Mainstreaming Corporate Governance Risk Analysis in the Investment Process

Presentation to DFI Meeting
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What is Mainstreaming?

✓ Easier process for IOs to secure CG Assessments by CG Unit and simplified CG Review tools and training for IOs to address 5 areas of CG risk and opportunity:
  
  o **Commitment** - the tone at the top and if the client values and relies on good CG - understands business benefits
  o **Board of Directors** - function and structuring of the board of directors - appropriate oversight and strategic roles
  o **Control Environment** - internal audit and internal controls - essential for appropriate risk management and efficiency
  o **Transparency & Disclosure** - accurate financial statements & appropriate reporting of financial information
  o **Minority Shareholder Rights** - treatment of investors like IFC

✓ Training for all investment staff - training on use of simple and field tested CG tools - CG Report generator & Matrix
What is Mainstreaming?

- A structured approach to assessing CG Operational Risk and enhancing Development Impact - Systemic CG risk assessment for IFC investment transactions using IFC’s CG Methodology - relies on IFC’s risk-tiering to determine level of analysis

- **Output:** Short CG report, a single IRM slide & discussion on risks and opportunities at IRM (for internal use only)

- **Value added for company:** When needed, as an add-on to appraisal - the CG Unit, for a separate fee, will deliver a CG Assessment to the client including a CG Improvement Program, presentation & suggested sequencing and timeline

- **Portfolio companies:** CG Unit can provide Assessments for fees

- **Tier III, CG Unit led Assessments** - required as of 9/30/2010

- **Tier I & II, IO led Reviews** - required after 7/1/2011
IFC’s Risk Based Tiering of Investment Decisionmaking Authority

- As part of effort to decentralize operations and delegate investment decisionmaking - three tier structure based on:
  
  - **Size and type of investment:** Higher thresholds for debt than equity
  - **Risk rating:** IFC Credit Risk Rating (CRR) - rating from one to six with six being greater risk - many risk factors incorporated including CG
  - **Innovation:** New investment products given fuller review

- Tier III - Committee of IFC Senior management (COC) - CG Assessment by a member of the CG Unit
  - Debt > $75m, Equity > $25m, CRR of 5 or 6

- Tier I & II - CG review by Investment Team
  - Delegated to manager and director levels accordingly
  - Lower thresholds for debt, equity and CRR
How level of CG Analysis is Determined at CRM

Risk Tiering from BPI

Tier III Deals (COC)

Tier II Deals (Director)

Tier I Deals (Manager)

Level of CG Analysis

CG Assessment:
CG Officer assigned to the deal and joins appraisal - risk report and slides to Investment Team

CG Review:
Investment Team, using CG Review tools, short written risk assessment and slide for IRM discussion.

All Tier III deals candidate for CG Assessment, but lead Director can opt for CG review by IOs instead

If CG risk identified early, seek CGA

All IOs trained in applying the CG Review tools
What would IOs need to do:

✓ COC-tier or high CG risk deals:
  • CG Assessment by CG Unit - include CG Officer in appraisal team, cover travel expenses from client fees - include CG Officer outputs in reports (CG Assessment and Slide for IRM)
  • If chairing Director waives CG Assessment, conduct CG Review as part of appraisal

✓ Non-COC tier:
  • Conduct CG Review using CG Review report tools - attend CG training
  • Think through CG risks ahead of appraisal and ask a few additional questions and document findings and recommendations
  • Prepare short review of CG issues and slide for IRM

✓ Where appropriate:
  • Sell CG value added services to clients committed to CG improvement
What would Directors need to do:

✓ COC-tier:
  • Decide, at CRM when COC tiering is confirmed, to either go forward with **full CG Assessment by the CG Unit**, or to waive CG Unit involvement and **rely on IO’s CG Review of risks**

✓ Non-COC tier:
  • Standard case - Ensure that IOs conduct CG Review as part of appraisal
  • If obvious CG risks at CRM (will be rare) - **seek CG Assessment by CG Unit**

✓ All deals:
  • Review CG slide in IRM deck and discuss risks and opportunities as needed
What would change?

✓ Better CG analysis for decisionmaking - consistent analysis/rating of risk
✓ Risk based allocation of CG efforts - CG Officer for all COC tier deals
✓ Simplified CG Review by IOs: new tools and training already field tested
  • Training, tools and support = better, more informed CG discussions at IRM
✓ Better articulated CG development impact - CG in DOTS
✓ Value added services available for clients on a fee basis

What would not change?

✓ Lead/Chairing Director decides - but with better information
✓ CGU advises Investment Team on risks - suggests strategy to address risk
✓ IOs decide how to use CG specialist input in their business decisionmaking: no clearances, approvals or mandatory CG attendance at CRM
✓ Reinforces IFC’s strong commitment to Corporate Governance
Corporate Governance in IFC

IFC Corporate Governance Unit
- Supports IFC investments
- Company assessments
- IO training
- Support to IFC Nominee Directors
- Global DFI Leadership

Private Good: CG Advice to IS & AS Client Companies

IFC Field-based CG Projects
- Implementing good CG practices
- Company interventions
- Capacity building
- Raising local awareness
- Bridging Investment and Advisory operations

Public Good: CG Enabling Environment Support

Global Corporate Governance Forum
- Global CG KM Platform
- CG reform tools and best practices
- KM training
- Centers for CG excellence for increased outreach and south-south capacity building

“IFC has learned that a comprehensive approach to CG is essential. It is not possible to work on the business case for CG in the absence of an adequate legal framework.”

-External Review of CG Projects-