

Corporate Governance

Sound governance of corporations plays important roles in attracting investment, establishing a healthy private sector, and building democratic societies. Well-governed companies tend to perform better and contribute to long-term productivity and growth. Equally important, good governance instills the core values of transparency, fairness, accountability, and responsibility. When these values spread throughout an economy, they buttress accountability in the political system and close off space for corruption. Good corporate governance likewise breaks the hold of vested interests that would otherwise undermine the proper functioning of markets and inhibit the development of democratic political institutions.

CIPE programs educate corporate directors in fundamental corporate governance principles; educate shareholders on their rights and responsibilities; and raise public awareness of the need for effective corporate governance practices. Partners in countries such as Egypt have crafted national codes of corporate governance that meet international standards while recognizing local business realities. Across Asia and the Pacific, a network of development finance institutions has implemented a corporate governance rating system to monitor potential areas for reforms.

Advancing Transparency and Accountability

by Jen Maceyko

Egypt undertook comprehensive reforms in the 1990s, including large-scale privatization and development of the capital market, as it shifted toward a market economy. Despite these efforts, the financial collapse of a number of major companies revealed the need for widespread adoption of corporate governance principles within the Egyptian business community. In a 2005 survey commissioned by the Center for International Private Enterprise (CIPE) of owners of listed and unlisted Egyptian companies, 92 percent agreed that corporate governance is one of the best ways to protect a company and promote economic development. The adoption of sound corporate governance principles creates safeguards against corruption and mismanagement while promoting transparency.

In October 2005, the Egyptian Institute of Directors (EIOD) issued the Egypt Code of Corporate Governance, developed by CIPE and local partners in consultation with the business community, accountants, and auditors. This was the first national governance code in the world to be written entirely in Arabic. It was created from scratch to suit Egypt's legal and regulatory environment and stakeholder requirements.

The code aims to promote transparency, openness, ownership, and responsibility, and to incorporate these values into Egypt's changing cultural mindset. "Implementing corporate governance in the right manner is not limited to respecting a set of rules and interpreting it literally in a restricted manner; it is also a culture and way of managing the relationship between owners of the company, its directors, and its stakeholders. Hence the interest of the whole community becomes more achievable when more people apply the code provisions."* By advancing best practices and concurrently enhancing the reputations of companies that adhere to the code, this governance initiative has laid the groundwork for an improved investment environment.

Creating the Code

EIOD and CIPE developed the governance code in several stages. The first stage conducted a review of international best practices in the realm of corporate governance in order to provide the group with a solid foundational understanding of corporate governance. The review formed an in-depth picture of the development and implementation of similar codes in other countries. The next stage carried out a review of the current legal framework in Egypt – including local literature, reports issued by Egyptian and international organizations, and summaries of discussions held at workshops and seminars previously held by CIPE. This stage was followed by discussions with the EIOD to establish the legal nature and scope of the code. While voluntary in nature, the code would be based on the capital market and company laws.

Dr. Ziad Bahaa El-Din, a local expert on investment and trade, drafted the first version of the code, which was presented to meetings of private sector and government representatives in early 2005. These groups included representatives from the Cairo and Alexandria Stock Exchange, the Egyptian Capital Market Authority, the Egyptian Banking Institute, and numerous business associations. At a series of workshops and seminars, they were asked to evaluate how the draft code could be more effective and applicable to economic and private sector development in Egypt. CIPE also surveyed business owners on individual items in the draft code. Responses from the groups were incorporated into the final version of the code, which was then presented to the EIOD for approval.

CIPE's partnership with EIOD produced the first national corporate governance code in the world to be written entirely in Arabic. The code serves as a model for similar private sector-driven initiatives in the region.

A Guide for All

Written in language accessible to all potential users, the Code of Corporate Governance defines the rights and responsibilities of corporate shareholders, boards of directors, internal and external auditors, and audit committees. It calls for full disclosure of

financial information and corporate policies to shareholders, board members, staff, and the public. The code also prescribes measures to avoid conflicts of interest.

While the code was written primarily to aid publicly traded corporations and financial institutions, it also applies to small and privately owned businesses. In the Middle East, as many as 90 percent of businesses are family-owned. All types of companies are urged to comply with the code to the best of their ability and to embrace the principles of accountability, responsibility, transparency, and trust that serve as its foundation. While the governance mechanisms of family-owned businesses differ from those of publicly traded companies, these businesses still contribute to a societal culture of corporate governance and must address the interests of their stakeholders.

The Egyptian code will be used as a model for similar private sector-driven initiatives in the region. It is hoped that external auditors and legal advisors will press corporate directors to abide by the code, and that banks and credit rating institutions will consider corporations' adherence to the code as part of their assessments. Corporations that comply with the code will reap the benefits of investor and public confidence in addition to improved performance.

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Note

* *Egypt Code of Corporate Governance, Guidelines and Standards* (Oct. 2005) section 1.4.

Sources

Egypt Code of Corporate Governance, Guidelines and Standards (Oct. 2005).

"Egypt Releases Corporate Governance Code," *Corporate Governance Trends* 8 (Summer 2005).

Scoring Corporate Governance: A Framework for Implementation

The Asian financial crisis of 1997 underscored the need for governance reform not only in the business community but also in national development finance institutions (DFIs). DFIs are established by governments to provide long-term financing and technical assistance to sectors of the economy not served by other providers of capital. Unlike regular commercial banks, development banks provide training and management expertise in addition to financial assistance. They can therefore play a central role in advancing corporate governance reforms. To effectively promote good corporate governance, however, DFIs must first institute good corporate governance practices themselves.

In response to this need, the Philippines-based Association of Development Financing Institutions in Asia and the Pacific (ADFIAP) began the DFIs for Corporate Governance Project in 2003 in partnership with the Center for International Private Enterprise (CIPE). ADFIAP's goal is to advance sustainable development by bringing together the national development banks and promoting mechanisms of good corporate governance. ADFIAP encourages DFIs to adopt and institutionalize good governance policies and practices, not simply because it is the "right thing to do," but because it is essential to business success.

Deputy Secretary General of ADFIAP Octavio B. Peralta has pointed out, "Effective boards of directors are vital if efforts to 'corporatize' DFIs are to be successful. Simply recognizing that corporate governance is important is not enough; board members must clearly understand their responsibilities and must have sufficient training and knowledge."

The Corporate Governance Scorecard

As part of its strategy to improve corporate governance, ADFIAP embarked on a new project to develop a corporate governance

“scorecard” for DFIs and their clients. Participants at a regional workshop in Manila developed an assessment and monitoring instrument called the ADFIAP Corporate Governance Rating System (ACGRS). This system, an adaptation and expansion of two existing international governance rating methods, monitors potential areas for governance reforms. ADFIAP was able to draw on CIPE’s wide network of corporate governance experts in developing the system.

Because the corporate sectors of ADFIAP countries share similar structures and legal frameworks, the adoption of a corporate governance rating system is a suitable and practical measure. By using a common system, concerned government, multilateral, and private institutions can monitor the progress of corporate governance reforms within each country and compare their progress with others in the region. The areas for improvement and relative importance of each reform area are clearly specified in the rating system.

The ACGRS clarifies the overall state and quality of governance in the financial institution by tracking the changes in governance policies and practices over time. Specifically, it consists of a questionnaire that requires a respondent to assess the corporate governance practices of their institution. There are two versions of the scorecard: one for DFIs and another for commercial banks and other financial institutions. A survey administrator converts the responses to a weighted score for each question using a predetermined point equivalence system. The scores for each criterion are consolidated into an overall weighted institutional corporate governance average. The weights for each governance criterion are: shareholder rights, 25 percent; commitment to corporate governance, 20 percent; board governance, 25 percent; disclosure and transparency, 15 percent; and auditing, 15 percent. The detailed point system is accompanied by matching checklists for each of the five elements.

Development finance institutions across Asia and the Pacific now have corporate governance policies or codes and key persons or units in their organizations who monitor and implement corporate governance programs and activities.

The ACGRS has been reviewed, tested, and revised in five national workshops held in Fiji, Malaysia, Mongolia, Pakistan, and Vietnam. The final version, developed in Manila, is being implemented by ADFIAP member institutions.

The ACGRS: A “Trailblazer”

This project has produced clear insight into the implementation of corporate governance practices among DFIs. Eight out of 10 ADFIAP member institutions now have corporate governance policies and/or codes approved by their respective boards of directors, and almost all of them have key persons or units in their organizations who monitor and implement corporate governance programs and activities. A total of 79 institutions – ADFIAP members, affiliates, and other networks – have participated in the program, along with 165 directors and senior managers from 23 countries in the region. ADFIAP itself has grown into a leading authority on governance matters, thanks in part to CIPE’s assistance with strategic planning over the years.

DFIs are “trailblazers” in the sense that they finance start-up projects that other financial institutions tend to avoid because of the inherent risks and long-term gestation of such projects. This initiative has provided ADFIAP’s member institutions with a chance to become model good governance institutions for sustainable business.

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Sources

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