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# CORPORATE GOVERNANCE *“CREATE A POSITIVE CHANGE”*

Güler Manisalı Darman  
International Chamber of Commerce



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## INTERNATIONAL CHAMBER OF COMMERCE (ICC)

- is the voice of world business championing the global economy as a force for economic growth, job creation and prosperity
- was founded in 1919
- has members in 130 countries
- has a cooperation agreement with JCI



# Corporate Governance Worldwide

- In the 20th century, modern corporations became one of the world's dominant institutions. Consequently the way they do business is now under close scrutiny



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# Corporate Governance Worldwide

Good corporate governance is an essential element of sustainable economic growth in a market economy

***Güler Manisali Darman,  
Author, Corporate Governance Worldwide  
JCI Turkey founding member***



# Corporate Governance Worldwide

The proper governance of companies will become as crucial to the world economy as the proper governing of countries

*James Wolfenson, President of World Bank*



# Corporate Governance Worldwide

## What is corporate governance?

Corporate governance refers to rules, regulations and best practices which ensure that boards and management secure the rights of shareholders, improve competitiveness, and enable access to capital in global markets

It should not be confused with management, which is concerned with day-to-day running of business



# Corporate Governance Worldwide

## Factors that contribute to good governance

- **accountability**
- **financial disclosure and transparency**
- **independence of the board**
- **shareholders' and other stakeholders' rights, equal treatment of shareholders**
- **ethical behavior and leadership**



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## The Board

Board is the key corporate governance mechanism. This is the process by which management is monitored by (outside) directors on behalf of shareholders in order to align the interests of all sides



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## The Board

Boards who realize the importance of human element, a chemistry that cannot be qualified, become effective and robust. Members of such boards behave in integrity, challenge each other's views and beliefs, but also respect each other

Welcome (my friend) aboard, but don't change a thing!



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## Board committees to ensure good governance

### **Audit Committee**

It is responsible for monitoring and safeguarding auditing and non-audit services

### **Nomination Committee**

Makes board appointments and ensures the independence of board members

### **Compensation Committee**

Deals with executive remuneration and puts together remuneration packages



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## Shareholders as shareowners

The ownership and control structure of a corporation should be fully transparent to all shareholders under all circumstances



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# Corporate Governance Worldwide

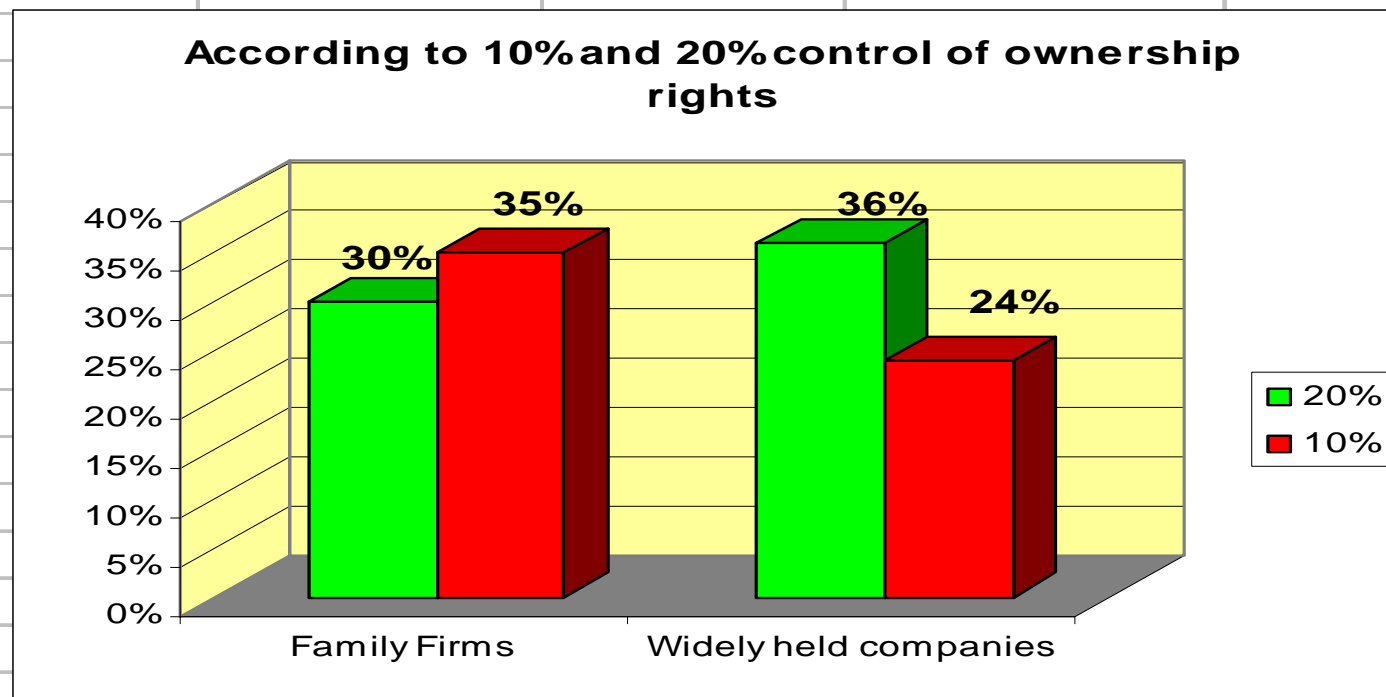
## Shareholders as shareowners

However, once the shareholders have invested, the capacity to exercise their rights may be abrogated by the management of the corporation and their power to influence the company can be minimal.

Therefore, the corporate governance framework aims to preserve the rights of, and minimize the risks to shareholders



# Corporate Governance Worldwide



Source: Rafael La Porta, Florencio Lopez-de Silanes, Andrei Shleifer

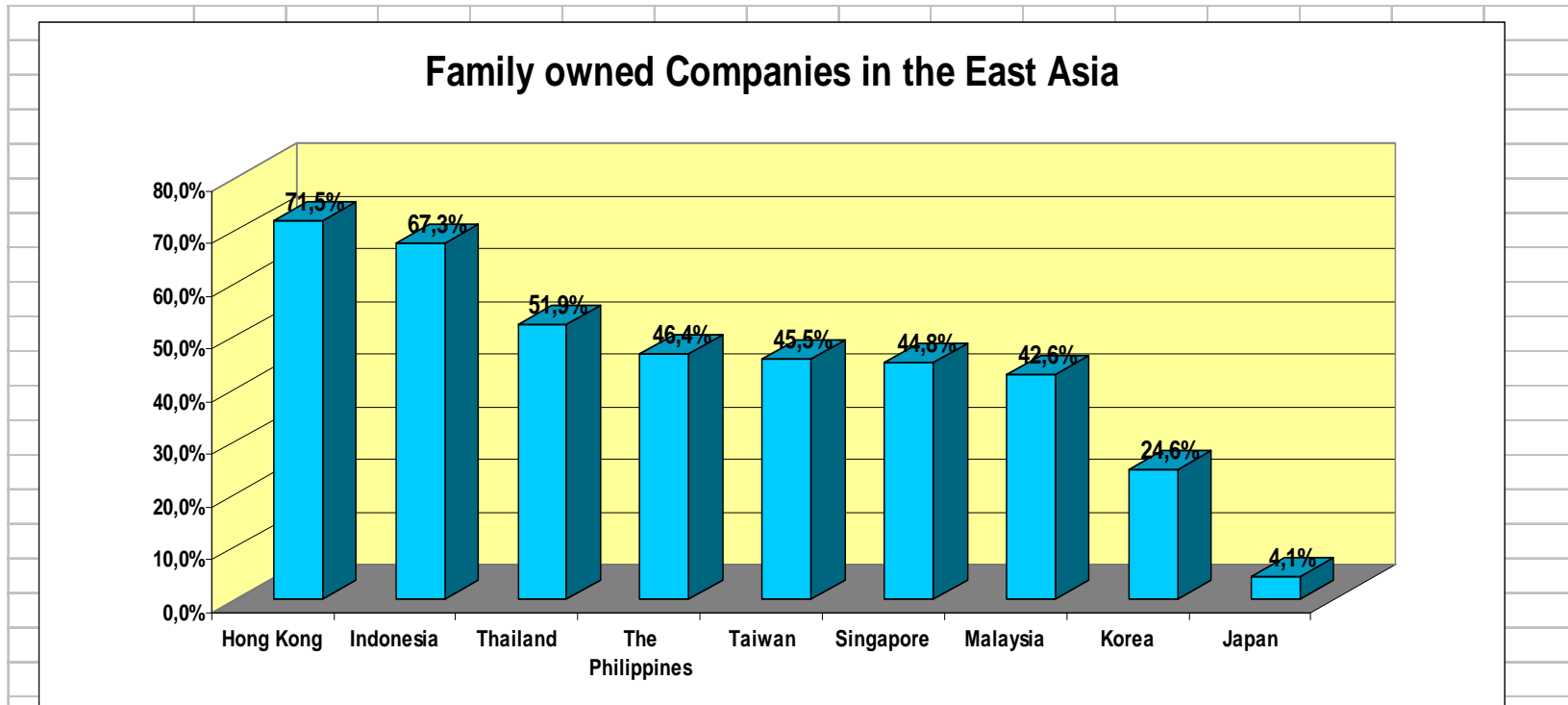
"Corporate Governance Around the Globe"

The Journal of Finance, Vol LIV No:2 April 1999

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Source: Stijin Claessens, Simeon Djankov, Larry H.P. Lang, "Who controls East Asian Corporations", Policy Research Working Paper, The World Bank, Şubat 1999

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# Corporate Governance Worldwide Hypothetical Cases

Case A: Case A: [www.widely-held-company.com](http://www.widely-held-company.com)

- Present Picture
- The weaknesses and failures [www.widely-held-company.com](http://www.widely-held-company.com) may encounter in its governance

Case B: Case A: [www.closely-held-company.com](http://www.closely-held-company.com)

- Present Picture
- The weaknesses and failures [www.widely-held-company.com](http://www.widely-held-company.com) may encounter in its governance



# Corporate Governance Worldwide

## Case A: [www.widely-held.com](http://www.widely-held.com) (1)

- Global multinational, too big to fail, enjoys many business opportunities
- Has many affiliates, subsidiaries, joint ventures in 30 countries
- Has more than 25000 employees
- Turnover more than \$25bn
- Has a flexible structure in operational activities



## Corporate Governance Worldwide Case A: [www.widely-held.com](http://www.widely-held.com) (2)

- Chairman and the CEO is the same person
- Has non-executive board-members some of which are said to be independent
- Heavily relies on financial engineering
- Is being rated
- Has good legal consultants



The weaknesses and failures [www.widely-held.company.com](http://www.widely-held.company.com) may encounter in the governance (1):

- Two classes of stock. Outside shareholders are restricted to ownership of one vote per share Class A stock, while insiders control the non-publicly traded Class B shares, which have ten votes per share
- A minority of independent board members shadows the eligibility of the board
- One director is a senior partner of the legal company that gives consultancy services; there are interlocking relations



The weaknesses and failures [www.widely-held.company.com](http://www.widely-held.company.com) may encounter in the governance (2):

- No succession planning
- There are no truly independent directors (or minority) in the compensation and audit and nomination committees
- No written charter of these committees
- It is not clear whether it is within the authority of the Audit Committee to hire or fire the company's auditors
- Serious concerns and questions about the efficacy of the Audit Committee
- There is extensive related party transactions involving senior management over the last few years



The weaknesses and failures [www.widely-held.company.com](http://www.widely-held.company.com) may encounter in the governance (3):

- Many shareholder class-action lawsuits
- Not enough information on the company website
- Exercising voting rights are too costly and burdensome; drawbacks on proxy voting
- The company does not allow its shareholders to vote by phone or mail
- There is no disclosure as to how the CEO is compensated
- Despite reported poor earnings, top executives are granted a highly considerable amount of options
- All sorts of accounting abuses, and gimmicks
- No code of ethics



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## Case B: [www.closely-held company.com](http://www.closely-held-company.com) (1)

- Listed company, the controlling shareholder is a family in the second generation
- Has many affiliates, subsidiaries, joint ventures in more than 10 countries
- Has more than 15000 employees
- Turnover more than \$15bn
- Grows continuously, enjoys many business opportunities in and abroad



## Corporate Governance Worldwide

Case B: [www.closely-held company.com](http://www.closely-held-company.com) (2)

- Still relies on debt financing
- Chairman and the CEO is *not* the same person
- Has non-executive board-members, none of them are truly independent
- Is being rated
- Has good legal consultants



The weaknesses and failures [www.closely-held.company.com](http://www.closely-held.company.com) may encounter in the governance (1):

- Pyramid structure groups of companies, may be cross holding
- Owner(s)/executives have a lavish style
- No independent board members – majority of the board members are employees or family members
- Serious problems in succession planning
- No independent internal auditing



The weaknesses and failures [www.closely-held.company.com](http://www.closely-held.company.com) *may* encounter in the governance (2):

- No audit, compensation and nomination committees
- Contention between the young and the old generation family members
- Family name/friendship is a knee-jerk criteria for employment & promotion
- Accounting only according to tax accounting and to national GAAP largely based on historical cost accounting



The weaknesses and failures [www.closely-held.company.com](http://www.closely-held.company.com) *may* encounter in the governance (3):

- No uniformity in charter of accounts among the group companies
- Lack of healthy consolidation
- Self financing or debt financing, great trouble with debts, but can either roll on, or postpone or pay only the interests
- Executives receiving compensation based on *bogus* revenues and unrealized profits



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The weaknesses and failures [www.closely-held.company.com](http://www.closely-held.company.com) may encounter in the governance (4):

- Keeping records in off-balance accounts through SPEs
- Crony capitalism in and abroad
- All sorts of accounting abuses, and gimmicks
- No code of ethics



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# Why to urge for High Standard Corporate Governance Principles!

Corporate Governance Constituents

**Shareholders**

**(Individual & Institutional Investors)**

**Board of Directors**

**CEO**

**Regulator, Insurer, Media, Supplier, Auditing Companies,  
Investor, Creditor, Employee, Customer, Society**



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- Recent corporate scandals and failures like Enron, WorldCom in USA, Parmalat in Italy , Ahold in the Netherlands, and Yanguangxia in China have accentuated the importance of good governance practices



# Corporate Governance Worldwide

## Corporate Scandals – Parmalat in Italy

- The debt burden was nearly €14.8 billion
- Shareholders' and savers' money went up in smoke
- Creditors all over the world prepared class-action suits
- The US life insurance industry was also seriously affected
- The auditors reputation was tarnished
- Banks came under scrutiny
- Questions were raised over the added value that rating agencies provide



## Corporate Governance Worldwide

The decline in public trust has to be restored. Companies and institutions cannot afford to have their reputations tarnished by inadequate oversight and unethical governance, nor can national economies continue to suffer from laxity and fraud in corporate activities



## Listing Requirements (1)

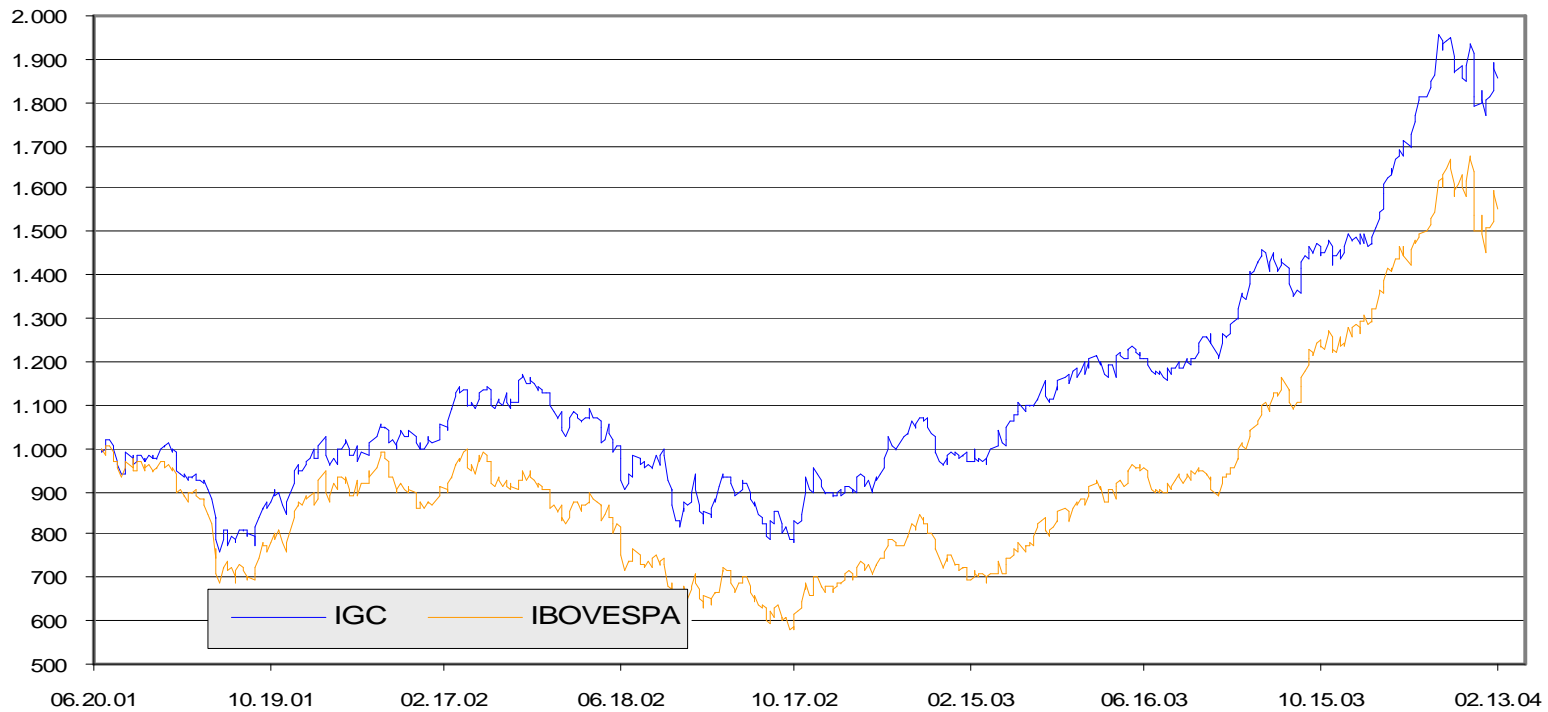
New York Stock Exchange  
NASDAQ,

or

BOVESPA, Brazil's Stock Exchange, NOVO  
MERCADO  
Borsa Italiana, Star



# IGC – IBOVESPA 26/6/2001 – 16/2/2004



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## Listing Requirements (2)

BORSA ITALIANA - “STAR” is another example of stock market segments that have decided to adhere to higher corporate governance standards. Created by Borsa Italiana in April 2001, STAR, an Italian acronym for Segmento Titoli con Alti Requisiti” (High Standard Mid Cap Market), is the segment of the Electronic Equity Market (Mercato Telematico Azionario – MTA) reserved for high-quality small- and medium-sized companies with a market capitalization less than 800 million euros.

Performed better than other comparable indices in Europe (in 2000 : + 23 per cent better than the London FTSE Small Cap, +17 per cent more than the Frankfurt SMAX



# Corporate Governance Worldwide

The McKinsey & Company Global Investor Opinion Survey 2002 reveals that Investors are willing to pay higher premiums for the shares of a well-governed companies. These Premiums are:

<b>North America &amp; Western Europe</b>	<b>:</b>	<b>12 – 14 %</b>
<b>Asia &amp; Latin America</b>	<b>:</b>	<b>20 - 25 %</b>
<b>Eastern Europe &amp; Africa</b>	<b>:</b>	<b>30 %</b>

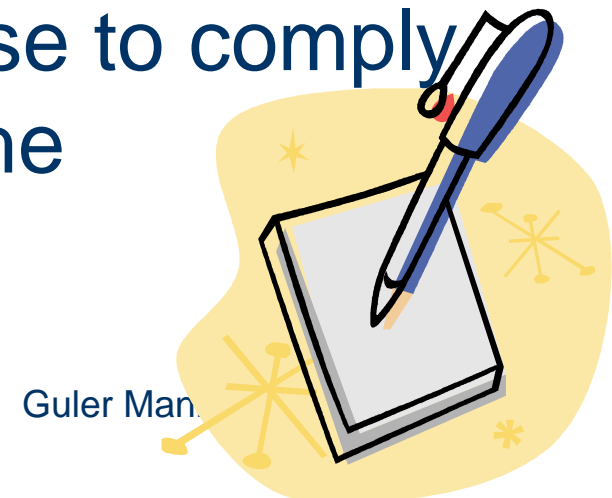
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But how companies conform to these principles and put them into practice is as important as their acceptance. Good corporate governance practices are not merely a box-ticking exercise to comply with a form; they are also the substance



# Corporate Governance Worldwide

Good corporate governance is shared responsibility. Corporate responsibility is the core of the issue. Responsible behavior is the linchpin of corporate credibility, and corporate credibility is closely linked to corporate responsibility



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corporate credibility @ corporate  
responsibility.com



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# Corporate Governance Worldwide and JCI (1)

JCI operates on the premise that the development of individual character and personality will result in communities that are better developed and, eventually, in a more peaceful world



## Corporate Governance Worldwide and JCI (2)

JCI is a people organization.  
It offers its members  
opportunities that will  
reinforce humane attributes  
such as communication,  
understanding, patience,  
and tolerance



## Corporate Governance Worldwide and JCI (3)

At this point begins the role JCI can or, more than that, should play in the proliferation of good governance practices because we must remind ourselves that JCI was founded to address global concerns.



**We are the BRIDGE.**

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