Assessing Corporate Governance in Investee Companies

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EBRD

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Presentation Plan

- The EBRD: what it is and what it does
- Assessing Corporate Governance Practices in investee companies
- Focus on Corporate Governance Codes
What is the EBRD?

- Founded in 1991
- Public financial institution with €20 billion capital
- Operates in 28 countries in Central and Eastern Europe, including the former Soviet Union
- Multinational shareholding: 61 countries, EIB and EU
- Cumulative commitment of €36.9 billion and total project value €115.5 billion
- Largest investor in the region
Where we operate

As of October 2006

Central Europe and the Baltic states
- Croatia
- Czech Republic
- Estonia
- Hungary
- Latvia
- Lithuania
- Poland
- Slovak Republic
- Slovenia

South-eastern Europe
- Albania
- Bosnia and Herzegovina
- Bulgaria
- FRY Macedonia
- Romania
- Montenegro
- Serbia

Eastern Europe and the Caucasus
- Armenia
- Azerbaijan
- Belarus
- Georgia
- Moldova
- Ukraine

Russia
- 23

Central Asia
- 24
- Kazakhstan
- Kyrgyz Republic
- Mongolia
- Tajikistan
- Turkmenistan
- Uzbekistan
Shareholding of the EBRD

EU [27] countries: 62.75%
USA: 10.1%
Japan: 8.61%
Others: 11.27%
EBRD region: 7.28% (excl EU members)
Active in all countries of operations

Cumulative commitments €36.9 billion

- Southeast Europe: 22%
- Russia: 26%
- Eastern Europe & Caucasus: 14%
- Central Europe & Baltics: 31%
- Central Asia: 7%
Portfolio by sector

- Financial Institutions: 31.6%
- General Industry: 12.5%
- Agribusiness: 8.4%
- Natural Resources: 6.6%
- Property & Tourism: 3.4%
- Natural Resources: 6.6%
- Energy Efficiency: 0.2%
- Telecoms: 7.4%
- Transport: 14.4%
- Power & Energy: 8.2%
- MEI: 7.2%

June 2006
Attracting co-investors triples EBRD’s investment

Total project value €115.5 billion

EBRD financing €36.9 billion

Resources mobilised €78.6 billion

Unaudited December 2007
“(...) the purpose of the Bank shall be to foster the transition towards open market-oriented economies and to promote private and entrepreneurial initiative in the Central and Eastern European countries and Mongolia (...)”

It means that every EBRD project is expected to have impact on the transition process (the so-called “Transition Impact”)
Transition Impact

Three areas in which an EBRD project can contribute to transition:

- The structure and extent of markets.
- The institutions and policies that support markets.
- Market-based behaviour patterns, skills and innovation.

The three areas are further divided into seven potential sources of transition impact. One of these is:

Setting standards for corporate governance and business conduct
Setting standards for corporate governance and business conduct

By implementing high standards of corporate governance in investee entities, projects contribute to spreading behaviour and attitudes enhancing the functioning of the market economy.

This is a form of demonstration effect which functions by establishing reference points for other firms and individuals concerning businesses that they wish to invest in or interact with.

Examples:

- Shareholder agreements
- Financial disclosure, IFRS accounts
- Strategic guidance and improved board procedures
- Improvements of corporate governance standards
Presentation Plan

- The EBRD: what it is and what it does
- Assessing Corporate Governance Practices in investee companies
- Focus on Corporate Governance Codes
Assessing Corporate Governance Practices in Investee Companies

1. Understanding where the company stands in terms of corporate governance
2. Benchmarking the company’s practices with best standards: focus on the local framework
3. Developing a “corporate governance improvement plan” with the company
4. Finalise the plan: working with local counsel
1. **Understanding where the company stands**

- Gather all preliminary information on the company
- Developing a questionnaire built on the preliminary company information, country information, type of company, type of operation etc.
- Developing a Corporate Governance Matrix
- Assessing the responses
- Highlight the company needs
- Discussing the responses with the company
2. Focus on the local framework

- Benchmark the company practices (responses to the questionnaire) with national legislation and practices
- Understand the quality and effectiveness of national corporate governance legislation
- Apply national corporate governance codes where possible
- Develop a draft corporate governance improvement plan
...understand the quality and effectiveness of national corporate governance legislation...
Understanding the Legal Framework

1. Legal Sector Assessments: *the law on the books* - extensiveness

2. Legal Indicator Surveys: *how the law works in practice* - effectiveness

A credible assessment requires an evaluation of both these components
Quality of Corporate Governance legislation

How to measure it?

We need a tool to benchmark international standards with national legislation
Corporate Governance: laws on the books

A checklist!
Quality of Corporate Governance Legislation: Corporate Governance Assessment 2008

- Hungary: 77.63%
- Russia: 74.02%
- Czech Republic: 73.31%
- Slovak Republic: 73.13%
- Lithuania: 70.80%
- Slovenia: 69.37%
- Romania: 69.13%
- Kyp trimmed: 68.20%
- Bulgaria: 66.34%
- Poland: 65.46%
- FYR Macedonia: 65.01%
- Uzbekistan: 64.43%
- Latvia: 62.55%
- Mongolia: 61.89%
- Croatia: 61.62%
- Serbia: 60.97%
- Armenia: 60.44%
- Moldova: 60.24%
- Kazakhstan: 59.85%
- Estonia: 58.68%
- Albania: 48.12%
- Turkmenistan: 47.98%
- FYR Macedonia: 46.92%
- Montenegro: 46.61%
- Georgia: 44.25%
- Tajikistan: 42.56%

Country abbreviations are used in the chart.
Ensuring the basis for an effective corporate governance framework

The Responsibilities of the Board

The rights of shareholders

Disclosure and Transparency

The equitable treatment of shareholders

The role of stakeholders in corporate governance

The responsibilities of the board

The rights of shareholders

Disclosure and transparency

The equitable treatment of shareholders

The role of stakeholders in corporate governance

0%

25%

50%

75%

100%
How to assess how corporate governance works in practice?

It requires the identification of a situation able to provide information on how the law is implemented.
How to assess how corporate governance works in practice?

.... a case study!
Extensiveness and Effectiveness: The Implementation Gap
Presentation Plan

- The EBRD: what it is and what it does
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- Focus on Corporate Governance Codes
## Overview of CG Codes in the EBRD Region: CEB

<table>
<thead>
<tr>
<th>Country</th>
<th>Name of the Code</th>
<th>Date</th>
<th>Drafting Authority</th>
<th>Reference in</th>
<th>Comply or explain</th>
<th>Supervision</th>
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<tbody>
<tr>
<td>Czech Republic</td>
<td>Corporate Governance Code</td>
<td>June 2004</td>
<td>Czech Securities Commission</td>
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<td>Hungary</td>
<td>Corporate Governance Recommendations</td>
<td>August 2007</td>
<td>Budapest Stock Exchange</td>
<td>Section 312 of the Companies Act</td>
<td>Yes</td>
<td>Formal</td>
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<td>Lithuania</td>
<td>The Corporate Governance Code for companies listed on the Vilnius Stock Exchange</td>
<td>August 2006</td>
<td>Vilnius Stock Exchange (VSE)</td>
<td>VSE Trading Rules - Rule 23.5</td>
<td>Yes</td>
<td>Formal (VSE can make an analysis of data and make it public)</td>
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<td>Jurisdiction</td>
<td>Name of the code</td>
<td>Date</td>
<td>Drafting Authority</td>
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<td></td>
<td>Federation of Bosnia and Herzegovina</td>
<td>April 2006</td>
<td>Securities Commission</td>
<td>Art 83 of the Rules of the Sarajevo Stock Exchange</td>
<td>No (Bylaws and Annual Report)</td>
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<td>FYR Macedonia</td>
<td>Corporate Governance Code for Companies Listed on the Macedonian Stock Exchange</td>
<td>January 2006</td>
<td>Skopje Stock Exchange</td>
<td>Listing Rules</td>
<td>Yes</td>
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<td>Montenegro</td>
<td>Corporate Governance Code Manual for Montenegro</td>
<td>July 2003</td>
<td>EU funded project</td>
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<tr>
<td>Romania</td>
<td>Corporate Governance Code (a new Code is being developed)</td>
<td>August 2001</td>
<td>University of Bucharest The new Code is being developed by the BSE</td>
<td>Art. 94 of the Code of the BSE Market Operator, Book I – Open Regulated Market, Title II</td>
<td>Yes (new Code)</td>
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<td>Serbia</td>
<td>Code on Corporate Governance</td>
<td>September 2008</td>
<td>Belgrade Stock Exchange</td>
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<td>Yes</td>
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## Overview of CG Codes in the EBRD Region: CIS

<table>
<thead>
<tr>
<th>Country</th>
<th>Name of the code</th>
<th>Date</th>
<th>Adopted by the stock exchange</th>
<th>Reference in</th>
<th>Comply or explain</th>
<th>Supervision</th>
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<td>Armenia</td>
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<td>July 2007</td>
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<td>Moldova</td>
<td>Code of Corporate Governance</td>
<td>June 2007</td>
<td>Yes</td>
<td>Accountancy Law</td>
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<td>Russia</td>
<td>Code of Corporate Conduct</td>
<td>April 2002</td>
<td>No</td>
<td>Secondary Regulation</td>
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<td>Tajikistan</td>
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<td>Turkmenistan</td>
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<td>Ukraine</td>
<td>Corporate Governance Principles</td>
<td>June 2003</td>
<td>No</td>
<td>None</td>
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<td>None</td>
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<td>Uzbekistan</td>
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Corporate Governance of Banks in Eurasia: A policy brief

- Corporate Governance Codes: implementation is the key
- Many countries in the EBRD region do not have functioning stock exchanges
- Banking industry well developed in all countries
- Specific set of guidelines for banks
- Banks as vehicle for improving corporate governance of investee companies
3. Developing a “corporate governance improvement plan” with the company

- Benchmark the company practices (questionnaire + discussion) with national legislation and practices
- Develop a draft corporate governance improvement plan
- Preliminary discuss the draft plan with the company (focus on company’s objectives)
- Get a preliminary agreement
4. Finalise the plan: working with local counsel

- Hire a local counsel
- Instruct the local counsel to perform a “Corporate Governance Due Diligence” (with particular reference to the statutory requirements)
- Confirmation of the priorities stated in the plan
- Refine the plan
- Get the final agreement on the plan
- Build an implementation schedule
Thank you!

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