

Promoting Good Corporate Governance

Sustainable businesses are well governed businesses. Well governed companies benefit from higher prices for their shares, have access to cheaper debt, and just perform better than their poorly governed peers. Firms with transparent and professional systems of direction and control are also more likely to understand the importance of taking social and environmental considerations seriously and mainstreaming them into their operations.

IFC systematically examines corporate governance in its investment process, and is a leader in the dialogue on corporate governance in emerging markets. We work with clients to improve their practices, looking at five dimensions in particular:

- Commitment to good corporate governance
- Equitable treatment of shareholders and other financial stakeholders
- The control environment
- Transparency and disclosure
- The role and functioning of the Board of Directors

Rather than rating a company's governance, IFC's analysis is designed to come up with practical solutions that add value to companies in which IFC is making an investment.

In addition to client companies, IFC provides advice on corporate governance issues to governments, regulators, stock markets, institutes of directors, and other private sector players. Since 2000, IFC has co-sponsored the Latin America Corporate Governance Roundtable with OECD. IFC also regularly contributes to similar fora in Asia, Eurasia, and Russia. The Global Corporate Governance Forum is now housed in the IFC/World Bank Corporate Governance Department.

In 2005, we launched a Companies Circle of firms recognized for their good governance practices to provide practical private sector input to the work of the Latin America Roundtable. The Circle recently published a set of case studies of their experiences in reforming and improving their own corporate governance practices, for the benefit of the broader market of Latin American businesses.

Policies for engagement through directorships in equity investments

As of November 2005, IFC had about 1,380 companies in its active investment portfolio. Of these, IFC had equity investments in 625 companies, 136 of which (10 percent of all companies) had an IFC-nominated director on their board. A majority of the companies in which IFC has nominated a director are financial intermediaries, including private equity funds, banks and insurance companies. In the companies with IFC directorships, the outstanding equity exposure is \$784 million – representing approximately 34 percent of IFC's total outstanding equity exposure.

In order to better ensure that our director nominees play a value-adding role on boards and to manage IFC's reputational risk, we maintain a formal set of policies and procedures and a monitoring system for directorships.

Our current policy on directorships outlines the factors that should be considered before we decide to nominate a director, including the current composition and quality of the board, any gaps in expertise that the nomination seeks to fill and the prospects for implementing better governance practices in the company. We also rolled out a revised training program for all IFC-nominated

directors in 2005. This program highlights that IFC's director nominees owe exclusive duties of care and loyalty to the company on whose boards they sit.

In addition, subject to their fiduciary obligations to our clients, insider trading laws, and similar considerations, IFC-nominated directors report annually to IFC on the activities and status of the board and the nominee's contribution to its effectiveness. The monitoring system aims to facilitate access to all essential company board documents and details of voting records.

From June 2006 all newly nominated directors will receive mandatory training in IFC's directorship policy and good corporate governance principles as part of the Corporate Governance Department's program of semi-annual director trainings.

Voting shares

IFC advocates improved corporate governance and offers both support and advisory services to further this goal. However, we may not be seen as managing the company or as a sponsor, and will limit our role in the investee company to that of a minority investor. Because of these restrictions, we will generally refrain from exercising our voting rights unless the matter to be voted on is considered necessary to protect IFC's interests or further a corporate goal. One example in which IFC has played a role in influencing corporate governance is a joint investment made by IFC and the European Bank for Reconstruction and Development (EBRD) in 2004 in Romania's Banca Comerciala Romana (BCR).

IFC purchased 12.5 percent of the shares of BCR, which was predicated on an overhaul of the bank's governance structure and practices, the reformulation of its Board of Directors, and training on corporate governance for its senior management and new Board members. Later that year, Fitch Ratings upgraded BCR's individual rating to "C/D" from "D", and Standard & Poor's rating of the company went from BB- to B+. In each case, corporate governance was cited as among the improvements undertaken at the bank on the advice of IFC.

 www.ifc.org/corporategovernance



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