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Boards that govern and lead

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What can and should we really expect from corporate boards? It is widely agreed among practitioners and scholars that boards are legally assumed to govern, guide and lead organizations toward opportunities that create value and reduce threatening risks, all on behalf of shareholders and stakeholders.

What should Indonesian organizations (both listed and unlisted) expect from their boards, and by extension their owners? One of the authors, a former president director of PT Telkom Indonesia and PT Pertamina, among the biggest corporations in Indonesia, shares his experience of more than five decades and expresses the specific challenges that boards at state-owned enterprises, but also

private organizations, may face. We back up our views with solid academic research and our own experience as governance and risk consultants in Asia for more than three decades.

What to expect?

Boards and their chairmen can be quite powerful, especially under single-tier boards where the function of chairman and chief executive officer is often combined. In the United States, in about 68 percent of the cases, the CEO combines this executive title with chairmanship of the board, making him or her extremely powerful. Cases such as Enron and Disney in the early 2000s showed that it is very hard to challenge such powerful chairmen-CEOs, and that entrenched boards may be too loyal decision makers, without being critical enough to optimize the creation of sustainable value for the organization. In Indonesia, the law requires the separation of the chairman (president commissioner) and CEO (president director) by having a dual-tier board structure.

Nonetheless, dual-tier boards in Indonesia still face very daunting challenges. Despite, the legal separation between those two functions, quite often the founder entrepreneur of the company remains at the helm of the company, usually as president commissioner or non-executive chairman of the supervisory board (board of commissioners). And for state-owned enterprises, the chair has often been a political appointment, complicating the objective to optimize organizational value creation.

Care, loyalty and prudence

Organizations can and should expect their board and managers to fulfill their respective fiduciary duties. A fiduciary duty (of loyalty, care and prudence) to the organization is essentially a legal relationship of confidence or trust between two or more parties, most commonly a fiduciary or trustee and a principal or beneficiary, who justifiably reposes confidence, good faith and reliance on his or her trustee. The fiduciary is expected to act for the sole benefit and interests of the principal, with loyalty to those interests.

The whole question boils down to “who” is this principal: are we referring to the long-term interests of the organization for which one works, or for the capital providers, investors or owners of the organization? Mainstream financial economics have veered toward the latter. However, we believe that this shareholder model has resulted in behavior by the trustees that may not be in the long-term interest of the organization as such. Owners or investors seem to be allowed to do anything with “their” organization to which they provided capital, even if that is at the expense of the long-term interest of the organization. We argue that theoretically it would make more sense to take the fiduciary duties to the organization

and stakeholders' interests into account. However, this is extremely difficult to materialize, be it in state-owned enterprises or in family-listed companies.

It is important to note that the typical "agency" problem – as it is defined in a Western context – in Indonesia and other Asian countries needs to be understood slightly differently. Although it is obvious that the top executives may use their privileged position and access to asymmetric information as a way to optimize their own short-term objectives instead of "maximizing shareholder value," it is exactly the task of a supervisory board to oversee and thus monitor the performance of the top executives. Executives at both state-owned enterprises and privately held enterprises make decisions on a daily basis that are supposed to serve the organization. However, quite often those decisions may better themselves at the expense of other parties related to the firm: those costs are known as agency costs, which find their roots in the separation of ownership and top management. A system of checks and balances – the basis of corporate governance is assumed to lessen those agency costs by controlling and monitoring top management.

In an Asian context, however, the typical agency challenge between managers and owners is often minimized by an inspiring and revered patriarch or a powerful leader of an SOE to a much more important challenge: the prevailing potential of abuse of power by the controlling family or state, the ultimate owners of a publicly listed company or state-owned enterprise, at the expense of minority shareholders, be it local or international and foreign shareholders. This potential conflict of interest between a majority principal versus minority principal can be detrimental to the long-term objectives of the organization, especially in listed SOEs. Obviously, majority owners, be it the family patriarch or state, can make final decisions, but that should not be at the expense of minority shareholders. How then to (1) rein in this king-entrepreneur who heads the board while still being able to tap into the founder's expertise and experience, and (2) limit the potential interventions through "parachuted" politically appointed commissioners at SOEs? In other words, how do we make Indonesian boards more effective while reducing potential entrenchment?

Corporate governance refers to the system of check and balances within an organization that takes optimal strategic decisions to create value, and that monitors its executive directors to execute strategies according to the objectives and to reduce risks where deemed necessary. Creating and sustaining organizational value fundamentally requires trust and cooperation among its board members, not just mere legal compliance to rules and regulations. Chairmen and CEOs are also aware that they, and not just the regulators, may need to lead the way forward. Massive corporate governance changes have swept through corporate boardrooms, affecting the way companies report earnings, pay executives and manage board and societal

expectations.

Governance may not fully prevent misconduct or misdeeds, but it can actually improve the way a corporation is run in Indonesia and for that matter in other Asian countries. One usually refers to successful companies that apply “best” [international] corporate governance principles which always need to be contextualized. The principles of the Organization for Economic Cooperation and Development (OECD), for instance, define good corporate governance as a set of relationships between a company’s management, its board, its shareholders and other stakeholders. Corporate governance not only provides

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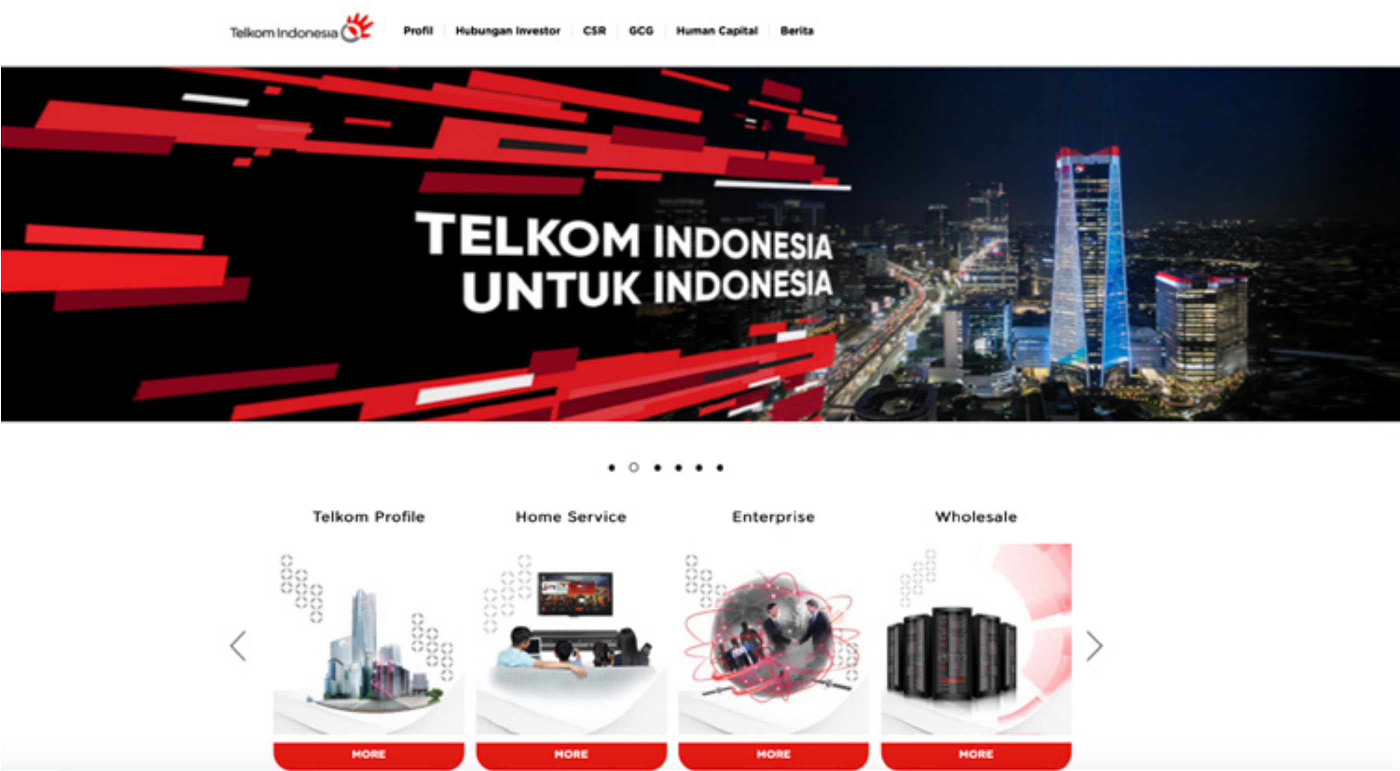
the structure through which the objectives of the company are set, but also the means of attaining those objectives and the ultimate organizational power to monitor the performance of the organization. The OECD’s Corporate Governance Principles (GCG) prescribe that a corporate governance framework should ensure the strategic guidance of the company, the effective monitoring of management by the board and the board’s accountability to the company and the shareholders. Indeed, corporate governance can be perceived as the collection of control mechanisms that an organization adopts to prevent or dissuade potentially self-interested managers from engaging in activities detrimental to the welfare of shareholders and stakeholders.

The OECD’s GCG – being taken over by the Indonesian code for good corporate governance – contains the following basic principles: (1) ensuring the basis for an effective corporate governance framework – the framework should promote transparent and efficient markets, be consistent with the rule of law and clearly articulate the division of responsibilities among different supervisory, regulatory and enforcement authorities; (2) the rights of shareholders and key ownership functions – the framework should protect and facilitate the exercise of shareholders’ rights. The basic shareholder rights should include the right to secure methods of ownership registration, to convey or transfer shares, to obtain relevant and material information on the corporation on a timely and regular basis, to participate and vote in general shareholder meetings, to elect and remove members of the board and to share in the profits of the corporation; (3) the equitable treatment of shareholders – the corporate governance framework should ensure the equitable treatment of all shareholders, including minority and foreign shareholders. All shareholders should have the opportunity to obtain effective redress for violation of their rights; (4) the role of stakeholders in corporate governance – the framework should recognize the rights of stakeholders established by law or through



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mutual agreements and encourage active cooperation between corporations and stakeholders in creating wealth, jobs and the sustainability of financially sound enterprises; (5) disclosure and transparency – the corporate governance framework should ensure that timely and accurate disclosure is made on all material matters regarding the corporation, including the financial situation, performance, ownership and governance of the company; and (6) the responsibilities of the board – the corporate governance framework should ensure the strategic guidance of the company, the effective monitoring of management by the board, and the board's accountability to the company and the shareholders.

The danger of entrenchment and mismanagement

Good corporate governance should therefore provide proper incentives for a board and its management to pursue objectives that are in line with the interests of the company and its shareholders.

Under the dual-tier board structure, the supervisory board of commissioners' main task is to monitor and oversee the performance of the (executive) board of directors and the continuity of the organization, aiming to ensure management that it is acting in the best interest of the company's long-term goals. In addition, the nonexecutive directors or commissioners

provide valuable advice and mentoring to top management. In this advisory capacity, the board pays attention to guide top management's decisions that balance risk and reward. The board is a governing body elected to represent the interests of shareholders and the company at large. Interpreting this in an Indonesian context, we believe that boards should not just supervise and govern the organization, but under certain circumstances should also lead.

Concretely, it means that any board should aim (1) to supervise or monitor the performance of the top executives to ensure that performance objectives are met and the oversight of the organization in general, including to sign off and be discharged on audit reports guarantee; (2) to coach and assist the management team to strategize potential business opportunities and pursue risks within agreed risk appetite borders; and finally (3) to develop leaders and to prepare leadership succession and the future nominations of new leaders.

Implementing these three supervisory board objectives has been a serious challenge at both Telkom and Pertamina, and likely other SOEs, where neither "consistency" nor optimizing financial performance seemed to have been an immediate "directive" or priority by the minister(s), representing the state as owner. Moreover, the continuous political influence and entrenchment made it hard for those SOEs to fully "professionally" function as an organization.

Let us get back to the fiduciary duties of the nonexecutive (BoC) and executive (BoD) board to clarify this request for professionalism. The functionality of any board is expressed through the fiduciary duties of its executives and nonexecutive board members to optimize organizational value, often (misquoted as maximizing shareholders' value). The fiduciary duty of a board usually includes a duty of care that requires directors to make decisions with due deliberation, a duty of loyalty that addresses conflicts of interest whereby the interests of shareholders should prevail over the interests of a director, and a duty of candor that requires that management and the board inform shareholders of all information that is important in their evaluation of the company and its management. These fiduciary duties are often translated in the legal requirement of having at least two or three professionally run subcommittees at the board: (1) a committee of internal audit and internal control to contain accounting and other specific risks; (2) a nomination committee that explicitly safeguards that the best professional CEO will be chosen; (3) a remuneration committee that decides on an appropriate and fair remuneration package for its top managers; and sometimes (4) a subcommittee to assess the risks that are allied to the suggested strategy.

Governance systems are influenced by the owners of the firm, its managers, creditors, labor unions, customers, suppliers, investment analysts, the media and regulators; in other words, relevant stakeholders and all those who could

significantly affect the value of the company.

In practice, supervising nonexecutive directors – board of commissioners in Indonesia – spend most of their time on supervising audit reports and on the determination of executive compensation according to monitored performances, and making sure that activities are performed according to and compliant with existing regulatory norms, while they unfortunately spend less time on advising management on strategic planning, competition and on preparing for leadership succession planning. However, co-author Tanri Abeng is convinced that a dual-tier board structure, where the supervisory board supervises and advises the executive board, should also function as a single-tier unified board in which the two boards collaborate as dancing partners. The former chair at Telkom made sure that both the supervisory board and the executive team were fully in sync with respect to important strategic decisions they jointly made that determined the future of the organization.

How relevant are the expected changes for "better" corporate governance for firms in Indonesia, now that a new cabinet under Indonesian President Joko Widodo is operational? And how can the new and powerful minister of SOEs, former media tycoon Erick Thohir, ensure that the dual-tier boards of SOEs are effectively organized?

Academic research indicates that in countries with relatively low legal protection for minority investors, controlling shareholders may be inclined to expropriate assets at the expensive of these minority shareholders, resulting in "private benefits of control." This kind of destructive entrenchment can be materialized by both powerful families that disregard minority shareholder rights, as well as political involvement and unnecessary mingling in daily operations by leaders of boards of state-owned enterprises.

The risk of expropriation of minority shareholders by large controlling shareholders is an important principal problem in most emerging countries, and even more so in Indonesia, where that gap between control and cashflow rights may be less outspoken and where both voting and cash flow rights are relatively among the highest (concentrated ownership) in Asia.

This possible entrenchment between owners, boards and to a lesser extent managers, or "tunneling effect," often outweighs the possible alignment effect in these family businesses. Tunneling is accomplished when resources are transferred from the company to the controlling shareholder through intercompany dealings whose terms favor the company in which the controlling shareholder has the larger equity stake. When an insider BoC, following orders from the "boss" (the family patriarch,) is heavily entrenched with management, there is an increased potential for expropriation of those minority shareholders' rights in family businesses. In state-owned enterprises, the risk of political involvement and entrenchment is always present

when the state intervenes or appoints board members as political alliances on those boards. Or when the minister, as the "owner" of the organization, regularly intervenes in a board's functions. We believe that the owner or state should limit itself to appoint the right board members who then should properly govern, lead where necessary and execute (in case of the BoD) the strategy of the firm in a professional and consistent manner, in line with its fiduciary duties.

In Indonesia – and in most Asian contexts – the capital market is characterized by very concentrated ownership, be it by a controlling family or a mighty state company, which may squash minority shareholders' rights. Most of the board members of these companies are consequently insiders, and not independent of the controlling shareholders. It is therefore of the utmost importance to safeguard equal shareholders' rights, have proper accountability and transparency and guarantee proper disclosure of relevant financial and nonfinancial information. In these Asian markets, minority rights are often not adequately protected. Moreover, in Indonesia (and in Asia in general), there is a hardly an active take-over market, and new market capitalization is underdeveloped compared to their Western counterparts.

Dual-tier board at Indonesian SOEs

There is a huge difference between dual-tier and single-tier boards. The major difference is that dual-tier boards have legally engrained a supervisory board in the board structure of an organization, whereas single-tier boards do not have such a separated supervisory board.

Both systems have advantages and disadvantages: a dual-tier board has proper supervisory structures in place to monitor the performance of the executive board members and limit the power of the top executive if deemed appropriate. Single-tier boards are usually more "unified" in making swifter strategic decisions to adapt to changed market conditions, and the CEO can be quite powerful, resulting in taking advantage of asymmetric information that may result in an agency problem. And even the chairperson (often combining the function with the CEO function in the United States) can be more hands-on under those structures.

Leading a company requires a lot of dedication and commitment by a professional board. We believe that if properly handled, dual-tier boards can leverage their natural advantage of proper governance and supervision, while also using the "natural Indonesian culture" of "unity in diversity," which allows the two distinctive boards to "team up" in a more cooperative and empowering manner by jointly focusing on main risks and major strategic decisions to steer toward a more competitive and productive organization. More broadly, when we apply those board challenges to companies in Indonesia, and especially to state-owned enterprises such as PT Telkom and PT Pertamina, the following issues should draw most of the

attention.

First, the lack of commitment by the supervisory board (BoC) to assist the management board (BoD). A primary task of a supervisory board – the board of commissioners – is to supervise and monitor the performance of the board of executive directors.

How can the chairman assure that the supervisory board collaborates with the executive board to ensure optimization of organizational value creation and preservation, while at the same time, walking that fine line of supervisor/ collaborator to also secure the necessary

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check and balances? At PT Telkom, the chair of the supervisory board did involve the executive board to assess, analyze and debate major risks that could affect certain major investment decisions. Any investment that strategically would affect PT Telkom was jointly decided by the two boards, guaranteeing they were on the same page, unifying the two distinctive boards and empowering both to fulfill their fiduciary duties of care, loyalty and prudence to make the right decisions that benefitted the organization.

Unfortunately, a similar fiat and performance was not exactly repeated or achieved at PT Pertamina because of many factors, among which were: (a) a lack of consistency, with PT Pertamina having appointed three CEOs during the previous five years, making it extremely difficult to create a cohesive and empowered team; (b) too many vested [political] interests; (c) having the unfortunate reputation of long-term corruption, collusion and nepotism; and (d) local fiefdoms that were hard to break up.

Second, patronage in board appointments by the majority owner (the state) and other vested political parties. We all have heard of stories where friends or acquaintances are appointed to boards to "look after" the interests of their respective patrons who put them on that board. Such practices often result in blatant nepotism and even corruption, where the interests of the particular boss or political party will prevail over the generic interest of the organization.

How can boards avoid unnecessary and often harmful political intervention in appointments of board members at SOEs? At PT Telkom, listed on the New York Stock Exchange and the Indonesia Stock Exchange, proper and very strict governance procedures were in place to guarantee proper adherence to predetermined rules, keeping it from becoming too dependent on the whims of too powerful and politicized owners. Unfortunately, at PT Pertamina, fully owned by the state, such strict

predetermined and market- enforced procedures do not apply. The result is that Pertamina has been run since its inception as a fiefdom of the powerful Indonesian political elite.

Moreover, to change a board, Pertamina's owner does not have to argue at an extraordinary shareholders meeting why there is a need to change the board; the minister of SOEs just calls in the relevant parties and single-handedly changes the chairperson, CEO or the whole board according to his or her discretion. Obviously, a similar debate on governance takes place between more "democratic" institutions versus more "authoritarian" regimes, both having pros and cons.

Third, lack of board skills to properly govern and lead the organization. As in any profession, board members need to have the necessary skills to govern and lead an organization or a board. Often, Indonesian boards are stacked with "friendly" members whose tasks are to protect the interests of the one who put them there, and not to genuinely provide guidance to management to enhance opportunities and reduce risk. What kind of leadership skill set is expected from board members, both commissioners and executive directors?

To assist the state, it can be suggested that to have the right people in charge of making crucial decisions at important SOEs, one installs a selection committee assisting the minister of SOEs. It would secure a reasonable and objective process helping the minister to appoint the appropriate team to the boards of SOEs. Indeed, the purpose of this selection committee is to recommend the right people to the minister of SOEs, after a thorough independent "search and select" process of leader candidates with the right skill set, impeccable integrity and proper management or leadership qualifications to govern or to steer, to lead and to execute the proper decisions. Candidates for a position of commissioner (or director), selected and recommended by this committee, with the envisaged right skill set and leadership qualifications, will help to empower the supervisory board to collaborate with the executive team, while also being accountable for monitoring the executive board. A supervisory board with professionals who know how to govern and to lead an organization will likely make better decisions in terms of risk management, strategy and development, and selection of capable, qualified people who are able to lead and execute major decisions.

Fourth, the decisiveness of boards and their board members (BoC and BoD). When boards make decisions, their members need to be decisive and take responsibility for their decisions, as well as be accountable for the consequences these decisions carry. Historically and culturally, one often sees that members of the board of directors will postpone decisions by pushing the buck to the supervisory board for "approval" because of the increased fear of doing something wrong. So boards, especially at state-owned enterprises, have become very ineffective and indecisive, undermining

their ultimate tasks.

How can the functioning of boards (BoC and BoD) be improved to ensure real collaboration and joint responsibility? How do you create a well-functioning board that takes advantage of the Indonesian dual-tier board structure while acting as a unified board? By empowering the senior supervisory board to advise, coach and collaborate with the executive board on strategic decisions, while also monitoring the performance of the executive board (BoD), PT Telkom was able to significantly improve its overall productivity and become a competitive player in the deregulated telecommunications industry.

Fifth, how do you implement real accountability on a board? When boards hide out of fear of wrongdoing, hardly any substantial decisions will be made, aggravating their ineffectiveness. Being collegial on a board does not mean avoiding tough decisions or disagreements. In the end, a board makes a unified decision, although individual disagreements can be noted in the board notes, and all board members should be accountable for decisions made.

How do you improve the accountability of a collegial board while improving incentivized performances? How do you avoid the silo mentality of individual board members? Boards take the final and ultimate responsibility for the performance of an organization, be it a state-owned enterprise such as PT Pertamina, a family company, a listed company with many different shareholders, a privately held company or a nongovernmental organization. All are bound by evaluating the performance of the board and its executives to the agreed objectives and goals of the organization. Corporate governance can and should be established at any organization, publicly listed or not, privately held or state owned. These good corporate governance principles that can and should be contextualized for any specific company will help firms to reduce threatening risks and guarantee that proper decisions are made according to established procedures and rules to safeguard the integrity of the organization – and not fall in the trap of particular interests (often vested) at the expense of the organization.

One could easily argue that good corporate governance is established through a combination of (1) the right people; (2) the right team; (3) the right processes; (4) the right culture; (5) the right information; (6) the right guidance; and (7) the right oversight.

As established above, the key principles of good corporate governance are ensuring that consistency, responsibility, accountability, fairness, transparency and effectiveness are deployed throughout an organization. Governance is much more than compliance. Good corporate governance is a question of culture and a climate to apply these best principles, which is the foundation of trust. Boards need to create trustworthy relationships, providing guidance and oversight to the directors and management in order to ensure that the

company creates value on a sustainable basis while protecting the interests of all stakeholders.

The shareholders should make sure that the roles of the board are properly defined and the duties of each of the directors are well understood and specified. Moreover, the board composition and committees' structure should be clarified. Finally, the board's working procedures and functions should be clearly expressed and documented, whereas desired board practices should be spelled out in the notes or constitution of the company. Usually, these factors are well taken care of at most SOEs. However, the actual implementation according to the spirit of the rules and regulations is another matter.

In the case of Pertamina and Telkom, Tanri Abeng, a former president commissioner of both companies, is convinced that the two following factors should be given priority: (1) openness and transparency in decision-making; and (2) installing and agreeing on objectives that are specific and for which one can account for, reducing the burdensome silo mentality that prevails on many boards of SOEs. It also means that the chairman who chairs the board meetings collaborates with the executive board on developing and providing a strategy. The supervisory board should be involved with the selection of the CEO and should be responsible to set the tone from the top in terms of ethical integrity among all its board members. The supervisory board should also take charge of the *modus operandi* of board functions and the professional competence of all board members. Moreover, the supervisory board should partner with the executive board and the owners on risk appetite, the development of a talent pool, installing a culture of decisiveness and on potential mergers and acquisitions and subsequent resource allocation.

Running and steering a huge company is always difficult, and taking charge of a corporation such as Pertamina is even more daunting. Regrettably, Tanri was not fully able to install the right structure at Pertamina and make it a leaner organization. Today, the organization features 11 executive boards of directors – not exactly the example of a nimble board. It somehow seems to be the ultimate reflection of the Indonesian state, President Joko's current and rather bloated cabinet, which attempts to accommodate numerous political interests. Maybe it is part of the culture to pacify all interests in a unified manner.

Tanri graciously admits that he did not fully succeed either during his term as chair of Pertamina in putting all the right people in the right places. His successor may want to focus on this unfinished task of developing the right professionals for leadership positions within Pertamina, to secure appropriate succession within the firm and withstand unproductive political interventions, and to safeguard the competitive survival of the firm. We presume that one could see a tradeoff between efficiency and effectiveness on one hand, which is the main task of any board at

any organization, and vested multi-interests and entrenchment of the owners (with different parties all vying for the assets of the SOE) that often are not necessarily aligned with the organization's objectives, on the other hand.

We strongly believe that one cannot serve two masters. Then, how to determine the accountability of the board members of SOEs? Should they serve their political masters as we often see today, or should we expect a board to be fully accountable for the objectives of the organization it represents and serves? Foremost and above all, the board should professionally focus on the organization's objectives, which should take priority over political interests. However, the objective of running an SOE as effectively and efficiently as possible does not necessarily mean that there is only one financial objective to be pursued – as in a mainstream Anglo-Saxon context to "maximize" profitability or shareholder value only. It is quite possible that the dual-tier boards of an SOE will adhere to a "stakeholder" model with different stakes to be fulfilled. However, those stakes and objectives should be transparently, clearly and properly defined to avoid any fuzziness. Too much "discretion" and entrenchment by powerful political elites involved in boards' functions should be avoided for the sake of more open and transparent communication. The organizational (and thus not political) objectives of the SOE – they may include the employment of Indonesian staff or stable energy provision security within particular benchmarks, next to financial and operational objectives – should be clearly defined, assessed and analyzed.

Allow us to reiterate the fiduciary duties of the dual-tier board: once the decision on the direction of the strategy is jointly made by the BoC and BoD, the BoD or executive board is responsible and accountable for its execution. Nonetheless, the supervisory board will oversee the performance of the executive board and supervise the BoD's execution, but won't and shouldn't be involved in the actual execution of the strategy (which is the BoD's task). One of the authors was asked as chairman to "intervene" in the executive management "to make the needed change happen," which would have overstepped the fiduciary duty of the supervisory board. It is as if asking the well-regarded Zinedine Zidane to get on the pitch for his Real Madrid soccer team, which would likely not be considered appropriate either: as head coach and supervisor (though he himself used to be a top player for the same club) Zidane is assessing, selecting, monitoring and steering his team to remain a world-class champion. The execution of Zidane's strategy and tactics is entirely up to the team itself. Both have a clearly defined and interdependent role to play in order to succeed.

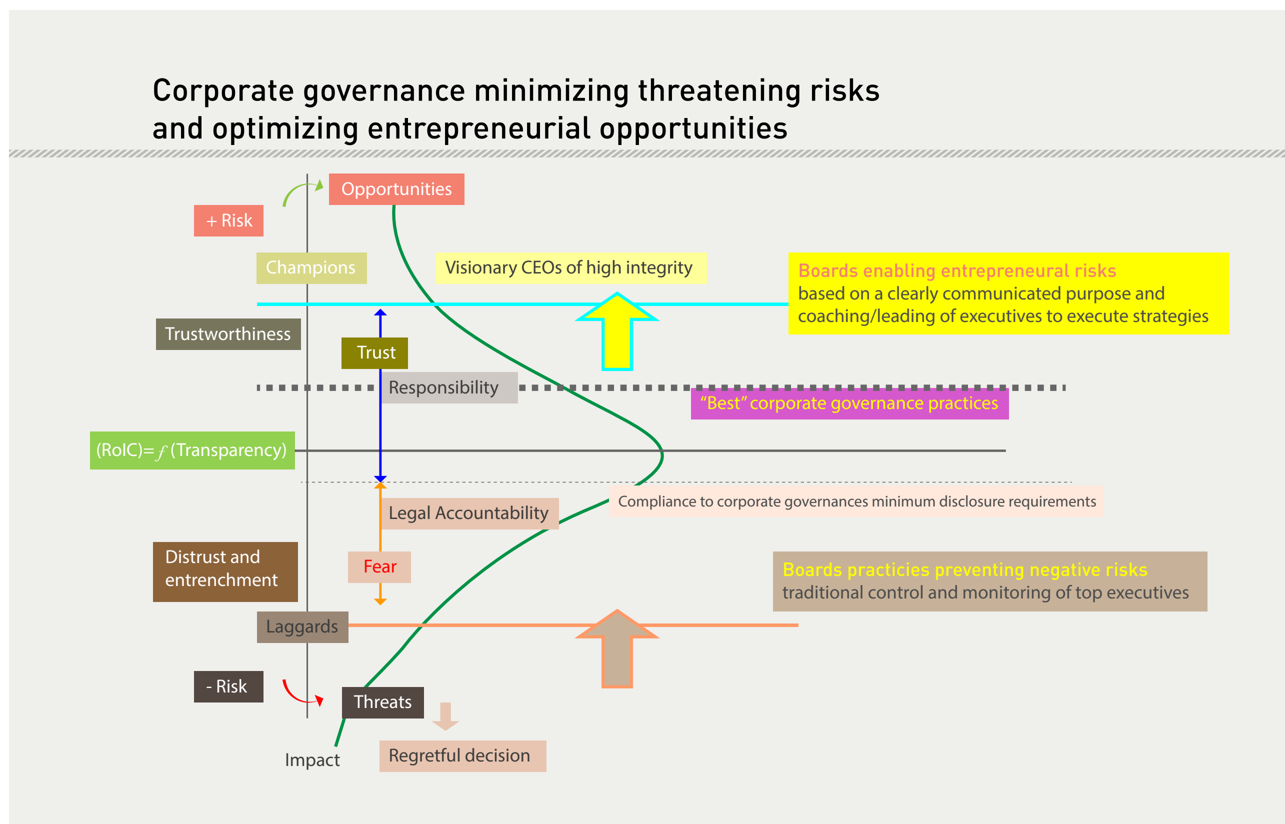
The supervisory board and the owners of SOEs (ie, the minister in charge) should stay out of the operations and nonstrategic decisions, which is the BoD's responsibility. And obviously, the minister and the supervisory board should steer clear of mingling in fields for which they have

given delegated authority to the BoD. Only in times of crisis, we suggest, should the chairman step in and take a more leading role in steering the organization out of risky waters toward open opportunities, as visualized in figure 1 below.

Entrepreneurial and innovative

More specifically, we put forward that there is a relationship between governance and its generic principles (especially transparency, accountability, responsibility and fairness) on the one hand, and entrepreneurial innovation or managerial entrepreneurship on the other hand. We believe that some simple rules can institutionalize that causal relationship and significantly improve the performance of the firm in the process.

Big companies such as Pertamina face the danger of being so big that innovative entrepreneurship or managerial entrepreneurship becomes impossible, and governance is reduced to mere compliance with some rules and regulations. Boards can do much more and can help to induce innovation – the necessary oxygen for any company – by setting an example on how to avoid groupthink or the status quo and how to improve decision-making. Let us try to visualize this as a risk – where boards ultimately try to avoid organizational value destruction on the threatening side, and to optimize entrepreneurial opportunities on the upside of the Gauss curve. Just sticking to the status quo and the average will no longer be a solution. The nation-state, the



employees and the board have a duty to optimize the opportunities of SOEs and use their vast resources more professionally and optimally in a transparent manner, underpinned by proper levels of integrity. At the same time, the nonexecutive and executive board of any SOE should minimize threatening risks and avoid making regrettable decisions that would continue to undermine the competitiveness of their organization. Organizations deserve better. The nation's vast resources are at stake and should not be spoiled for politically misguided short-term objectives.

By becoming more open to a changed context and to accommodate such changes, big companies may avoid becoming ineffective. Although boards may have the ultimate legal power in any organization, boards do not necessarily have a monopoly on truth and will need to induce managerial entrepreneurship throughout the organization, learning from a number of international cases such as Polaroid (the now-defunct inventor of instant pictures), IBM or Bridgewater. In our approach, we see a causal correlation between accountability and openness, between well-governing boards and improved innovative entrepreneurship within the company. How do we explain why Malaysia's Petronas, roughly with the same revenue stream of more than $50 billion as Pertamina, was (and still is) many times more profitable and thus more financially effective than its Indonesian counterpart?

So, one of the first exercises we would suggest to undertake with a new dual-board is going through the following counterintuitive question: how to kill the old Pertamina culture, encumbered by vested political and personal interests and entrenchment, to help the board engage in increased accountability, while at the same time avoiding group-think and becoming better "managerial entrepreneurs" for the company. A daunting and almost impossible task for many, as all consultants and academics are well aware, is that organizational culture is the software of an organization that "eats every other challenge for breakfast."

Is Basuki Tjahaja Purnama, the former Jakarta governor and recently appointed chief commissioner of Pertamina, the man who would dare to ruffle feathers in the establishment and reduce the entrenchment challenges that have characterized Pertamina for so many years? Possibly, if the political spirit remains in the bottle. Maybe running Pertamina like a publicly listed company according to best corporate governance practices and procedures is a good start? And yes, we are mindful that Pertamina may not choose to go through an IPO process. We nonetheless believe that applying good corporate governance practices and running the firm accordingly would hugely benefit all stakeholders in the longer term.

At the end of the day, a good functioning board is about good leadership, about securing that organization's sustainability over a long period, by preparing and executing appropriate strategies; by

securing that no excessive risks are taken; that executives remain within risk boundaries as agreed by the board; that enough liberty is given to executives to take reasonable risks to create value; and that all board members and executives can be held accountable for their performances according to the objectives in a transparent and fair manner. State-owned enterprises would enormously benefit from "depolitization," de-bureaucratization and a professionalization of their boards and managers with clear fiduciary duties to the organization and not to its changing political and often entrenched patrons, while also guaranteeing a succession of managerial talent for the future. Only then, we believe, will state-owned companies have a chance to survive and thrive in the long term.

And that is the duty of any government official who has opted for public service for the common public good, not self-interest or political patronage. This applies as well to board members serving on state-owned enterprises who are paid to create organizational value, not to destroy it or pay "patronage" to those who put them in that position. Only people with high integrity, supported by strong and professional structures and governance rules, may have a chance to take on the daunting challenge to secure competitiveness and productivity in these organizations, while simultaneously serving the bigger common goals of state-owned enterprises.