

Corporate Governance: Transparency between government and business.

By

**John D. Sullivan
Center for International Private Enterprise
US Chamber of Commerce**

Corporate Governance: Transparency between government and business.

By

**John D. Sullivan
Center for International Private Enterprise
US Chamber of Commerce**

Presented to the

**Mediterranean Development Forum 3
World Bank Meeting**

Cairo, Egypt

Tuesday, March 7, 2000

The Center for International Private Enterprise's mission is to build democracy around the world through the promotion of private enterprise and market-oriented economic reform. Established as an affiliate of the US Chamber of Commerce in 1983, CIPE is principally supported by the National Endowment for Democracy, with additional support from private foundations and the US Agency for International Development. In its 16 years of operation, CIPE has completed over 500 projects in more than 70 countries working with policymakers, business leaders, and journalists to build the civic institutions vital to democratic society. Together with USIA, CIPE publishes *Economic Reform Today*, a quarterly magazine for policymakers, business leaders, and journalists that is distributed in some 90 countries with regular issues in English and Spanish with annual readers in Arabic, Chinese, French, and Russian. *Economic Reform Today* and other electronic resources can also be found on CIPE's Web Page: <http://www.cipe.org>

Introduction

Few topics are more central to the international business and development agendas than that of corporate governance. A series of events over the last two decades have placed corporate governance issues as a top concern for both the international business community and the international financial institutions. Spectacular business failures such as the infamous BCCI scandal, the United States' savings and loan crisis, and the gap between executive compensation and corporate performance drove the demand for change in developed countries. More recently, several high profile scandals in Russia and the recent Asian crisis have brought corporate governance issues to the fore in the developing countries and transitional economies. Further, national business communities are learning and re-learning the lesson that there is no substitute for getting the basic business and management systems in place in order to be competitive internationally and to attract investment.

As a result, the World Bank, the Organization of Economic Cooperation and Development, most of the regional development banks, and the various national development agencies have either launched or expanded programs in this area in the last several years. Similarly, business-related organizations like the Center for International Private Enterprise, an affiliate of the US Chamber of Commerce, have placed corporate governance at the top of their list of concerns. Think tanks and business associations throughout the developing world and in the transitional economies are also focusing resources on these issues.

In developing countries, the roots of what is now recognized as corporate governance type issues can be found in the drive for privatization that grew in the late 1970s and throughout the 1980s. Clearly, creating a sound corporate structure should have been central to the success of privatization both from the point of view of the government seeking to sell the firm and from the point of view of the potential investors. In fact, some of the most telling failures in the early privatization experiences can be traced back to a lack of sound regulatory structures that allowed unwise business practices. Chile comes to mind in this respect. In the mid-1970s, Chilean business groups were able to purchase banks, often with only 20 percent initial payments. In 1982, Chile experienced an economic crisis generated by a combination of external shocks and an overvalued exchange rate. The business groups responded by using their banks to shore up the firms which led both into even more serious trouble. Finally, the government responded by re-nationalizing a host of firms and banks.¹

The fall of the Berlin wall and the drive to rapidly privatize the entire business structure of the post-communist economies began to increase interest in corporate governance as a development topic. As a start, state owned firms had to be corporatized, i.e. converted from a governmental type structure to a corporate form. Second, the whole body of commercial law had to be put into place including bankruptcy, laws on property, accounting systems, and a host of

¹ Ahmed Galal and Mary Shirley, *Bureaucrats in Business*, Published for the World Bank by Oxford University Press: Oxford, 1995, p. 93

other rules of the game. Most dauntingly, talent had to be nurtured. Few individuals had any experience as members of a board of directors.

It is perhaps not surprising that the countries that rushed into large-scale privatization, especially the Czech Republic and Russia, have experienced large scale corporate governance failures including asset stripping and fraud. Hungary, which chose to sell its firms to international strategic investors, and Poland, which chose to delay privatization of large companies, have had better results. Today, however, all of the post-communist countries are having to come to grips with the need to substantially improve corporate governance standards and practices.²

The Asian financial crisis has now driven the process worldwide much further. One of the lessons learned out of the crisis is that weak or ineffective corporate governance procedures can create huge potential liabilities for both individual firms and, collectively, for society. In this sense, corporate governance failures can potentially be as devastating as any other large economic shock. As M.R. Chatu Mongkol Sonakul, the Governor of the Bank of Thailand has observed:

There is no doubt in my mind that for the Asian economic crisis to be solved in a sustainable and long-lasting fashion, the government and the corporate sector have to work together better. By this, I don't mean that not working together was the cause of the recent economic crisis. Probably it was the other way around, working far too well together and in collusion with each other. ... The Asian financial crisis showed that even strong economies lacking transparent control, responsible corporate boards, and shareholder rights can collapse quite quickly as investor's confidence erodes³.

As can be seen from Dr. Sonakul's observations, corporate governance is at the very heart of the development of both a market economy and a democratic society. That view may be a bit of a surprise to those who think mainly of corporate governance as the issues of shareholder protection, management control, and the famous principal-agent problems of such concern to management and economic theorists. The focus of this paper is the concept of corporate governance as a key feature of the market system of competitive enterprise. In addition, the paper shows why corporate governance should also be of direct concern to those focusing on democratic development especially rule of law issues. Corporate governance ultimately depends upon public-private sector cooperation to achieve both goals--the creation of a competitive market system and the development of law-based democratic society.

These concerns are not limited to developing countries, even in the advanced industrial societies, there is a global trend toward strengthening corporate governance. For example, in

² A number of programs can be reviewed at www.cipe.org under the corporate governance tab. The World Bank's corporate governance program contains a number of links as well – www.worldbank.org.

³ M.R. Chatu Mongkol Sonakul, Governor, Bank of Thailand, "Corporate Governance and Globalization," opening address at the "Asian Economic Crisis and Corporate Governance Reform" conference held on September 12-14, 1999, Bangkok, Thailand. Full text at www.cipe.org.

recent years, the Cadbury Commission in the United Kingdom, the Vienot Commission in France, and the Organization of Economic Cooperation and Development (OECD) have all issued new guidelines. In the United States, there is mounting concern over the “independence” of independent audits as witnessed in the recent publicity surrounding violations of rules prohibiting auditors to invest in companies that they audit. In all of these cases, the underlying concerns center around ways to accomplish the core values of corporate governance including transparency, accountability, and building value.

Definitions

Corporate governance is typically perceived by academic literature as dealing with “problems that result from the separation of ownership and control.”⁴ From this perspective, corporate governance would focus on: the internal structure and rules of the board of directors; the creation of independent audit committees; rules for disclosure of information to shareholders and creditors; and, control of management. A recent academic survey began with the following quote:

“Corporate governance deals with the ways in which suppliers of finance to corporations assure themselves of getting a return on their investment. 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? How do suppliers of finance control managers?”⁵

From this point of view, corporate governance tends to focus on a simple model:

1. Shareholders elect directors who represent them.
2. Directors vote on key matters and adopt the majority decision.
3. Decisions are made in a transparent manner so that shareholders and others can hold directors accountable.
4. The company adopts accounting standards to generate the information necessary for directors, investors and other stakeholders to make decisions.
5. The company’s policies and practices adhere to applicable national, state and local laws.⁶

Focusing on these types of internal control processes is quite natural when the subject is corporate governance within the advanced market economies. Point number five assumes that a functioning legal system is in place. Although there are considerable differences between the Anglo-American, German, Japanese, and other systems, they all share the luxury of defining the

⁴ OECD Principles of Corporate Governance, issued by the Organization for Economic Cooperation and Development, see www.oecd.gov.

⁵ Andrei Shleifer and Robert Vishny, “A Survey of Corporate Governance,” *The Journal of Finance*, Vol. LII, No.2, June 1997, p. 737.

⁶ This list is drawn from a course for new directors developed by the Central European University and CIPE. See CIPE’s Web page for more information at www.cipe.org.

subject of corporate governance within the context of functioning market systems and highly developed legal institutions.

When the subject of corporate governance arises in the context of transitional or developing countries, it involves a much wider range of issues. The recent Asian economic crisis, the continuing turmoil in Russia, and the recent experience of the Czech economy have combined to push the issue of corporate governance from the sidelines to center stage. In Asia, what began as a financial crisis is now viewed to be a crisis of corporate transparency involving relationships between government and business, between holders of debt and equity, and the legal remedies for bankruptcy and cronyism. Further, as seen in the daily papers, the lack of adequate institutions in Russia have resulted in several highly publicized cases involving allegations of asset stripping, stock register manipulation, and fraud⁷. The Czech Republic privatization program has demonstrated the weakness of the voucher method in the absence of sound corporate governance mechanisms since it resulted in a lack of corporate restructuring and a consequent decline in competitiveness.⁸

What these examples have in common is that they all involve the basic rules of the economy and the relationship between these rules and the way companies are governed. The issues involved include some very familiar topics. In the interest of space, here are just a few core issues:

- Transparency -- or full disclosure of financial and key performance information
- Conflicts of interest involving boards of directors and managers
- Procedures for bankruptcy
- Property rights
- Contract enforcement
- Corruption and theft

Each of these issues poses grave challenges for both the functioning of a market economy and a democratic society. Solving corporate governance problems such as those listed above involves going beyond a narrow view of how owners and managers of capital interrelate. In developing or transitional economies, the standard definition should be supplemented by placing it in context as follows:

Corporate governance systems depend upon a set of institutions (laws, regulations, contracts, and norms) that create self-governing firms as the central element of a competitive market economy. These institutions ensure that the internal corporate government procedures adopted by the firms are enforced and that management is responsible to owners (shareholders) and other stakeholders.

⁷ For example see Andrew Jack, "Oil giant bogged down in Siberian intrigue: BP Amoco's stake in Sidanco has become a litmus test for foreign investment in Russia," *Financial Times*, October 20, 1999.

⁸ Joseph E. Stiglitz, "Quis Cutoiet Ipsos Custodes? (Who is to guard the guards themselves?), ABCDE Conference-Europe, pp. 11-12. Available on the World Bank web page.

The key point in this definition is that the public and private sectors have to work together to develop a set of rules that are binding on all and which establish the ways in which companies have to govern themselves.

Creating New Norms

Transitional economies have to make fundamental changes in the relationship between citizens and the state in order to create market economies. One interesting illustration of the fundamental nature of this reorientation can be found in the first law on private enterprise passed in Poland in 1988. The Law on Economic Activity stated that:

“Within the scope of their economic activity, economic subjects may perform operations and actions which are not forbidden by law.”

Most entrepreneurs in market economies would find that wording decidedly odd. The clear understanding in a market-oriented society (i.e. non-statist) is that all actions not forbidden by law are allowed. That expectation is at the heart of private, individual initiative. The converse rule has been applied in command economies and in economies with a statist tradition. That is, only those actions specifically authorized by law, regulation, or written permission are allowed.

Building a market economy requires a complete overhaul of legal norms to allow for innovation and initiative rather than predefining areas of allowable activity. That is why corporate governance should be thought of as a mechanism for creating self-governing organizations. However, it is equally important to emphasize that a market economy is not simply the absence of governmental intervention.

How often has it been said that, “the government should get out of the way and let the market function?” Of course, that idea is a myth. Government is absolutely essential in setting up the framework of a market economy. Without rules and structures of a binding nature, anarchy results. Under such conditions business becomes nothing but "casino capitalism" where investments are simply bets: bets that people will keep their word, bets that the firms are telling the truth, bets that employees will be paid, and bets that debts will be honored. What corporate governance is all about in larger terms is how a structure can be set up that allows for a considerable amount of freedom within the rule of law. Ultimately, these arrangements provide the basis for the establishment of trust, one of the most important ingredients in business.

OECD Principles

A useful first step in creating or reforming the corporate governance system is to look at the principles laid out by the OECD and adopted by the governments which are members of the OCED itself. These principles can be found on their Web site: www.oecd.gov. In summary, they include the following elements.

I. The Rights of Shareholders

These include a set of rights including secure ownership of their shares, the right to full disclosure of information, voting rights, participation in decisions on sale or modification of corporate assets including mergers and new share issues. The guidelines go on to specify a host of other issues connected to the basic concern of protecting the value of the corporation.

II. The Equitable Treatment of Shareholders

Here the OECD is concerned with protecting minority shareholders rights by setting up systems that keep insiders, including managers and directors, from taking advantage of their roles. Insider trading, for example, is explicitly prohibited and directors should disclose any material interests regarding transactions.

III. The Role of Stakeholders in Corporate Governance

The OECD recognizes that there are other stakeholders in companies in addition to shareholders. Banks, bond holders and workers for example are important stakeholders in the way in which companies perform and make decisions. The OECD guidelines lay out several general provisions for protecting stakeholder interests.

IV. Disclosure and Transparency

The OECD also lays out a number of provisions for the disclosure and communication of key facts about the company ranging from financial details to governance structures including the board of directors and their remuneration. The guidelines also specify that annual audits should be performed by independent auditors in accordance with high quality standards.

V. The Responsibilities of the Board

The guidelines provide a great deal of detail about the functions of the board in protecting the company, its shareholders, and its stakeholders. These include concerns about corporate strategy, risk, executive compensation and performance, as well as accounting and reporting systems.

The OECD guidelines are somewhat general and both the Anglo-American system and the Continental European (or German) systems would be quite consistent with them. However, there is growing pressure to put more enforcement mechanisms into those guidelines. The challenge will be to do this in a way consistent with market-oriented procedures by creating self-enforcing procedures that do not impose large new costs on firms. The following are some ways to introduce more explicit standards:

- Countries should be required to establish independent share registries. All too often, newly privatized or partially privatized firms dilute stock or simply fail to register shares purchased through foreign direct investments.
- Standards for transparency and reporting of the sales of underlying assets need to be spelled out along with enforcement mechanisms and procedures by which investors can seek to recover damages.
- The discussion of stakeholder participation in the OECD guidelines needs to be balanced by discussion of conflict of interest and insider trading issues. Standards or guidelines are needed in both areas.
- Internationally accepted accounting standards should be explicitly required and national standards should be brought into alignment with international standards.
- Internal company audit functions and the inclusion of outside directors on audit committees needs to be made explicit. The best practice would be to require that only outside, independent directors be allowed to serve on audit committees.

A good example of model corporate governance procedures that builds on many of these points is the General Motors guidelines which are frequently used as a code of corporate governance by others.⁹ Interestingly, the pension funds have also become a major source of improved corporate governance along the same lines. Specifically, the California Public Employees' Retirement System (CalPers) has developed a very active program to promote good corporate governance and they, along with other pension funds, are using their investment clout to force change. CalPers' has taken this approach in order to increase the returns on their investments by ensuring that the firms are well run and that corporate strategies are well thought out. As more and more pension fund investments flow into developing countries, these funds can be expected to make similar demands in these countries.¹⁰

Some may think that these standards are too heavily influenced by the Anglo-American tradition and are not really necessary in most countries. A recent study by the Center for European Policy Studies noted that the wider the distribution of shareholding, the greater is the role of the market in the exercise of corporate control. Hence there is more need for corporate governance procedures in this type of economy than in one where shareholding is relatively concentrated. The report went on to note, however, that financial market liberalization, increased privatization, and the growing use of funded systems to support pensions is driving European countries toward more explicit and more comprehensive rules on corporate

⁹ These guidelines can be found in the corporate governance section of CIPE's Web site: www.cipe.org.

¹⁰ CalPers also has an excellent web site which hosts their recommendations for improvements in corporate governance. www.calpers-governance.org

governance.¹¹ In short, globalization is forcing convergence of different systems into a more open and internationally accepted set of standards.

The reason why it is important to take note of the trends toward convergence is that many people have cited the European experience as proof that corporate governance issues only apply to countries that follow an Anglo-American tradition, such as India for instance. Recent history would seem to show that, without sound corporate governance procedures, including the larger institutional features mentioned earlier, economic crises in developing countries are likely to become more frequent. Many developing countries face rather stark choices: either create the type of governance procedures needed to participate in and take advantage of globalization, run the risk of severe (and frequent) economic crises, or seek to build defensive walls around the economy. It should be noted that the last option usually entails the risk of keeping out investors, new technologies, and lowers growth rates dramatically.

Another consideration in the debate over corporate governance systems is the risk that individual firms face. Unless a company is able to build the kinds of governance mechanisms that attract capital and technology they run the risk of simply becoming suppliers and vendors to the global multinationals.

A recent Asian conference on corporate governance holds a number of lessons for countries in the Middle East. During this conference, the participants debated quite extensively the need for outside directors and independent audit committees in particular. Several of those present -- including representatives from Indonesia and South Korea -- noted that there was some reluctance to adopt rules requiring audit committees to be made up of outside directors and requirements that audits should be public. In the end, however, there was general agreement that such reforms are essential to prevent a repeat of the Asian crisis. The full list of recommendations from the Bangkok conference is attached as annex 1.

Benefits to Society

A strong system of corporate governance can be a major benefit to society. Even in countries where most firms are not actively traded on stock markets, adopting standards for transparency in dealing with investors and creditors is a major benefit to all in that it helps to prevent systemic banking crises. Taking the next step and adopting bankruptcy procedures also helps to ensure that there are methods for dealing with business failures that are fair to all stakeholders, including workers as well as owners and creditors. Without adequate bankruptcy procedures, especially enforcement systems, there is little to prevent insiders from stripping the remaining value out of an insolvent firm to their own benefit.

Recent research has also shown that countries with stronger corporate governance protections for minority shareholders also have much larger and more liquid capital markets.

¹¹ "Corporate Governance in Europe: Report of a CEPS Working Party," Center for European Policy Studies, Chairman, Dr. Ulrich Bosh (Senior Vice President, Deutsch Bank), Rapporteur, Karel Lannoo (CEPS), June 1995 available at www.ceps.be. See also, the European Corporate Governance Network - www.ecgn.ulb.ac.be

Comparisons of countries that base their laws on different legal traditions show that those with weak systems tend to result in most companies being controlled by dominant investors rather than a widely dispersed ownership structure. Hence, for countries that are trying to attract small investors--whether domestic or foreign--corporate governance matters a great deal in getting the hard currency out of potential investors' mattresses and floorboards.¹²

Many economists and management experts make the point that competition in product markets and competition for capital act as constraints on corporate behavior, in effect forcing good corporate governance. The fact that pension funds such as CalPers have had to take a very active role in improving corporate governance would seem to contradict this point. However, whether or not this is really the case in developed market economies, competition is surely a much smaller factor in transitional and developing countries. In many developing countries, competition in product or goods markets is quite limited, especially where significant regulatory barriers exist. These realities further underscore the importance of adopting the best possible corporate governance systems in countries where the market system is underdeveloped.¹³

Corporate governance is also directly related to another topic that has emerged to a position of great prominence world wide – combating corruption. In many societies this is not a subject that is easy to deal with, both because of political sensitivities as well as potential legal action. Yet corruption has to be dealt with in order to secure a position in the global economy and to secure the benefits of economic growth. The recent signing of the OECD anti-bribery convention is the beginning, not the end, of a concerted global anti-corruption campaign. Efforts to improve corporate governance, especially in the provision of transparency in corporate transactions, in accounting and auditing procedures, in purchasing, and in all of the myriad individual business transactions is a large scale effort. Nevertheless, strengthening the corporate governance standards along lines suggested above would be one place to start.

Improving corporate governance procedures can also improve the management of the firm, especially in areas such as setting company strategy, ensuring that mergers and acquisitions are undertaken for sound business reasons, and that compensation systems reflect performance. It is also important to note that good corporate governance systems also have to include improvements in management systems. In many developing countries, there has been a tradition of very centralized management usually involving the owners of the firms directly. Throughout Latin America, for example, the family business groups have tended to dominate the business landscape. This is now changing rapidly as a result of financial globalization, adherence to the World Trade Organization's liberalization rules, and the increasing integration of Latin

¹²Rafael La Porta, Florencio Lopez De Silanes, Andrei Shleifer, and Robert Vishny, "Legal Determinants of External Finance," in *The Journal Of Finance* 52, July 1997, pp. 1131-50.

¹³ For a review of the available literature with special reference to Russia, see Erik Berglof and Ernst-Ludwig von Thadden, *The Changing Corporate Governance Paradigm: Implications for Transition and Developing Countries*, presented at the World Bank's ABCDE conference and available on the World Bank's Web site – www.worldbank.org

America's regional markets.¹⁴ As a result, Latin America's firms are increasingly adopting modern management techniques, financial accounting systems, and business strategies. All of this requires delegation of authority, paying increased attention to developing highly trained staff, and use of management information systems in lieu of the older centralized decision making structures. It is highly probable that these trends will force similar changes throughout the Middle East.

Conclusion

One way to sum up the concept of corporate governance is to look at it from the perspective of the corporate director. Increasingly directors are being held liable for their actions or inaction, at least in the developed countries. What then does a director need to be able to function and have a balanced view of the firm? According to one seasoned corporate director, the following is the minimum essential information:

- Operating systems, balance sheets, and cash flow statements that compare current period and year-to-date performance to target performance and previous year performance.
- Management comments about current performance that focus on explaining the deviations from the target performance and revise performance targets for the remainder of the year.
- Information on the company's market share.
- Minutes of management committee meetings.
- Financial analysts' reports for the company and its major competitors.
- Employee attitude surveys.
- Customer preference surveys.
- Key media articles on the company, its major competitors, and industry trends.¹⁵

The list not only sums up the key responsibilities of a board by showing the kinds of information that a board should review and disclose. These concerns reinforce the argument that corporate governance reflects the underlying systems of law and regulation. Most importantly, without sound and accurate accounting systems, how could the director function? The list also

¹⁴ For a very concise summary of these trends in Latin America and the response of Latin America's leading firms, see the interview with Cesar Souza "Latin America's Rapidly Changing Corporations," in *Economic Reform Today*, Number one, 1999, available at www.CIPE.org. Souza is Senior Vice President of Odebrecht of America, a heavy construction firm operating in 14 countries.

¹⁵ Walter Salmon, "Crisis Prevention: How to Gear Up Your Board," *Harvard Business Review*, 7(1), 1993. Quoted in Marek Hessel (ed.), *In Search of Good Directors: Corporate Boards in Market and Transition Economies*, 1998 (second edition), Washington DC: CIPE., p. 97.

points up that good corporate governance will bring with it modern management systems. For example, reviewing the minutes of the management committee meetings implies that a functioning management committee system is in place with delegation of authority and accountability.

Investors, creditors, workers, and others also need such information. Unlike the corporate director, they do not have the time or resources to compile and analyze the information needed to make sound decisions. This is where the media, especially the financial media, comes into the picture. A vigorous and well informed journalist community is essential for the small investor and for the other stakeholders in society, including employees.

Creating sound system of corporate governance is a high priority for both the public and the private sectors. However, there may be a temptation for the private sector to just say, "well, we'll let the government work this out and then we'll follow the results." In some cases, there may also be a temptation--especially for the countries with protected markets and a large state sector --to put off corporate governance reform until after the privatization process and other types of reforms are fully completed. Experience would indicate that this would be a very unfortunate decision. Both the private and public sectors have much to gain by setting up clear and simple rules for all to follow. A sound corporate governance structure will be a great inducement to international trade and investment. In addition, sound corporate governance systems are a major advantage to those countries seeking to fight corruption. In this sense, good corporate governance is a way for the private sector to protect itself from outside demands and for the public sector to prevent undue influence in governmental decision making.

However, it is vital to avoid simply copying other countries systems or asking foreign experts to write model laws. Although the foreign donor community often pushes this type of approach, it should be resisted. Throughout Central and Eastern Europe a network of extremely capable policy research institutes, think tanks, have been formed and others will surely follow. Many of these centers have been formed with the backing of the business leadership and are in a position to devise, adapt, and advocate for systems that will be appropriate to the status of each country. In the process, not only will the resulting policy reforms advance better systems of corporate governance, they will point to the need for other reforms. The need for adoption of modern management systems including areas such as knowledge management and strategic planning will become more apparent in the process. As more and more countries in the region enter the WTO process and further their participation in the global market, the demand for corporate governance will surely grow. Its up to the policy research centers, the national business associations, and others in civil society to work with governments to craft the best national systems.

Annex 1

Business Leaders Call for Incorporating Corporate Governance into ISO Standards

Bangkok, Thailand - An unprecedented gathering of senior business executives from six Asian countries convened on September 12-14, 1999. Some 40 corporate, business association and private think tank executives from India, Indonesia, South Korea, Malaysia, Philippines, Singapore and Thailand participated in the conference and offered their ideas on how businesspeople can encourage positive changes in the way in which corporations are structured and managed. They agreed that business can and must play a leading role in promoting more transparent interchanges between the public and private sectors and recommending possible structural and democratic reforms to help prevent a recurrence of the Asian economic crisis and restore international investor confidence in the region.

Corporate governance is the body of “rules of the game” by which companies are managed internally and supervised by boards of directors, in order to protect the interests and financial stake of shareholders who may be located thousands of miles away and far removed from the management of the firm. Just as good government requires transparency so that the people can effectively judge whether their interests are being served, corporations must also act in a democratic and transparent manner so that their owners can make educated decisions about their investments.

The Asian executives in Bangkok said they would contact the International Standards Organization in Geneva and propose the incorporation of standards for corporate governance into the ISO system. They said Asian business organizations would be willing to work with the ISO in developing corporate governance standards that would promote adoption of best management practices in corporations worldwide.

The business leaders also called for regional and country-specific awards that recognize companies that adhere to sound corporate governance practices. They said the new awards would help promote public understanding of the importance of corporate governance not only to firms, but to consumers, employees and other public stakeholders.

The Bangkok meeting was sponsored by The Thai Federation of Industries, The Thai Chamber of Commerce, Institute for Management Education for Thailand Foundation (IMET) and the Center for International Private Enterprise (CIPE) of the United States. The recommendations drew on the Confederation of Indian Industries’ guidelines.

###

Recommendations for Action

The business participants explored corporate governance reforms by examining the impact on four sets of constituencies: general public, media, business community and government and policy makers. The executives developed the following list of specific initiatives that businesses and business organizations can undertake with each constituency:

General Public

- Educate general public that good corporate governance is beneficial for all to help elevate the status of corporate governance in the national business agenda.
- Initiate education and training programs with target groups (chambers of commerce, federations of industry and other business associations) that promote good corporate governance.
- Encourage companies to promote positive interaction between suppliers and consumers, formulate transparent guidelines for transactions, offer recourse for consumer complaints and establish mechanisms to receive complaints and feedback.
- Establish third-party monitoring and evaluation systems on corporate governance, and foster collaboration among firms, business associations and consumer groups.
- Promote good corporate citizenship and social responsibility among firms and standards of fairness in interaction with the public.
- Organize periodic reviews and information exchanges with businesspeople both nationally and internationally to ensure continued relevance of standards and possible adoption of new ideas.
- Establish new awards by November 2000 in ASEAN Chambers of Commerce and Industry to be conferred on firms in the region that practice sound principles of corporate governance.
- Create regional database on good corporate governance including information on corporate success stories and disseminate to the public.

Business Community

- Increase percentage of independent directors on corporate boards initially to one-third and eventually to 50 percent.
- Disclose information on directors including remuneration, family relationships and business relationships that may constitute conflict of interest.

- Propose legislation to hold directors legally responsible for failure to discharge fiduciary responsibility, taking into account differences in liabilities between executive and non-executive directors consistent with national legislation.
- Place responsibility for company management in the hands of professional and experienced executives, establish clear management policies and make these known to employees and shareholders.
- Establish audit committee consisting of at least three independent directors that reports directly to the Board. Internal auditors also should report directly to the Board.
- Publish annual reports containing extensive information on firm's financial condition, ownership structure and corporate governance standards.
- Encourage business associations to serve as training and information resources on corporate governance practices for small and medium-sized firms.

Media

- Organize press events immediately after the conference in other participating countries led by participants to publicize conference findings
- Promote development of a strong financial press by disclosing information, and preparing short objective articles and editorials defining the concept of good corporate governance for publication in the business media.
- Encourage the media to publicize corporate governance reforms by providing success stories from regional and national business associations and others in the business network to identify companies that practice good corporate governance.
- Incorporate the principles of good governance into the agenda of the media seminars or workshops held regularly by institutes and associations.

Legislative and Government

- Incorporate corporate governance into the International Standards Organization system.
- Adopt a grading system utilizing corporate governance principles to help business evaluate the efficiency of government agencies.
- Encourage the evaluation and review of current laws, rules and regulations to improve the quality of existing legislation and simplify administration.

- Encourage governments to sign-on to the anti-corruption convention of the Organization of Economic Cooperation and Development (OECD).
- Recommend that governments adopt simplified, clearly defined, transparent, and time-limited systems for any government process.
- Recommend adoption by the accountancy profession of international Generally Accepted Accounting Principles (GAAP).
- Propose that governments adopt full disclosure of information on economic conditions as recommended by IMF.
- Develop corporate governance workshops for government officials.

CENTER FOR INTERNATIONAL PRIVATE ENTERPRISE

WWW.CIPE.ORG

Corporate Governance Programs

1992 – 2000 summaries

Central European University (CEU), Czech Republic/Regional - CIPE's corporate governance program began in 1992 through a training program undertaken by the Central European University with support from the Soros Foundation and the National Endowment for Democracy. The program was developed to establish a core group of senior Central European corporate directors schooled in the basics of corporate governance, and to develop a new generation of corporate directors who would have an understanding of the responsibilities of corporate governance, thus strengthening emerging corporate institutions in Central Europe. Developed in three phases over four years, the project served to develop a curriculum and materials for a course on the basics of corporate governance. After testing the impact of the program in the Czech Republic during the first phase, the subsequent two phases concentrated on replicating the program through the training of instructors and the translation of materials for licensed courses to be taught in Hungary, Poland, Ukraine, and Russia.

CIPE/In-house, Romania - In cooperation with the Romanian American Enterprise Fund, CIPE sponsored a one and a half-day seminar and training program in Romania. The seminars explored the concepts surrounding corporate governance in the Romanian environment, and began building a public/private consensus on the need for a strategy to strengthen corporate governance policy and education in Romania. The goal of the program was to establish a common frame of reference from which policy and business leaders could begin developing a corporate governance strategy for Romania.

Center for Economic and Social Studies (CESS), Albania - Acknowledging the critical nature of effective corporate governance in ensuring successful privatization in Albania, the Center for Economic and Social Studies (CESS) is undertaking a comprehensive research and advocacy program on corporate governance and privatization. The future success of privatization will depend on the introduction of core system of corporate governance principles and practices that will ensure these vital enterprises are managed in an open and responsible manner. The effective exercise of ownership rights in restructuring and managing these firms will be crucial not only to their continued success, but also to contributing to the creation of a new climate of business in Albania. Investors must have confidence that enterprises will be managed effectively, and that government can provide the framework in which ownership rights can be exercised and guaranteed. The CESS project will survey current practices and highlight failures and shortcomings in Albanian corporate governance structures, CESS will conduct a national advocacy program of seminars, publications and media outreach to promote new policies and practices which could help ensure more successful privatization and a smoother transition process.

Center for Economic Development (CED), Bulgaria - The Center for Economic Development in Sofia, Bulgaria conducted a pilot program on corporate governance issues targeted at specific interest groups to provide a general introduction to corporate governance values and principles, broaden the debate on the Bulgarian approach to these issues, and further develop a strategy for corporate governance education. Ignorance of corporate governance principles

must be fought at a variety of levels, within SOEs, among capital market institutions, policy makers, and the general public, as well as in the media. However, for those leading the fight for better principles the need exists to define issues, and the scope and extent of the problems to be addressed. CED organized and administered four one-day training seminars to address a variety of issues surrounding corporate governance. The seminars addressed specific groups and discussed their role in creating a society supportive of corporate governance concepts. The seminars served as two-way dialogues, providing information on corporate governance issues to participants, and promoting a two-way dialogue between CED researchers and affected groups as to the challenges they face in implementing corporate governance procedures, and ways in which CED can further support this transition.

Center for Economic Development (CED), Slovakia – CED is developing a research and advocacy program on corporate governance in the Slovak Republic. The main objective of the project is to help the Slovak economic system tailor the optimal corporate governance framework for the Slovak economy and tackling the informational institutional environment. The project will attempt to define the inside corporation's problems and design more flexible framework, which will allow for faster corporate reforms. They will implement an intensive education campaign of policy decisions makers, media, general public and managers about the necessary information needed for improving the governance system. Lastly, the project will seek to identify the main barriers to changing the corporate governance system in Slovakia towards an optimal one. Through seminars, bulletins, surveys, economic sheets and a corporate governance pamphlet, CED hopes to put corporate governance reform in the forefront of its national business agenda.

Center for Study of Democracy (CSD), Bulgaria - As privatization moves forward in Bulgaria, the issues surrounding corporate governance become clearer and more urgent. Currently there is little information available to Bulgarian privatization officials and enterprise managers in this crucial element of structural reform. CSD has undertaken a corporate governance education program aimed at the key players in privatization, as well as educating interested members of the general public. The program consists of study visits to transition economies, workshops for key private sector representatives, town hall for the general public, and public education campaigns through articles and radio and TV presentations. CSD has created a coalition comprising the Association of Industrial Capital, Association of Voluntary Pension Funds, Center for Economic Development, Investors' Union, and Securities Holders Association. The objective is to facilitate the adoption of relevant corporate governance standards and procedures that would ensure accountability, transparency and control in the economy.

International Center for Entrepreneurial Studies (ICES), Romania – ICES will work with the Strategic Alliance of Business Associations (SABA) to promote investor confidence, bettering the business environment and reducing corruption. SABA and ICES will establish a working group on corporate governance to coordinate the research and policy development efforts. Project results will then be disseminated to the broader business community, media and parliament via a series of workshops, policy roundtables and media outreach. The workshops and roundtables are designed to develop a draft code on corporate governance with which a National Task Force on Corporate Governance will be organized to build a public-private consensus on a corporate strategy for Romania to be reflected in a favorable legal framework for implementation.

CIPE/In house, Russia – CIPE - Moscow held a roundtable on corporate governance entitled "Shareholder Rights as an Example of Property Rights: Amendments to Legislation on the Securities Market" at the Moscow Stock Center. More than 20 participants representing think tanks, the Duma, the Central Bank, the Federal Securities Commission, Russian securities exchanges, and the media attended the roundtable. The discussion produced concrete recommendations on specific amendments involving shareholder registries and the desirability of holding public hearings on securities legislation.

CIPE/In house, Asia – Institute of Management Education of Thailand (IMET) in conjunction with the Federation of Thai Industries and the Thai Chamber of Commerce hosted a regional program on corporate governance to explore corporate governance best practices worldwide and identify specific reforms that are needed to help encourage recovery from the Asian economic crisis and help prevent a recurrence. Representatives from the Thai Chamber of Commerce, Thai Federation of Industries, Singapore Chamber of Commerce and Industry, Philippine Chamber of Commerce and Industry, Makati Business Club, Federation of Korean Industries, Malaysian Chamber of Commerce and Industry, called for a set of policy specific recommendations among the business sector, government, media and the general public in order to advance corporate governance reform. This unprecedented declaration shows that many Asian business groups acknowledge that business can and must play a leading role in promoting more transparent interchanges between the public and private sectors. They recommended possible structural and democratic reforms to help prevent a recurrence of the Asian economic crisis and restore international investor confidence in the region.

CIPE/In house, Africa – CIPE is collaborating with the Institute for Economic Affairs (IEA) and the Center for Economic Policy Analysis (CEPA) in Ghana to organize two one day seminars for policy leaders, business and financial community representatives, the media, and international donor community on growth and accountability through sound corporate governance. The goal of the seminars is to increase awareness of the need for effective corporate governance policies and practices among policy makers, business leaders and the financial community. The seminars will attempt to increase investor confidence by introducing best practices to West Africa and also enhance the capabilities of African think tanks and private sector business associations to serve as “centers of excellence” to pursue appropriate activities to promote corporate governance concepts.

