finance companies.[70] The rest of the country, however, was more concerned with a complete overhaul of Thai political institutions and traditions.[71] The crisis fueled the passage of two of the most significant acts of Parliament — the Official Information Act B.E. 2540 (A.D. 1997) and the New Constitution B.E. 2540 (A.D. 1997).[72] The Official Information Act allows citizens greater access to government documents and enables citizens to evaluate whether the government is effectively managing state affairs.[73] As with most newly enacted Thai laws, it will be some time before this act is implemented into the everyday practice of government officials and ministries.[74] On a more sweeping scale, the New Constitution heralds in a new era of greater transparency through the establishment of special courts and independent regulatory bodies.[75] Through the recently instituted Constitutional and Administrative Courts, citizens may enforce their rights in courts for wrongs committed by government officials and corporations.[76] In addition, the New Constitution enhanced the role of the prior Counter Corruption Commission by creating an independent organization called the National Counter Corruption Commission.[77] The most significant changes come in the form of wider jurisdictional powers, impeachment powers, and investigative capabilities

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[67] *Id.* at 515.
[68] *Id.* at 516 (presenting another academic's view that legal transplants "provid[e] technical and political guarantees of strong institutional development that is necessary for foreign donors").
[69] *Id.* at 515.
[70] *See* Overholt, *supra* note 2, at 1016.
[71] *See id.* at 1014-15 (noting that after the financial crisis, "economic issues were relegated a lower priority than political reform").
[72] *See* DEUNDEN NIKOMBORIRAK, THAILAND DEVELOPMENT RESEARCH INSTITUTE, THE CRISIS AND THE STRUGGLE FOR BETTER GOVERNANCE IN THAILAND 6 (1999).
[73] *See id.*
[74] *Id.* at 7 ("Most state bureaus have not proceeded with the required declassification of certain official documents. Officials are also reluctant to deliver the requested documents too easily.").
[75] *See id.* at 8-9.
[76] *See id.* at 9-10.
[77] *See id.* at 8-9.

of state officials prior to the establishment of a guilty verdict.[78] Sanctioning such rights for citizens and enhancing the role of independent institutions are key components for governance reform because it demonstrates the government's commitment to enhancing transparency and accountability.[79]

1. *Thailand's Model Institution: The Securities and Exchange Commission*

Among the various public reform initiatives that Thailand embarked upon, the Thai Securities and Exchange Commission (SEC) took the most active role in confronting corporate wrongdoing and is generally touted as Thailand's "model independent institution."[80] Despite receiving this accolade, the SEC is not without its problems. One scholar, John Fagan, surveyed top Thai officials, scholars, and corporate officers about the current securities environment and published his findings in a comprehensive article on the trials and tribulations of the securities legal framework. The article exposed a number of limitations in the SEC's institutional and enforcement powers. In regards to its institutional structure, the Stock Exchange of Thailand (SET) and the SEC share jurisdictional responsibility over the regulation of securities, which creates the problem of jurisdictional confusion.[81] Despite the fact that the SEC is designated as the principal regulator of the primary market and for issuing companies, the SET, in addition to its duties as the regulator of the secondary market, continues to administer full regulatory control over companies registered prior to the establishment of the SEC.[82] Without a single centralized regulator, it is inevitable that enforcement and investigative actions will remain unsynchronized and inefficient.[83] The SEC is also less independent than it appears to be since the government's Minister of Finance sits as Chairman of the SEC.[84] The fact that the SEC appoints five of the ten board members of the SET exemplifies the SET's lack of independence.[85] Also, all SEC proposed legislation must be approved by the Ministry of Finance and Parliament.[86] Aside from being too closely related to one another, both the SET's and SEC's institutional

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78 *See* Nat'l Counter Corruption Comm'n, *Duties and Responsibilities of NCCC*, http://www.nccc.thaigov.net/nccc/en/duty.php. The National Counter Corruption Commission (NCCC) investigated Prime Minister Thaksin Shinawatra's accounts and found that he concealed assets under the names of his maid, driver, and security guard, but the Constitutional Court later overturned the NCCC's decision in an 8-7 ruling. *Beware of the Watchdog*, ECONOMIST, Aug. 17, 2002, LEXIS, News Library.

79 *See* Michael RJ Vatikiotis, *The Struggle for Reform South-East Asia, in* ASIA PACIFIC GOVERNANCE: FROM CRISIS TO REFORM 31, 32 (Charles Sampford et al. eds., 2002). In the past, Southeast Asian nations focused on development and economic growth rather than the individual rights of a citizen. *See id.* at 32. Therefore, Thailand's efforts at refocusing its governance values may indicate a shift in its political beliefs. *See id.* at 32, 34, 41.

80 NIKOMBORIRAK, *supra* note 72, at 22.

81 *See* Fagan, *supra* note 31, at 326.

82 *See id.* Between 1974 and 1992, companies that listed with the SET were also regulated by the SET, as there was no SEC at the time. Unless these companies have issued new shares after 1992, they will still be regulated by the SET. *See id.*

83 *See id.*

84 *See id.*

85 *See id.*

86 *See id.*

structures are fraught with political undertones. This intertwined setup creates two legal institutions that are susceptible to partisan pressures.

The current legal framework for regulating securities also has enforcement-related problems because the primary mode of enforcement is through the criminal system.[87] This means police officers and public prosecutors lead criminal prosecutions of securities violations after the SEC brings a claim against the alleged violator.[88] Police officers and prosecutors, however, do not have the knowledge or the resources to understand how securities laws work.[89] Furthermore, the standard of proof is too high for criminal convictions in that there must be proof beyond a reasonable doubt for all elements, including scienter.[90] This is in contrast to the United States securities regulatory system where civil remedies are more common and standards of proof range from a presumption of reliance, if the investor can prove that she bought the injurious security without knowledge of a material misstatement or omission, to various standards of recklessness on the defendant's part.[91] For cases that make it to trial, the likelihood of a successful prosecution against the defendant is very low since Thailand's civil-law judges are prohibited from basing their rulings on past decisions or developing case law by considering outside factors to a case.[92] The SEC has initiated securities cases against alleged embezzlers, share price manipulators, fraudulent company executives, insider traders, unregistered companies and the like, but to no avail.[93] Cases that do reach the Supreme Court are ultimately dismissed because of the insufficient amount of evidence available to establish proof beyond a reasonable doubt, the high level of scienter referred to earlier.[94] Even when the SEC insists that there is sufficient evidence to prove that the defendants engaged in misdealing or securities fraud, public prosecutors, either because of a lack of experience or a lack of incentive to prosecute, eventually drop the cases.[95] In 2002, for example, the SEC brought a claim against seven executives of the Brinton Group who allegedly engaged in

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[87] *See id.* at 327.
[88] *See id.* at 327-28.
[89] *Id.* One regulator recalls that, "First we have to explain to them [the police and prosecutors] what a stock is." *Id.* at 328.
[90] *Id.* at 328, 353 nn.91, 97 & 103. Both SET and SEC regulators comment that, "barring confession by one of the parties, hard evidence is difficult to come by in securities fraud, insider trading and market manipulation cases." *Id.* at 328.
[91] THOMAS LEE HAZEN, THE LAW OF SECURITIES REGULATION, §§ 7.3[2], 7.3[4], 12.4[2], 12.8[3], 12.8[4] (4th ed. 2002). Under the United States' 1933 Securities Act, the standard of proof for §11(b) liability uses a presumption of reliance where the purchaser only needs to show that she (1) bought the security, and (2) there was a material misstatement or omission in the registration statement. Under Rule 10b-5 of the U.S. Federal Securities laws, scienter for 10b-5 liability is established by a showing of recklessness, despite language that plaintiff must prove "fraud or deceit." *See id.* at §§ 12.4[2], 12.8[3]. This recklessness standard varies among lower courts, from a "barely reckless" standard to a "highly reckless" standard. *See id.* at § 12.8[3].
[92] *See* Fagan, *supra* note 31, at 328.
[93] *See* SEC. AND EXCH. COMM'N, THAIL., *Chapter 4: Legal Action on Offenders and Violators,* FIRST DECADE OF THE THAI SEC AND CAPITAL MARKET IN THAILAND (1992-2002) 134, 142-151, *available at* http://www.sec.or.th/en/infocenter/pub/other/decade4_e.pdf (last visited Mar. 24, 2005) (chronicles the investigative actions undertaken by the SEC during the past decade).
[94] *Id.* at 144. The Court ruled that "the lack of proof that the accused had colluded in the buying and selling of shares" resulted in the prosecutors dropping two cases against corporations. *Id.*
[95] *See* Fagan, *supra* note 31, at 351.

boiler room operations that were headquartered in Thailand.[96] The Brinton executives defrauded unknowing Australian and New Zealander investors by selling worthless shares of overseas companies at inflated prices.[97] SEC officials and prosecutors found evidence contrary to the Brinton Group's publicized image of being a capable brokerage house and investment advisory service.[98] The evidence showed that the employees of the Brinton Group were neither qualified to sell securities nor to give investment advice to prospective clients.[99] As public and international pressure mounted, the SEC urged public prosecutors to see the case through Thailand's onerous legal system.[100] Eventually, however, prosecutors dropped the case against these foreign executives.[101] Meanwhile, securities regulators were reprimanded by both the domestic and international public for their failure to effectively prosecute such a high-profile case.[102]

While the Thai criminal justice system serves as a significant barrier to successful prosecutions of grave securities violations, administrative sanctions, though more commonly enforced, may also be even more effectively administered. First, rather than requiring companies to implement compulsory corporate governance mechanisms, the SEC only encourages voluntary adoption of such mechanisms.[103] By using a "largely voluntary approach," Thailand cannot expect to remedy long-standing incentive issues nor will it cure the problem of having an uneven standardization of corporate governance instruments among publicly listed companies.[104] Prior to the time of this writing, several scholars urged the SEC to require companies to comply with certain regulations and to fine violators an amount significant enough to deter them from future violations.[105] In recent times, the SEC issued regulations requiring companies to disclose

> annual reports which should include information on their compliance with the [SET's] 15 C[orporate] G[overnance] principles, the company definition of independent directors, a list of directors (specifying who are independent), the frequency of board meetings per year, the board meeting attendance record of individual directors, remuneration for individual directors, and the non-audit fee.[106]

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[96] *See id.*
[97] *See* SEC. AND EXCH. COMM'N, THAIL., *supra* note 93, at 148-49.
[98] *See id.* at 148.
[99] *See id.* at 148-49.
[100] *See* Fagan, *supra* note 31, at 351.
[101] *See id.*
[102] *See id.*
[103] *See* Limpaphayom, *supra* note 11, at 275-76.
[104] Fagan, *supra* note 31, at 334 (discussing why Thailand's lack of market forces creates a market where "[g]ood actors are not rewarded and bad actors are not sanctioned").
[105] *See id.* at 329; Limpaphayom, *supra* note 11, at 275-76; Mobius, *supra* note 48, at 211-12 (noting that in Hong Kong, administrative punishments for securities violations are so minimal and often equivalent to mere operating costs that violators can easily pay off).
[106] *SEC Encourages All Listed Companies to Strengthen Corporate Governance Practice*, THAI PRESS REP., Jan. 14, 2005, *available at* http://www.lexis.com.

Furthermore, the SEC now imposes disciplinary penalties on directors for failing to comply with SEC rules and regulations and also publicly reprimands such directors, thereby tarnishing their business reputations.[107] Other specific reforms include encouraging whistleblowers to cooperate with law enforcement officials and SEC regulators, and implementing a registration system to monitor publicly listed company directors and management.[108] These changes clearly illustrate the SEC's continued efforts at becoming a stronger institution, but perhaps the problems are not "imperfect laws and sub-optimal enforcement."[109] Some observers argue that the public simply lacks faith in the judicial system. Fagan reveals that there is a "traditional reluctance in Thailand to prosecute elite members of society, such as business or political leaders, for any crimes whatsoever, let alone a crime so difficult to prove as securities fraud."[110] If that is the general sentiment of Thai investors and the public, then it is the Thai legal culture that needs to change and not simply securities institutions and their regulations.

C. WHY CURRENT PUBLIC REFORM EFFORTS ARE WANTING

Public reform measures are slow mechanisms for change because such reforms ultimately seek to alter legal and political cultures. Especially in the field of corporate governance, scholars are beginning to realize that "culture matters to legal development" and that reformers need to study a country's legal culture if they wish to alter a country's corporate governance framework.[111] As Jeremy Kingsley notes, legal culture encompasses the "ideas, values, and opinions people hold, with regard to law and the legal system."[112] Changing culture at any level, however, is like changing an entire society's way of life and altering their perspectives on current legal and societal structures. Altering existent legal cultures cannot be done by simply borrowing another country's legal standards. But with corporate governance, some advocate the use of legal transplantation where one country's "more effective" corporate governance framework is transplanted without regard to the recipient country's cultural differences.[113] One scholar specializing in Asian Law comments on the drawbacks of using a simplified system of transplantation for Asian legal systems:

> Law is a plant that grows out of the roots of the people, and it is an important way of educating people to change. If what is sought is a *ready-*

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[107] *See id.* In one case involving a misappropriation of loan money, the SEC imposed disciplinary penalties on sales executives, temporarily suspended one executive from his position, and publicly remanded another executive. *See id.*

[108] *See* SEC. AND EXCH. COMM'N, THAIL., CAPITAL THAILAND: QUARTERLY NEWSLETTER (Jan. 2005), *available at* http://www.sec.or.th/th/infocenter/pub/other/ct/no0348.html.

[109] Fagan, *supra* note 31, at 331.

[110] *Id.*

[111] Tabalujan, *supra* note 54, at 171 (noting, after studying why Indonesian corporate governance failed, that the corporate governance debate cannot be viewed from a purely economic, legal, or financial viewpoint).

[112] Kingsley, *supra* note 32, at 517.

[113] *See id.* at 515-16.

> *made law*, it can be bought "of the peg" from any consultant. But all there is then is a law. People still do the same things they always did. *Nothing changes*. That is the lesson of Asian history.[114]

One of the main problems in East Asian countries is the lack of effective enforcement of laws. As the quote above explains, however many laws there are in place, and however many changes to the black-letter law and to institutions there are, the legal culture must change before we can begin to see fundamental improvements in the corporate governance of a society.[115] Given that political and institutional changes are already set in place in Thailand, the country should allow those mechanisms for change to run their course and begin investigating how private reform may further corporate governance reform.

IV. PRIVATE REFORM PROPOSALS

A. CONTEXTUALIZING CORPORATE GOVERNANCE IN DEVELOPING ECONOMIES

Corporate governance deals with how owners are able to ensure that they receive the proper return on their investment.[116] "How do the suppliers of finance get managers to return some of the profits to them? How do they make sure that managers do not steal the capital they supply or invest it in bad projects?"[117] These are the basic corporate governance questions that economists and reformers ask. But in developing nations, corporate governance often relates to how outside or foreign investors may mitigate agency problems that arise from external financing of local business ventures.[118] In such countries, the two main corporate governance problems are: (1) individual or minority investors may not have the resources or incentives to ensure that managers are fulfilling their commitments which results in a free-rider problem where investors rely on other investors to investigate the matter; and (2) enforcement mechanisms may be too weak to punish those who are violating their commitments to the firm and to other investors.[119] Remedying these two problems is a major concern for nations like Thailand since such ills result in greater transaction costs for firms and decreased economic growth.[120]

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[114] Tabalujan, *supra* note 54, at 170 (emphasis added) (quoting Mary Hiscock, *Contemporary Law Modernism in Southeast Asia: A Personal Perspective, in* ASIAN LAW THROUGH AUSTRALIAN EYES 31, 46 (Veronica Taylor ed., 1997).
[115] *See id.* at 168.
[116] Shleifer & Vishny, *supra* note 15, at 737 ("Corporate governance deals with the ways in which suppliers of finance to corporations assure themselves of getting a return on their investment.").
[117] *Id.*
[118] *See* Berglöf & Claessens, *supra* note 19, at 6.
[119] *See id.* at 6-7.
[120] *See id.*

B. HOW PRIVATE REFORM CAN HELP

In developing countries such as Thailand, where legal systems are not strictly abided by and laws are not effectively enforced, the government should encourage the private sector to accelerate reforms in corporate behavior through corporate ownership changes or structural transformations. By using a private reform method, the two corporate governance problems mentioned above may be remedied more quickly.[121] Erik Berglöf and Stijn Claessens, economists studying corporate governance mechanisms in transitioning and developing economies, note that when a country's enforcement environment is weak, "[p]rivate sector efforts . . . can precede and serve as a basis for public laws."[122] This means that necessary changes in the private sector may cause later changes in the legal system rather than having the government regulate private actors or having the private sector comply with previously enacted laws. In countries with weak enforcement mechanisms, Berglöf and Claessens argue that "[p]rivate initiatives can take place outside the legal system [in that they] can be unilateral, bilateral, and multilateral."[123] Unilateral mechanisms occur when an individual firm finds it useful to improve its commitments to its shareholders.[124] An example is when a firm reforms its management and improves its corporate governance culture resulting in a higher stock value in the market.[125] Bilateral mechanisms occur when two firms engage in a venture that may enhance the reputation of one firm.[126] In such cases, the more reputable firm (Firm A) will not risk engaging in business with the other firm (Firm B) unless Firm A believes that Firm B will uphold its commitments.[127] Multilateral mechanisms are, for example, when multiple parties engage in agreements to establish codes of conduct..[128] Trade associations, self-regulatory organizations, and industry-specific organizations are examples of such multilateral enforcement mechanisms.[129] In Thailand, the Thai Institute of Directors, which serves as a center for directors of companies to exchange ideas and learn about good corporate governance, is the closest body to a multilateral enforcement mechanism.[130] This Note mainly focuses on unilateral mechanisms for

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[121] *See supra* text accompanying note 119.

[122] Berglöf & Claessens, *supra* note 19, at 41. The abstract to this paper notes that "bottom-up, private-led tools preceded and even shaped public laws" in developing countries. *Id.* at 1.

[123] *Id.* at 15. Although the paper discusses private initiatives in the sense of private lawsuits and the like, private reform changes may also be carried out through changes created by the private sector . For example, if private firms want to encourage investor confidence they may think it wise to implement independent audit committees prior to it becoming a requirement for them to do so.

[124] *See id.* at 17.

[125] *See id.* The example given by the authors is when the large Russian oil company, Yukos, "unilaterally reformed its management and corporate governance," it "was generously rewarded by the stock market." *Id.*

[126] *See id.* at 18.

[127] *See id.* The example given by the authors is when Yukos and McKinsey Company, a reputable consulting company, engaged in efforts to reform Yukos. *See id.* The authors argue that McKinsey would not have agreed to serve as a consultant for Yukos unless it believed that Yukos could fulfill its commitments. *See id.*

[128] *See id.* at 19.

[129] *See id.*

[130] *See* Thail. Inst. of Dirs., *About IOD*, http://www.thai-iod.com/eng/index.asp (last visited Mar. 24, 2005).

change, particularly firm-initiated changes in firm ownership structures. Some bilateral mechanisms for change will be presented, like when local Thai firms collaborate with foreign firms to increase ownership value. The conclusion will discuss multilateral mechanisms for change that have recently been established.

Returning to the main point, since private initiatives do not have to wait for the government or public enforcers to encourage change, they are generally more efficient than public sector reforms. Private players may find it important and in their own self-interest to make changes prior to it becoming the law. Particularly within the corporate governance debate for developing economies, policies for such countries should "focus [more] on promoting private mechanisms and empowering shareholders through information dissemination."[131] This will accomplish two things: (1) corporate governance improvements will happen more quickly through self-regulatory enforcement mechanisms within firms; and (2) investors, especially minority shareholders, will be able to evaluate firms using their own standards rather than risk having their investments be (mis)managed by majority or controlling shareholders.

C. UNDERSTANDING FIRM OWNERSHIP STRUCTURES

1. *General Studies on Ownership Structures*

Improving corporate governance requires an understanding of firm ownership structures since corporate governance concerns owners who want to ensure that they receive returns on their investments.[132] In the past, scholars worldwide believed in the Berle and Means image of the corporation.[133] That image was of corporations typically being widely held and run by managers who had little regard for shareholders' interests.[134] In the past thirty years, however, scholars have questioned whether this is the typical makeup of corporations. The Berle and Means study was based on United States firms, but economists later discovered that even within the United States, there are a large number of publicly traded firms with majority shareholders.[135] Nowadays, moreover, United States firms often have management interests aligned with ownership interests, which dispels the notion that managers and owners are separate parties with disparate interests.[136] As scholars observed the changing corporate ownership landscape of rich countries like the United States, they also began investigating ownership structures in other nations, developed and developing, around the world. They discovered that, generally, the Berle and Means concept of a widely held corporation is not a common

[131] Berglöf & Claessens, *supra* note 19, at 14.
[132] *See* Shleifer & Vishny, *supra* note 15, at 737.
[133] *See* La Porta et al., *supra* note 19, at 471 (noting that the Berle and Means image of the corporation was detailed in ADOLF BERLE & GARDINER MEANS, THE MODERN CORPORATION AND PRIVATE PROPERTY (MacMillan ed., 1932)).
[134] *See id.*
[135] *See id.* at 471-72.
[136] *See id.* at 472.

ownership feature of firms, especially for firms residing outside the United States.[137] Although widely held firms are more common in the richest common law countries, most countries with poor shareholder protection exhibit firms with controlling shareholders as owners, even in the largest firms where dispersed ownership would be expected.[138] La Porta *et al.*'s study is the first to illuminate that corporate governance studies should recognize that widely held firms are not the dominant form of ownership and that corporate governance reform should not be based on the fiction that firms are widely held.[139] Although La Porta *et al.*'s study includes minimal research on Thailand, concentrated ownership within even the largest firms is generally true of many East Asian countries with weak minority shareholder protection laws.[140]

Just one year after La Porta *et al.* published their findings on the corporate ownership composition of the largest publicly traded firms in the twenty-seven richest countries, Stijin Claessens, Simeon Djankov, and Larry Lang undertook a similar study by focusing instead on publicly traded companies within nine East Asian nations (Hong Kong, Indonesia, Japan, Malaysia, the Philippines, Singapore, South Korea, Taiwan, and Thailand).[141] Claessens *et al.* confirmed that more than half of the East Asian corporations in the study are family-controlled firms.[142] When family control is not significant, state control becomes prominent in five of the nine countries, including Thailand.[143] Cross-country differences do exist though. For example, the highest concentration of ownership and control exists in Thailand and the Philippines.[144] An interesting finding is that the separation of ownership and control within firms is most evident in family-controlled and smaller firms.[145] This means that such firms display some sort of "wedge" between owners (those who receive "cash-flow rights") and those who control the firm (those who receive "control rights").[146] Amongst family-held firms, Claessens *et al.* find that older and smaller firms are more commonly controlled by families.[147] This finding challenges the long-held claim that a firm's ability to disperse ownership is simply a matter of time and thus a part of a firm's life cycle.[148] The study also indicates that as the level of economic development increases, the level of

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137 *See id.*

138 *See id.* at 511 (concluding that even in the largest firms of countries with poor shareholder protection, controlling shareholders dominate over widely held firm structures).

139 *Id.* at 495-96 (arguing that "to understand corporate governance in most countries in the world, to appreciate what is essential about the countries where Berle and Means corporations are common, and consequently to see how corporate governance is *changing or can be changed*, it is important to recognize how much of an exception widely held corporations really are.").

140 *See* Claessens et al., *supra* note 19, at 82 (including Thailand in their corporate ownership studies).

141 *See id.*

142 *Id.*

143 *See id.*

144 *See id.* at 100 tbl.4 (indicating that firms in the Philippines and Thailand have the lowest separation of ownership and control or the highest concentration of ownership and control).

145 *See id.* at 82.

146 *Id.* at 101.

147 *Id.* at 82.

148 *See id.* at 105. As mentioned earlier, even in United States firms, managerial ownership is more common than it was in the past. *See supra* text accompanying note 134.

concentration between ownership and control decreases.[149] Such a finding may lead some scholars to conclude that dispersing ownership structures in developing East Asian firms may be the key to improving corporate governance and ultimately, corporate performance. Whether such a plan will be effective will be investigated further in this Note.

Claessens *et al.* conclude that East Asian firms are ultimately controlled by large shareholders, that ownership and management are to some extent separated, but that in most firms, management exhibits the most control.[150] How is ownership separate from management when management ends up possessing most of the voting rights within a firm? Many large controlling shareholders (those with the highest cash-flow rights) use various techniques to ensure that they are also able to hold the most voting rights in other firms or in subsidiary firms. Families may appoint individual family members to management positions of subsidiaries[151] or exercise control of other firms through pyramid structures, cross-holding patterns, or informal alliances with other family firms.[152] Viewed in relation to the other available evidence, the fact that management and control are not separate suggests that East Asian firms exhibit managerial ownership structures. This is because East Asian firms are generally controlled by single shareholders that are able to acquire the most voting rights within other firms, thereby allowing themselves an indirect method of control over other firms within the group. The following sections will show that Thailand has firms with owners that typically control the firm,[153] firms with owners that hold a large percentage of the economy's wealth,[154] and firms with a large controlling stakeholder.[155]

2. *Ownership Structures of Publicly Traded Thai Firms*

In order to understand the ownership structures of the largest publicly traded Thai firms, Claessens *et al.* offer the findings set forth in Table 1. The top fifteen wealthiest families in Thailand own 53.3% of the total value of listed corporate assets in their study.[156] This is in contrast to Japan's top fifteen families owning a mere 2.8% and Indonesia's top fifteen families owning as much as 61.7% of the total value of listed corporate assets.[157] When viewing the percentage of GDP owned by the top fifteen families of

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[149] *See id.*
[150] *Id.* at 110.
[151] *See id.* In general, "management of 60% of the firms that are not widely held is related to the family of the controlling shareholder." *Id.*
[152] *See id.* at 93-94.
[153] *See id.* at 99. "The separation of ownership and control is . . . lowest in the Philippines and Thailand." *Id.*
[154] *See id.* at 108. The top fifteen wealthiest families in Thailand own 39.3% of the country's GDP. *See id.* at 108 tbl.9.
[155] *See id.* at 103 tbl.6; Stijn Claessens, Simeon Djankov & Larry H.P. Lang, *Who Controls East Asian Corporations?* 32 tbl.4 (World Bank Pol'y Res., Working Paper No. 2054, Feb. 1999), *at* http://econ.worldbank.org/docs/345.pdf [hereinafter Claessens (1999)]. Both tables exhibit that Thai firms that are ultimately owned by large controlling stakeholders account for at least 90% of the firms sampled.
[156] Claessens et al., *supra* note 19, at 108 tbl.9.
[157] *See id.*

these Asian nations, the top fifteen families in Thailand only own about 39% of GDP which indicates that Thailand's capital markets are not as developed as Hong Kong's, where the top fifteen families own a mammoth 84.2% of the country's GDP.[158] Additionally, wealth in the majority of these East Asian nations is highly concentrated within the hands of a small number of families.

Table 1: How Concentrated is Family Control?[159]

Country	Average number of firms per family	% of total value of listed corporate assets that families control (1996)				% of GDP (1996)
		Top 1 family	**Top 5 families**	**Top 10 families**	**Top 15 families**	**Top 15 families**
Hong Kong	2.36	6.5	26.2	32.1	34.4	84.2
Indonesia	4.09	16.6	40.7	57.7	61.7	21.5
Japan	1.04	0.5	1.8	2.4	2.8	2.1
Korea	2.07	11.4	29.7	36.8	38.4	12.9
Malaysia	1.97	7.4	17.3	24.8	28.3	76.2
The Philippines	2.68	17.1	42.8	52.5	55.1	46.7
Singapore	1.26	6.4	19.5	26.6	29.9	48.3
Taiwan	1.17	4.0	14.5	18.4	20.1	17.0
Thailand	1.68	9.4	32.2	46.2	53.3	39.3

Furthermore, as indicated by the 1998 Securities and Exchange of Thailand Companies Handbook and set forth in Table 2, of the 167 publicly traded companies in Thailand, over 90% are owned by an ultimate owner[160] with a large stake of control rights.[161] Within that category, 51.9% are owned by a family, 24.1% by the state, 6.3% by a widely held financial company like a bank or an insurance company, and 9.5% by a widely held corporation.[162] Only a mere 8.2% of publicly traded Thai firms fall within the category of

[158] *See id.* at 108-09. This is in comparison to Japan where the largest fifteen families control corporate assets worth 2.1% of GDP and to the United States where the number is 2.9% of GDP. *See id.*
[159] *See id.* at 108 tbl.9.
[160] *See* Claessens (1999), *supra* note 155, 6, 8. "Ultimate control" may mean that firms "can have more than one significant owner." *Id.* at 8. Furthermore, Claessens (1999) discusses La Porta *et al.*'s finding that owners often extend their control over a firm

> through the use of pyramiding and management appointments, as well as through frequent cross-ownership and the use (less frequently) of shares that have more votes. Another interesting pattern is [that] . . . control of East Asian corporations can be achieved with significantly less than an absolute majority share of the stock, as the probability of being a single controlling owner through holding only 20% (or more) of the stock is very high. *Id.* at 6.

[161] *See id.* at 8, 32 tbl.4.
[162] *See id.* at 32 tbl.4.

widely held firms or firms without a large controlling shareholder.[163] In comparison to other East Asian nations, Japan and Korea have the highest share of widely held firms while only Hong Kong and Indonesia outrank Thailand with the highest proportion of family-held firms.[164]

Table 2: Control of Publicly Traded Companies in East Asia[165]

(weighted by market capitalization)

Country	Number of Corporations	Widely Held	Family	State	Widely Held Financial	Widely Held Corporation
Hong Kong	330	7.0	71.5	4.8	5.9	10.8
Indonesia	178	6.6	67.3	15.2	2.5	8.4
Japan	1,240	85.5	4.1	7.3	1.5	1.6
Korea	345	51.1	24.6	19.9	0.2	4.3
Malaysia	238	16.2	42.6	34.8	1.1	5.3
The Philippines	120	28.5	46.4	3.2	8.4	13.7
Singapore	221	7.6	44.8	40.1	2.7	4.8
Taiwan	141	28.0	45.5	3.3	5.4	17.8
Thailand	167	8.2	51.9	24.1	6.3	9.5

As mentioned earlier, scholars purport that a high proportion of widely held firms tends to be indicative of a more developed economy,[166] while a high proportion of concentrated control structure firms may hamper the development of institutions and legal rights.[167] Although arguments can be made that concentrated control within firms tends to diminish as economic development increases, readers should be cautioned that the evidence supporting this statement is still fairly premature due to the small number of firms sampled in each country.[168]

D. ALTERING OWNERSHIP IN THAILAND

1. *Keep the Controlling Shareholders or Disperse Ownership?*

The previous section illustrates how the majority of publicly traded Thai firms have concentrated ownership structures. How much of an

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[163] *See id.*
[164] *See id.*
[165] *Id.* The table has two main categories, widely held corporations and corporations with ultimate owners. *See id.* "Widely held" refers to corporations that do not have owners with significant control rights. *See id.* at 8. Corporations with "ultimate owners" are ultimately owned by (1) a family, (2) the state, (3) a widely held financial corporation such as a bank, or (4) a widely held corporation. *See id.*
[166] *See* Claessens et al., *supra* note 19, at 104.
[167] *See id.* at 109.
[168] *See id.* at 104.

impact does this type of firm feature have on a country's economy, corporate performance, and the development of good corporate governance patterns? General studies on concentrated ownership, corporate performance, and corporate governance investigate whether restructuring concentrated ownership firms, such as family and state-held firms, into widely held firm structures will improve corporate governance or whether concentrated ownership is not such a harmful feature for such firms.[169] Studies on Thai firms analyze similar questions by examining the level of concentration between ownership and control in publicly traded firms prior and subsequent to the Asian financial crisis.[170] Other researchers attempt to extract a relationship between the performances of non-financial Thai firms with highly concentrated ownership as compared to similar firms with less concentrated ownership structures.[171] As yet, however, economists are only able to show that the existence of certain country characteristics are consistent with concentrated ownership firms, but are unable to strongly argue that firms with dispersed ownership perform better than firms with controlling shareholders. Studies like La Porta *et al.* show that "countries with endemic corruption, with poor shareholder legal protection, corrupt judiciaries, and the like *tend* to have highly concentrated ownership . . . usually involv[ing] wealthy families with control pyramids."[172] Others hypothesize that controlling shareholders may borrow company assets for their own personal accounts, pay inflated prices to (or receive deflated prices from) other companies that they own, or engage in risky investment ventures with the knowledge and assurance that the costs of such investments will be spread to other shareholders.[173] In 2000, Claessens *et al.* offered interpretations of their data on East Asian firms that concentrated ownership may offer owners a greater incentive to expropriate minority stockholders' capital and that "[a] concentrated control structure of the whole corporate sector could lead to the suppression of minority rights and hold back the institutional development of legal and regulatory channels to enforce those rights."[174] Arguments supporting these statements stem from the fact that government officials are frequently involved in the ownership and control of the corporate sector,[175] which creates conflicts of interest across both the public and private sectors.[176] Advocates of dispersed ownership fear that the continued use of concentrated ownership

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[169] *See* Shleifer & Vishny, *supra* note 15, at 739.
[170] *See* Khanthavit et al., *supra* note 22, at 1.
[171] *See* Jira Yammeesri & Sudhir C. Lodh, *The Effects of Ownership Structure on Firm Performance: Evidence from Thailand* 3 (2003) (paper for inclusion in the Hawaii International Conference on Business), *available at* http://www.hicbusiness.org/biz2003proceedings/Jira%20Yammeesri.pdf (last visited Mar. 24, 2005).
[172] Randall Morck & Bernard Yeung, *Special Issues Relating to Corporate Governance and Family Control* 12 (World Bank Pol'y Res., Working Paper No. 3406, Sept. 2004), *at* http://econ.worldbank.org/files/38739_wps3406.pdf (emphasis added).
[173] *See* Yupana Wiwattanakantang, *Controlling Shareholders and Corporate Value: Evidence from Thailand*, 9 PAC.-BASIN FIN. J. 323, 327 (2001).
[174] Claessens et al., *supra* note 19, at 109.
[175] *See* Fagan, *supra* note 31, at 327. As mentioned earlier, Thailand's Prime Minister, Thaksin Shinawatra is also the wealthiest man in Thailand, owning the largest telecommunications company in the nation. *See supra* text accompanying note 52.
[176] *See* Claessens et al., *supra* note 19, at 109.

structures will allow public officials and corporate owners to further capitalize on their privileged positions at the expense of other shareholders and will continue to retard the development of institutions and legal enforcement mechanisms aimed at improving corporate governance.[177]

In 2004, however, the same scholars that attributed a lack of institutional development and poor corporate governance in countries like Thailand to concentrated ownership acknowledged that such ownership structures may actually be part of the corporate governance solution for countries with weak enforcement and underdeveloped institutions.[178] Generally, large shareholders with the largest stake in the firm have the wherewithal and the incentives to monitor a firm.[179] Further, in concentrated ownership firms, agency costs that would normally arise from using managers, who oftentimes do not have the best interests of shareholders in mind,[180] are mitigated[181] thus leading to the possibility of increased firm performance. Concentrated ownership aligns shareholders' rights (those receiving cash flow rights) and managers' rights (those receiving control rights) through the use of a large shareholder with at least a substantial minority ownership stake (10 to 20%).[182] This is especially important in countries with weak minority shareholder protection laws on the theory that, at the very least, the large controlling shareholder will have incentives to monitor bad business practices as they have much at stake within the firm. Scholars, however, offer the following cautionary analyses of managerial ownership at varying levels. At low levels of managerial ownership, management's incentives to maximize the firm's value exist.[183] At medium levels, management may be wealthy enough to exploit firm privileges unavailable to outside shareholders.[184] At high levels of managerial ownership though, management's high equity level is especially dependent on the firm's performance.[185] As a result, management will have fewer incentives to expropriate since they are unable to externalize any costs that arise from engaging in risky behavior.[186] Ultimately, Berglöf and Claessens recognize the pervasiveness of concentrated ownership firms in

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[177] *See id.*; Berglöf & Claessens, *supra* note 19, at 38 ("In Thailand senators blocked bankruptcy reforms, as they were also major owners of distressed corporations.").
[178] *See* Berglöf & Claessens, *supra* note 19, at 4, 38.
[179] *See* Shleifer & Vishny, *supra* note 15, at 754.
[180] *See id.* at 740-43. Agency costs generally arise in widely held firms when owners hire managers to run the firm but continuously worry about whether managers are appropriately allocating resources and improving the firm's performance rather than their own self-interests. *See id.*
[181] *See id.* at 754.
[182] *See id.* Claessens *et al.* also discovered that even though large shareholders may only own substantial minority ownership stakes (10 to 20%), their control rights often exceed their cash-flow rights through the use of control enhancement mechanisms—pyramid structures and cross-holding patterns. Claessens et al., *supra* note 19, at 93. Although Claessens *et al.* specifically finds that large controlling shareholders within Thai firms opt out of pyramid and cross-holding uses, Khanthavit *et al.* investigates the matter further and discovers that direct ownership is the most common form of ownership in publicly traded Thai firms. Khanthavit et al., *supra* note 22, at 8. However, in addition to direct ownership, controlling Thai shareholders often combine their direct shareholdings with either pyramids or pyramids and cross-holdings. *See id.* at 9.
[183] *See* Wiwattanakantang, *supra* note 173, at 330.
[184] *See id.*
[185] *See id.*
[186] *See id.* at 330-31.

developing economies and, therefore, argue that "[t]he challenge is not to undermine perhaps the most potent corporate governance mechanism in less developed economies, concentrated ownership, while at the same time mitigating the potential costs that come along with these ownership structures."[187]

2. *Comparing Thai Firms' Ownership Structures and Corporate Performance*

Studies published in 2001 that evaluated the effects of ownership structures (or, more specifically, controlling shareholders) on the corporate performance of publicly traded Thai firms from 1993 to 1996 made the following three findings. First, Thai firms with controlling shareholders tend to perform better than firms without controlling shareholders.[188] The reason for this may be because, as Shleifer and Vishny noted above, controlling shareholders have great incentives not to expropriate firm funds, as this may lead to discounted share prices on the market, and consequently, to controlling shareholders owning a large amount of discounted shares.[189] If controlling shareholders expropriate company funds or engage in self-dealing, they are unable to externalize the costs associated with such expropriation because they own a large stake of the company's shares.[190] Pedro Alba, Stijin Claessens, and Simeon Djankov qualify this first finding by noting that "[o]wnership concentration is positively (and significantly) related to profitability in 1992," but, in 1996, these same firms show deteriorating performance relative to firms with less concentrated ownership "(albeit not significant[ly])."[191] Reasons for deteriorating performance in 1996 may be due to the fact that these Thai firms with concentrated ownership were less likely to implement changes to corporate behavior or respond to changing market conditions between 1992 and 1996.[192] Second, family-controlled firms, foreign-controlled firms, and firms with multiple controlling shareholders have higher corporate performance than firms with no controlling shareholders.[193] This finding is in contrast to many scholars' repeated concerns that family firms place family interests over the corporation's[194] by, for example, appointing family members to top managerial positions which disadvantages the firm from employing the most suitable executive for the firm. On the other

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[187] Berglöf & Claessens, *supra* note 19, at 4.
[188] *See* Wiwattanakantang, *supra* note 173, at 326. *See also* Yammeesri & Lodh, *supra* note 171, at 12, 26. Wiwattanakantang's study uses the Stock Exchange of Thailand's definition of "controlling shareholder"—"an entity who owns more than 25% of [the] firm's shares directly, or indirectly." *Id.* at 336.
[189] *See* Wiwattanakantang, *supra* note 173, at 327-28 (reviewing other economists' literature on the pros and cons of controlling shareholders).
[190] *See id.* at 325.
[191] Pedro Alba, Stijin Claessens & Simeon Djankov, *Thailand's Corporate Financing and Governance Structures: Impact on Firms' Competitiveness* 17 (1998) (paper submitted for Conference on Thailand's Dynamic Economic Recovery and Competitiveness, May 20-21, 1998) *available at* http://www.worldbank.org/html/dec/Publications/Workpapers/wps2000series/wps2003/wps2003.pdf (last visited Nov. 23, 2005).
[192] *See id.*
[193] *See* Wiwattanakantang, *supra* note 173, at 326.
[194] *See id.* at 329.

hand, the evidence suggests that the advantages of family firms overshadow the disadvantages. Family firms have incentives to perpetually increase firm value because their wealth is connected to the performance of the firm, ownership of the firm typically continues down the family line, and the family's reputation and last name are often linked to the company's name.[195] In addition, foreign-controlled firms probably perform well because they are able to provide advanced technological resources that domestic firms may lack while firms with multiple controlling shareholders outperform firms with no controlling shareholder because numerous large shareholders may monitor the firm better.[196] Third, firms where controlling shareholders hold top executive positions perform worse than firms where controlling shareholders do not undertake control positions.[197] This finding is especially detrimental to firms where controlling shareholders with 25 to 50% ownership stakes engage in management of the firm.[198] To summarize, controlling shareholders, in particular family-controlled and foreign-controlled firms, are positively associated with corporate performance. Firms where controlling shareholders engage in managerial positions are negatively associated with corporate performance, and performance is especially impaired when controlling shareholders own 25 to 50% of the company.

In addition to the previously mentioned findings, analyzing the impact of the Asian financial crisis on changing ownership structures is important because it may show what private reform measures are being undertaken, unilaterally and bilaterally, by firms as a result of a serious "macroeconomic shock."[199] In a 2003 study, Anya Khanthavit, Piruna Polsiri, and Yupana Wiwattanakantang updated findings on publicly traded non-financial Thai firms by investigating the changing ownership structures of such firms prior to and subsequent to the Asian financial crisis.[200] The authors use 1996 as the pre-crisis year of comparison and 2000 as the post-crisis one.[201] Khanthavit *et al.* find that amongst non-financial publicly traded Thai firms, family-controlled firms[202] play a diminished role as they are being replaced by foreign investors (including financial institutions) and domestic financial institutions.[203] Firms with multiple controlling shareholders are also on the rise.[204] Additionally, the concentration of

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[195] *See id.*
[196] *See id.*
[197] *See id.* at 325.
[198] *See id.*
[199] *See* Khanthavit et al., *supra* note 22, at 1. Like Wiwattanakantang's study, Khanthavit *et al.*'s study uses the Stock Exchange of Thailand's definition of a "controlling shareholder"—"a shareholder who *directly* or *indirectly* owns more than 25 percent of a company's votes." *Id.* at 4.
[200] *See id.* at 1-2. Wiwattanakantang is one of the authors, discussed in the previous paragraph, who published a study in 2001.
[201] *See id.*
[202] *See id.* at 7. Although the proportion of family-controlled firms declined approximately 5% from 1996 to 2000, family-controlled firms are still the most prevalent ownership structures amongst non-financial firms traded in the Thai stock market. *See id.*
[203] *See id.* at 18-19.
[204] *See id.*

ownership and control in such firms has slightly increased,[205] which suggests that Thai firms continue to use direct ownership rather than indirect ownership or control enhancement mechanisms like pyramid structures and cross-holding patterns.[206] Finally, other scholars note that since the crisis, firms with state-controlled ownership are beginning to privatize at the urgency of international organizations that provide monetary assistance to Thailand.[207] Pressure from groups like the International Monetary Fund ("IMF"), the World Bank, and the Asian Development Bank should accelerate the much needed restructuring of longstanding state-owned enterprises (SOEs).[208] Many of these private reform measures, which were enacted during the post-crisis period, may not have directly resulted from the Asian financial crisis. Nevertheless, because they are occurring after the crisis, it is inevitable that reformers will approach these changes with the utmost caution so as to avoid the risk of developing deficient firms.

V. ANALYSIS OF PRIVATE REFORM MEASURES

A. Possible Implications of the Post-Crisis Private Reform Movement

As discussed above, the empirical evidence on non-financial publicly traded Thai firms indicates that ownership structures are already beginning to shift.[209] Each major change indicated in the previous section will be analyzed in terms of future benefits to Thailand's corporate governance framework and corporate performance.

First, family-controlled firms are decreasing in number.[210] On the other hand, firms controlled by foreign investors (including foreign financial institutions) and domestic financial institutions are, to some extent, more common in the post-crisis period than in the pre-crisis period.[211] This replacement of controlling shareholder types has two implications for Thailand's corporate sector. Foremost, as Mark Aguiar, Gita Gopinath, and John Romalis discovered, foreign acquisitions of target firms, especially those that lie within less developed emerging markets such as Thailand, add

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[205] Recall that concentrating ownership and control signifies that cash-flow rights are aligned with control rights.

[206] Khanthavit et al., *supra* note 22, at 19.

[207] *See* John R. Dempsey, Note, *Thailand's Privatization of State Owned Enterprises During the Economic Downturn*, 31 LAW & POL'Y INT'L BUS. 373, 373-74 (2000). "It now appears that the world has adopted the conventional wisdom that privatization is the best route to the development of competitive industries, the deepening of domestic and international capital supplies, and to continued economic growth in a world fixated on reducing commercial barriers and promoting a free market." *Id.* at 374.

[208] *See id.* at 389. When Thailand approached the IMF for a financial bailout in 1997, one of the conditions imposed upon Thailand was a sincere and effective effort at privatizing SOEs. *See id.*

[209] *See* Khanthavit et al., *supra* note 22, at 18-19; Wiwattanakantang, *supra* note 173, at 325-26; Yammeesri & Lodh, *supra* note 171, at 26.

[210] *See* Khanthavit et al., *supra* note 22, at 18.

[211] *See id.* at 19.

significant value to the target firms.[212] Although there is no evidence that foreign firms bring greater value to their targets as compared to domestic firms, the evidence may be biased since foreign firms generally target larger firms than do domestic firms.[213] The underlying benefit that foreign investors may bring to Thailand's corporate sector is a greater demand for more stringent accounting and disclosure standards from firms. "[F]oreign investors are willing to pay 27% more for equity shares of listed companies in the SET [Stock Exchange of Thailand] with good governance standing."[214] This remark clearly illustrates the premium foreign investors, retail and institutional, are willing to pay for Thai firms to clean up their corporate governance infrastructure. As more foreign investors become controlling shareholders of Thai firms, such firms should, unilaterally, begin implementing good corporate governance mechanisms. Aguiar *et al.* also detect that when foreign acquisitions of local target firms are announced, the stock values of firms in the same industry and country of the target firm tend to decrease.[215] This indicates a semi-efficient market where public information about a particular company has immediate or near immediate effects on competing companies within the same market.[216] If this is the case for the Thai market, having an influx of foreign owned firms within the Thai economy should mobilize disclosure and accounting standards across the board.

The second implication that may result from the decrease of family-controlled firms deals with the synchronous increase of both foreign and domestic institutional investors. These creditors or banks resemble other large shareholders but they also play the role of monitoring firms.[217] Banks become large shareholders by holding equity and debt of the firms in which they invest.[218] They also become monitors because they want to ensure that borrowers (the firms) will not default on their loans.[219] Shleifer and Vishny document that in order for large creditors to be effective monitors, they must also be able to enforce adequate legal rights.[220] Thailand already employs a bank-centered financial system where "banks[, rather than investors,] play the lead role in the monitoring of firms."[221] Since the financial crisis, Thailand established a new bankruptcy court and

[212] Mark Aguiar, Gita Gopinath & John Romalis, *The Value of Foreign Ownership* 8, 10, tbl.5 (Univ. Chi., Working Paper, Aug. 2003) (on file with author).
[213] *See id.* at 8-9.
[214] Deunden Nikomborirak, *An Assessment of the Role of Board of Directors in Building Good Governance: The Case of Thailand* 2 (2001) (paper submitted for Thail. Dev. Res. Inst. Conference, The Third Asian Round Table on Corporate Governance, The Role of Boards and Stakeholders in Corporate Governance, Apr. 4-5, 2001) *available at* http://www.oecd.org/dataoecd/51/32/1872778.pdf (last visited Nov. 23, 2005).
[215] *See* Aguiar et al., *supra* note 212, at 9-10.
[216] *See* JAMES D. COX, ROBERT W. HILLMAN & DONALD C. LANGEVOORT, SECURITIES REGULATION: CASES AND MATERIALS 101-02 (4th ed. 2004). The authors explain that "the semi-strong state of market efficiency uses information that is 'publicly available.'" *Id.* at 101.
[217] *See* Shleifer & Vishny, *supra* note 15, at 757-58.
[218] *See id.* at 757.
[219] *See id.*
[220] *Id.*
[221] Alba et al., *supra* note 191, at 4-5.

implemented new bankruptcy and foreclosure laws.[222] With an increased number of foreign banks acquiring Thai banks, lending practices should improve through more stringent "credit requirements and accounting standards."[223] Although loopholes in Thailand's current bankruptcy laws still exist,[224] improvements are being made and the increased number of financial institutions as controlling shareholders of Thai firms should act as a strong mechanism for improved corporate governance practices.

Second, an increased number of multiple controlling shareholders in Thai firms results in further monitoring of firm activities.[225] When there is more than one large shareholder, the incentive to monitor should increase from when there is only one controlling shareholder. This is because all the large shareholders (if they are acting as such) have the resources to monitor the firm, the incentive to ensure that they are receiving a proper return on their investment, and their role as a large controlling shareholder will reduce agency costs that typically arise in widely dispersed firms where managers run the firm.[226]

Third, non-financial publicly traded Thai firms concentrate their ownership and control rights even more during the post-crisis period.[227] They do so by using direct ownership measures rather than indirect ownership methods, those employing pyramid structures and cross-holdings.[228] In some cases, controlling shareholders combine their direct shareholdings with either pyramids or pyramids and cross-holdings, but for over two-thirds of these firms, direct ownership continues to be the method of choice.[229] The implications for direct ownership are, as explained above, that controlling shareholders may hold management positions and exploit firm resources unavailable to outside shareholders.[230] However, because this concern only exists when controlling shareholders own shares at the 25 to 50% level and subsides when they own shares at higher levels, the negative implications associated with direct ownership may be unfounded.[231]

Fourth and last, accelerating the privatization process of state-owned enterprises (SOEs) will significantly impact the corporate sector because such entities[232] will become publicly traded firms, bought and sold by individual investors, family firms, foreign investors, and institutional

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[222] *See* Overholt, *supra* note 2, at 1017-18.
[223] *See id.* at 1017.
[224] *See id.*
[225] *See* Wiwattanakantang, *supra* note 173, at 329, 359.
[226] *See* Shleifer & Vishny, *supra* note 15, at 754.
[227] *See* Khanthavit et al., *supra* note 22, at 19.
[228] *See id.* at 8-9, 19. Recall that "direct ownership" occurs when controlling shareholders own large stakes in a firm under their own name or under names of private companies directly held by them. *See supra* text accompanying note 38.
[229] *See id.* at 8-9.
[230] *See* Wiwattanakantang, *supra* note 173, at 330-31.
[231] *See supra* text accompanying notes 179-182, 193-94.
[232] Some 24% of publicly traded Thai firms are already controlled by the state. *See* Claessens et al. (1999), *supra* note 155, at 16, 32 tbl.4. Privatization measures are aimed at fully or partially privatizing SOEs fully held by the state or largely owned and controlled by the state. *See* Dempsey, *supra* note 206, at 377-78.

investors. Although the privatization effort is a part of the government's agenda, both the public and private sectors stand to benefit from the reform.[233] In countries with weak institutions, the privatization of SOEs will relieve the government from maintaining inefficient SOEs and allow further allocation of resources to the development of sound regulations and institutions.[234] In Thailand, John Dempsey records that although the private sector held "most of Thailand's eighty-nine billion dollars of foreign debt, . . . [t]he public sector, however, held nearly twenty billion dollars of this debt, largely due to the need of SOEs to tap international credit facilities to finance their operations."[235] Additionally, privatizing SOEs separates government tasks from private ones, further enhancing the government's appearance as an independent entity.[236] One of the major concerns of SOEs is that they provide the government and their employees with opportunities to exploit public funds.[237] "Non-benevolent governments," governments that do not always try to maximize social welfare, will "deliberately . . . transfer resources to supporters."[238] As Dempsey points out, the Thai government is this type of "non-benevolent government." Dempsey partially attributes the delayed privatization process in Thailand to "actors with vested interests — SOE employees, managers, [and] directors."[239] In sum, the main benefits for accelerating the privatization of SOEs in Thailand deal with transparency and independence, economic efficiency, and cost-effectiveness. First, there will be less concern for relationship-based transactions between the government and certain favored businesses since government institutions should operate independently of pressures from private actors.[240] Second, if private firms operate former SOEs, Thailand stands to gain both greater innovation and faster economic growth from these competitive industries. Third, privatization will allow the Thai government to allocate more resources to the development of effective institutions and courts, rather than waste public money on the maintenance of debt-ridden SOEs.

In conclusion, the ownership changes within publicly traded non-financial Thai firms made during the post-crisis period indicate significant potential for improving the corporate governance framework. Although family-controlled firms remain the most common controlling shareholder

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[233] *See supra* text accompanying note 64.
[234] *See* Enrico Perotti, *State Ownership: A Residual Role?* 5-6, 16 (World Bank Pol'y Res., Working Paper No, 3407, Sept. 2004)), *at* http://econ.worldbank.org/files/38740_wps3407.pdf.
[235] Dempsey, *supra* note 207, at 381 (asserting that SOEs held almost 25% of Thailand's $89 billion of debt).
[236] *See* Perotti, *supra* note 234, at 14, 16.
[237] *See* Andrei Shleifer, *State Versus Private Ownership*, 12 J. ECON. PERSP. 133, 141-42 (1998).
[238] *Id.* at 135, 141-42 (noting that private firms that support or have special relationships with the government presumably fit within the category of "supporters").
[239] Dempsey, *supra* note 207, at 375.
[240] *See* Shleifer, *supra* note 237, at 143. Shleifer cautions that, "the process of privatization is itself susceptible to corruption [since] . . . [i]n exchange for campaign contributions or bribes, politicians may award contracts or sell whole firms to inefficient providers, overpay these providers, fail to make them accountable for quality, and even fail to enforce those contracts." *Id.* Theoretically, "a corrupt government is less able to privatize, regulate or contract in the public interest, but is also less able to run enterprises in the public interest." *Id.* Thailand's privatization process may, therefore, be tainted by special contracts and sales that are awarded to favored firms. *See id.*

type, the addition of new domestic institutional and foreign investors will help monitor the accounting and disclosure standards of Thai firms and, hopefully, improve the corporate governance structures of firms. In the process, perhaps these new investors will recognize the importance of transparency and disclosure by allowing minority shareholders to receive an increased amount of information about the firm. Foreign investors will improve the economy by bringing technological know-how to Thai firms. Institutional investors will accelerate the process of reforming bankruptcy and debtor/creditor laws. With an increased number of Thai firms owned by multiple controlling shareholders, there will be greater incentives to monitor firm activities and agency costs will also be reduced. The continued use of direct concentrated ownership structures may be beneficial to corporate performance when managers hold a low level or a high level of shares, but probably not when they hold between 25 and 50% of the firm's shares. Finally, the further privatization of SOEs should allow the Thai government to focus its efforts and resources on cleaning up the government's reputation, bulking up institutional structures, and developing more effectively enforced public laws.

VI. CONCLUSION

After Thailand experienced the 1997 Asian financial crisis, questions relating to political, public, and private reform permeated the country's corporate governance debate. Local and foreign economists argued about the most effective and efficient ways to improve Thailand's less-than-perfect corporate governance infrastructure. It was not that Thailand's corporate governance practices were necessarily worse than its neighbors, but in order for the country to mobilize much needed foreign capital and to instill investors' faith in a floundering economy, corporate governance standards needed to be improved and firms had to seriously abide by the rule of law.

Initially, public reform measures aimed at improving the SEC's effectiveness in policing white collar crime and monitoring firms' adherence to SEC rules and regulations offered outside investors a glimpse of Thailand's commitment to improving corporate governance. On a larger scale, Thailand's revised Constitution offered greater rights to citizens and promised to promote the transparency of all government agencies and officials. This glimmer of hope, however, should largely be viewed in light of the realities existent in Thailand's legal and political culture. Thailand's legal problems arise from the inability of courts and regulators to effectively punish wrongdoers while its political issues range from a lack of transparency to the privileged status afforded government officials and wealthy elites. These public reform obstacles run deep and are in fact cultural issues that are difficult to alter over a short period. Corporate governance, therefore, cannot be promptly altered through public reform measures.

Instead, to improve its corporate governance infrastructure, Thailand should focus on using private reform measures adopted unilaterally by firms, bilaterally by two firms, and multilaterally by entire industries. On a macroscopic level, private reform aimed at altering the ownership structures of publicly traded non-financial Thai firms will speed up corporate governance reform and may influence the development of more efficient public laws. Since over half of these firms are family-controlled, replacing traditional controlling shareholders (family firms) with foreign and institutional investors rather than with widely dispersed ownership structures may serve as an expedited means of offering firms incentives for change. Foreign and institutional investors may demand higher accounting and disclosure standards, which results in better monitoring of firms. Additionally, encouraging firms to be held by multiple controlling shareholders may allow for similar results. Although the benefits of highly concentrated ownership structures are as yet unclear, Thai firms should balance the concentration of high ownership and control rights with the assurance to investors that resources are not being misappropriated and opportunities are not being exploited. Furthermore, the privatization of SOEs will offer the private sector an opportunity to develop efficient and competitive industries while making available more resources and opportunities for the government to create sound legal institutions. The point is that private sector reforms work faster (and sometimes more successfully) than public reform measures as they are not hindered by the "bureaucratic red-tape"[241] public actors must endure. Therefore, Thailand should encourage and emphasize the use of private actors, such as firms, to adopt means for enhancing corporate governance, rather than simply anticipate and await slow-coming institutional or cultural reform in the political and public spheres.

Although this Note serves as a preliminary study on the benefits of using private promotion to improve corporate governance, Thailand should further investigate and identify specific mechanisms that may encourage or discourage private reform. The following three areas are designated by some as potential frontiers for improving corporate governance through the private sector:

1. The government should encourage self-regulatory agencies or private authorities to create more stringent standards such as those relating to licensing in the auditing and accounting profession.[242] Thailand's Institute of Certified Accountants and Auditors of Thailand ("ICAAT") needs to improve weaknesses in "accounting rules, certification [of qualified accountants], and enforcement of a code of ethics."[243] In the future, ICAAT

[241] *See* Dempsey, *supra* note 207, at 387.
[242] *See* Alba et al., *supra* note 191, at 16.
[243] *Id.*

aims to align all relevant Thai accounting rules with those stipulated in the International Accounting Standard.[244]

2. Centers like the Thai Institute of Directors ("IOD") and the recently created Corporate Governance Center ("CGC") will serve as crucial multilateral enforcement mechanisms. The IOD offers certification and training programs for directors that are especially encouraged for those sitting on the boards of SET-listed companies.[245] The CGC, in conjunction with the SET, aims to improve corporate governance by educating and working with firms to develop internal corporate governance infrastructures.[246]

3. Although the SET has implemented new corporate governance regulations such as allowing shareholders, rather than boards of directors, to approve or disprove interested or related party transactions,[247] firms should unilaterally create additional mechanisms for protecting shareholders' rights.[248] For example, most of the major mechanisms for enhancing shareholder protection already exist under Thai law, but the minimum share requirements for utilizing these mechanisms are much higher than in most other countries.[249] Firms should, therefore, lower the share requirements for exercising these rights. Other firm-initiated shareholder protection mechanisms deal with the creation of committees, such as independent audit committees and separate remuneration committees.[250] This area looks to be quite promising in light of the fact that many companies implemented independent audit committees prior to the 1999 deadline presented by the SEC and SET.[251] Furthermore, as of 1999, firms with "significant foreign [equity] holdings" were unilaterally implementing

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[244] *See* Thail. Investor Serv. Ctr., *Accounting Standard*, http://www.thailandoutlook.com/thailandoutlook1/capital+market/corporate+governance/Accounting+Standard/ (last visited Mar. 24, 2005).

[245] *See* Thai Inst. of Dirs., *supra* note 130.

[246] *See* Alba et al., *supra* note 191, at 13. In a 1997 Price Waterhouse survey of 202 SET-listed companies, the majority of firms vouching to improve corporate governance practices preferred a method whereby the SET and a system of self regulation implemented corporate governance mechanisms. *See id.* As a result, the CGC was created in 2002. *See id.*

[247] *See* Nikomborirak, *supra* note 214, at 9.

[248] *See* Limpaphayom, *supra* note 11, at 247-48. Of forty-six firms surveyed in a 1999 Asian Development Bank study, twenty-eight complied with SET regulations dealing with interested and related party transactions. *See id.*

[249] *See* Nikomborirak & Tangkitvanich, *supra* note 3, at 17.

[250] *See* Nikomborirak, *supra* note 214, at 19-20.

[251] *See id.* at 17.

remuneration committees to enhance "the transparency and efficiency in personnel management."[252]

These considerations only touch upon the surface of private reform mechanisms, but, at the very least, there is real evidence that the private sector is beginning to understand the potential benefits implicit in transforming its corporate governance culture.

[252] *Id.* at 20.