Survey of Corporate Governance Practice in the Kyrgyz Republic
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CONTENTS

INTRODUCTION .................................................................................................................................................. 3

THE IMPORTANCE OF CORPORATE GOVERNANCE IN THE KYRGYZ REPUBLIC ................................. 4
  1.1. Corporate governance in the banking sector of the Kyrgyz Republic ................................................................. 4
  1.2. Background of the formation of corporate governance in the Kyrgyz Republic .................................................. 5

SURVEY OF CORPORATE GOVERNANCE PRACTICES IN THE KYRGYZ REPUBLIC .......................... 7
  1.1. The purpose of the survey ........................................................................................................................................ 7
  1.2. Methodology .......................................................................................................................................................... 7
  1.3. Timeframe .............................................................................................................................................................. 8
  1.4. Survey Coverage ................................................................................................................................................... 8

SECTION I. JOINT STOCK COMPANIES

SUMMARY OF SURVEY ........................................................................................................................................ 10
  1.1. Awareness of and commitment to international practice in corporate governance .............................................. 10
  1.2. Management of joint stock companies: General Meetings of Shareholders, Board of Directors and Executive Body ................................................................................................................................. 11
  1.3. Disclosure of information and transparency of companies’ activities .................................................................. 13
  1.4. Monitoring and auditing of financial and operational activities ........................................................................... 14
  1.5. Compliance with the Kyrgyz Republic legislation on corporate governance .................................................... 14
  1.6. Identifying areas of concern in the corporate governance practices .................................................................. 15

CORPORATE GOVERNANCE PRACTICE IN JOINT STOCK COMPANIES .................................................. 16
  1.1. General information on joint stock companies ........................................................................................................ 16
  1.2. Commitment to best practices in corporate governance ........................................................................................ 18
  1.3. Management of joint stock companies .................................................................................................................... 27
  1.4. Disclosure of information and transparency ........................................................................................................ 38
  1.5. Monitoring and auditing of financial and operational activities ........................................................................... 39
  1.6. Identifying areas of concern in the corporate governance practices .................................................................. 41

SECTION II. BANKS

SUMMARY OF SURVEY OF BANKS .................................................................................................................. 45
  1.1. Awareness and commitment to corporate governance .......................................................................................... 45
  1.2. Management bodies of a bank ................................................................................................................................. 45
  1.3. Disclosure of information and transparency of banks’ activities ....................................................................... 46
  1.4. Monitoring and auditing financial and operational activities ................................................................................. 47
  1.5. Compliance with the legislation of the Kyrgyz Republic in the field of corporate governance .......................... 47
  1.6. Identifying areas of concern in corporate governance practice .......................................................................... 47

CORPORATE GOVERNANCE PRACTICE IN KR BANKS ............................................................................ 48
  1.1. General information on banks ................................................................................................................................. 48
  1.2. Commitment to best practices in corporate governance ........................................................................................ 50
  1.3. Banks’ management bodies .................................................................................................................................... 53
  1.4. Disclosure of information and transparency ........................................................................................................ 61
  1.5. Monitoring and auditing of financial and operational activities ........................................................................... 61
  1.6. Identifying areas of concern in the corporate governance practices .................................................................. 62
The International Finance Corporation (IFC), a member of the World Bank Group, is the biggest global development institute focusing its activities on the private sector in developing and transition economies. The IFC creates opportunities for improving the quality of life and reducing poverty. It provides funding to companies thereby promoting the employment and expanding provision of basic services, mobilizes capital and provides advice to ensure sustainable development. During the period of global economic uncertainty, the amount of the IFC’s new investment in fiscal year 2010 has increased to a record US$ 18 billion in more than 500 projects in countries with developing and transition economies. IFC’s investment in Europe and Central Asia in fiscal year 2010 reached the peak US$ 3 billion in 105 projects thus providing necessary support to the region most affected by the global economic crisis.

The IFC Corporate Governance Project was launched in 2008 to assist joint stock companies (JSC) in the Kyrgyz Republic to improve their corporate governance, as well as to strengthen capacity of JSCs for attracting investment. This project is the result of a logical extension of the IFC Corporate Governance Program in Central Asia launched in Kazakhstan in 2006 and in Tajikistan in 2007.

The project aims to improve corporate governance practices in JSCs including banks. For this purpose, the project staff held seminars on a regular basis to share international best practices in corporate governance with joint stock companies and provide free individual consultations. The project is implementing a pilot program, which supports certain companies in developing and implementing recommendations to improve their corporate governance practices.

As part of the project, the project team works to involve in governmental working groups in legislative and enforcement reform in the area of corporate governance in the Kyrgyz Republic. In order to bring up future generation of business leaders, the project cooperates with HEIs to develop training programs and conduct guest lectures on corporate governance. To raise awareness of the population on issues relating to corporate governance, the project conducts the campaigns to inform the wider public of the latest trends in improving corporate governance practices.

The IFC Central Asia Corporate Governance Project is supported by the Netherlands-IFC Partnership Program.

The Netherlands is one of IFC’s key partners in delivering advisory services. The Netherlands-IFC Partnership Program (NIPP) was established in 2002 to consolidate Dutch-supported advisory programs under one umbrella. The NIPP was a Framework Agreement with a focus on private sector development, an emphasis on small business development, access to finance, the business and investment climate, and sustainable corporate practices. Globally, the Netherlands is one of the world’s largest donors, spending US$6 billion, which is equivalent to 0.8% of its GDP.
Good corporate governance is important both for companies planning to attract capital from external sources and for the Kyrgyz Republic in general striving to foster investment in the private sector. International experience has shown that a proper system of corporate governance helps not only to overcome the consequences of crises, but also to minimize their impact on companies.

To date, the Kyrgyz Republic is seeking to follow international principles for regulating corporate relationships in accordance with the international norms - Organization for Economic Cooperation and Development’s (“OECD”) Principles of Corporate Governance. The OECD Principles of Corporate Governance (the “OECD Principles”) have become the first international code of corporate governance standards approved by governments. Since 1999, the OECD Principles have been applied throughout the world as best practice in corporate governance.

As noted in the OECD Principles, “corporate governance is a key element for improving economic efficiency, which involves a set of relationships between a company’s management, its board of directors, its shareholders and other stakeholders. Corporate governance also provides the structure through which the objectives of the company are set, and the means of attaining those objectives and monitoring performance are determined.

Good corporate governance should provide proper incentives for the board and management to pursue objectives that are in the interests of the company and its shareholders and should facilitate effective monitoring, thereby encouraging company to a more efficient use of the resources”\(^1\)

Although the OECD Principles are intended for joint stock companies with publicly traded shares, these principles can also be useful for JSCs operating in the Kyrgyz Republic, the majority of which are not publicly traded. The regulated system of corporate relations in JSCs will help even these companies to develop more dynamically and attract investment for business development.

1.1. CORPORATE GOVERNANCE IN THE BANKING SECTOR OF THE KYRGYZ REPUBLIC

The banking sector in the Kyrgyz Republic is the most organized sector of country’s economy. Improvement of corporate governance is important both for the banks and for strengthening their influence on JSCs that are their borrowing clients. Banks will be able to pay closer attention to companies-borrowers when assessing their credit risk, while good corporate governance is one of the most effective ways to reduce risks. In assessing the creditworthiness of the borrower, banks will facilitate the improvement of corporate

\(^1\) OECD Principles of Corporate Governance, OECD, 1999
governance practices of the company-borrower.
There were 21 commercial banks operating on the territory of the Kyrgyz Republic as of beginning of 2009.

In early 2008, the Board of the National Bank of the Kyrgyz Republic (hereinafter - NBKR) approved the Regulations on Corporate Governance in Commercial Banks of the Kyrgyz Republic. This document was developed in accordance with the Law of the Kyrgyz Republic on the National Bank of the KR, articles of the Law № 59 of the Kyrgyz Republic on Banks of July 29, 1997 and Law № 60 Banking Activity in the Kyrgyz Republic of July 29, 1997, as well as normative legal acts of the NBKR. The above Regulations are mandatory for all commercial banks. As stated in the Regulations, “effective corporate governance in commercial banks is one of the most important conditions for stable development of individual banks and the banking system as a whole”.

The methodological basis for the effective corporate governance in banks and banking groups are the recommendations of the Basel Committee on Banking Supervision. The document developed by the Basel Committee on Banking Supervision “Strengthening Corporate Governance in Banking Institutions”, as well as the OECD Principles Governance were recommended to the banks of the Kyrgyz Republic.

1.2. BACKGROUND OF THE FORMATION OF CORPORATE GOVERNANCE IN THE KYRGYZ REPUBLIC

Corporate governance in the Kyrgyz Republic has a history of approximately two decades. It emerged in the Soviet Union with the adoption of the Law on Enterprises comprising the first norms that regulated legal corporate relations. In Kyrgyzstan, the first law of this type was the Law № 513 - XII of the Republic of Kyrgyzstan on Joint Stock Companies of the Republic of Kyrgyzstan of June 26, 1991. The Civil Code of the Kyrgyz Republic (hereinafter - KRCC), adopted in 1996, has provided new approaches to corporate governance and became a starting point for the formation of the legislative and regulatory framework governing legal corporate relationships in the country. The adoption of the CC resulted in the development of a new Law No 60 of the Kyrgyz Republic on Business Partnerships and Companies, which was adopted on November 15, 1996 and substituted the 1991 RK Law On Joint Stock Companies.

The current norms on corporate governance are provisions of the KRCC and the KR Law On Joint Stock Companies of March 27, 2003. It is important to note a number of special laws governing some areas of business activity and in one or another way dealing with corporate relations. These include the following laws of the Kyrgyz Republic: Law № 60 on Banks and Banking Activity of July 29, 1997, Law № 92 on Investment Funds of July 26, 1999, Law № 80 on Private Non-State Pension Funds in the Kyrgyz Republic of July 31, 2001 and Law № 96 on Organization of Insurance in the Kyrgyz Republic of July 23, 1998.

Despite the current regulatory framework it should be recognized that there are some contradictions both in the KR Law on Joint Stock Companies and between other related laws and, more importantly, between the law and current practices.

The current tendency is that many companies choose the form of “a limited liability company”, because they do not know about the advantages of “a joint stock company”. Based on the survey of corporate governance practice in the Kyrgyz Republic conducted
in 2008-2009, the majority of JSCs in the Kyrgyz Republic were formed as a result of the privatization process (except banks, for which the law originally prescribed the form of JSCs). The majority of JSCs created in such a way failed to adjust and change their management style. This is largely due to the fact that shares were distributed amongst employees of the company who did not understand the concept of share ownership. Consequently, many joint stock companies could not understand the importance of corporate governance, with the exception of joint stock companies which were created as such from the very beginning. Nevertheless, just a few companies really understand the importance of corporate governance. In practice, the corporate governance reforms are often superficial in nature and are used for PR purposes, rather than as a way to introduce structures and procedures that allow JSCs to gain shareholders’ trust, reduce the risk of financial crises and increase access to capital.

In 1994, the first Kyrgyz stock exchange (KSE) was founded in Kyrgyzstan. The first shares auction and its official opening took place in May 1995, when the process of privatization was actively underway in the country. Initially and until 2000, the KSE operated in the form of a non-profit membership organization with a total of 16 members. Corporatization of the KSE took place in 2000, and one of the largest shareholders and a reliable partner of the KSE was the Istanbul Stock Exchange, which still actively helps KSE to improve its activities today.

There are currently the following three stock exchanges in the republic: CJSC Kyrgyz Stock Exchange, JSC Central Asian Stock Exchange and CJSC Kyrgyzstani Stock Exchange – Exchange Trade System. More than 600 companies are listed on the three stock exchanges.
1.1. THE PURPOSE OF THE SURVEY
The purpose of this “Survey of the corporate governance practice in the Kyrgyz Republic” was to determine the level of corporate governance in JSCs of the Kyrgyz Republic and identify problems faced by companies at this stage of economic development. The findings of the survey were obtained through interviews with the companies’ management, Boards of Directors and Corporate Secretaries. The obtained data were further analyzed against norms of the national legislation and corporate governance practices. In particular, the survey has covered the following:

- the current corporate governance practices in joint stock companies, including banks (financial and credit institutions);
- the compliance by the JSCs, including banks (financial and credit institutions) with the Kyrgyz legislation on corporate governance;
- the compliance by JSCs, including banks (financial and credit institutions) with the best international practices in corporate governance;
- identifying problems in corporate governance of JSCs, including banks (financial and credit institutions).

1.2. METHODOLOGY
90 out of the originally selected 184 JSCs, and 5 banks out of the original sample of 12 banks were surveyed. JSCs and banks provided information by answering questions in the questionnaire. Individual interviews with representatives of each of the JSCs and banks were additionally conducted.

The survey included four phases: I phase – sampling; II phase – survey in real (field) conditions; III phase – conducting the survey; and IV phase – final data processing (summarizing) and analysis of the results.

The survey was conducted in the form of personal meetings with senior management staff of the selected JSCs and commercial banks (credit associations). Each respondent spent at least one hour completing the questionnaires. The survey team has made every effort to ensure that the respondents provided complete answers to all questions in questionnaires.

Two types of the response – “yes” or “no” were proposed to the respondents in questionnaires, however, some adjustments were made based on additional information provided during the interview.

Unfortunately, not all JSCs and banks agreed to participate in the survey, answer the questions and share their views regarding the development of corporate governance in the Kyrgyz Republic. The IFC Corporate Governance Project would like to thank to all companies which participated in this survey.
In addition, the IFC Corporate Governance Project would like to express special thanks to Mr. A. B. Alymkulov, President of the CJSC Central Asia Stock Exchange, Mr. B. Takenov, Head of the Department for Securities Market Development, representatives of the State Service for Regulation and Oversight of the Financial Market of the Kyrgyz Republic for their recommendations in preparing this survey, and to the CAIConsulting survey team for drafting the report based on the survey, as well as to the whole team of the IFC Corporate Governance Project in Central Asia and Azerbaijan for their valuable comments and support.

1.3. TIMEFRAME
The survey was conducted by the CAIConsulting survey team. The survey has started in October 2008. JSCs and banks received questionnaires during the interview in October – December and the completed questionnaires were received in March 2009.

1.4. SURVEY COVERAGE
A total of 90 out of the originally sampled 184 JSCs took part in the survey and completed the questionnaires. The survey covered JSCs from Bishkek and Osh as well as Chui, Issyk-Kul and Jalal-Abad Oblasts. All respondents from the banking sector were registered and had head offices of the banks located in Bishkek.

<table>
<thead>
<tr>
<th>No</th>
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<th>Joint stock companies</th>
<th>Banks</th>
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<td>2</td>
<td>Osh city (south)</td>
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<tr>
<td>3</td>
<td>Chui Oblast (north)</td>
<td>23</td>
<td></td>
<td>23</td>
</tr>
<tr>
<td>4</td>
<td>Issyk-Kul Oblast</td>
<td>3</td>
<td></td>
<td>3</td>
</tr>
<tr>
<td>5</td>
<td>Jalal-Abad Oblast (south)</td>
<td>10</td>
<td></td>
<td>10</td>
</tr>
<tr>
<td></td>
<td><strong>Total</strong></td>
<td><strong>90</strong></td>
<td>5</td>
<td><strong>95</strong></td>
</tr>
</tbody>
</table>

At the time of sampling, JSCs participating in the survey had the following characteristic features: (a) the share of state and foreign ownership was either 0 or less than 50%; (b) at the time of the survey all companies were operating; and (c) JSCs with at least 25 employees.

In most cases, questionnaires were completed by senior management staff of JSCs, for example, by heads of the executive bodies (in 49 companies out of 90) and members of the executive bodies (in 9 cases), as well as by individuals acting as companies' secretaries (Corporate Secretaries) (in 11 companies). In some cases, questionnaires were filled in by Chairpersons (13) or other members (5) of the Boards of Directors.
In 5 banks, heads of the executive bodies were interviewed, while questionnaires were filled in by companies’ secretaries and lawyers.

JSCs including banks that refused to participate in the survey stated confidentiality, insignificance of the survey or lack of interest as the main reasons for their refusal.

In order to show the most realistic current situation in JSCs and reflect the actual level of corporate governance in JSCs of the Kyrgyz Republic, the survey team used several types of analysis. The data are indicated in percentage terms, followed by an explanation from which figures the above percentage were calculated. In a number of questions, the respondents were offered to choose from several answers in the questionnaire. Such responses are not reflected in percentage, and the number of responses received on each point is provided instead.
1.1. AWARENESS OF AND COMMITMENT TO INTERNATIONAL PRACTICE IN CORPORATE GOVERNANCE

- JSCs are poorly aware of the OECD Principles. The surveyed JSCs demonstrated poor awareness of the corporate governance principles (21% or 19 companies out of 100 heard about the recommendations of the OECD). With regards to corporate governance, the surveyed JSCs are governed by the norms of the current legislation.

- The management of JSCs is largely represented by one person. The majority of companies have a one-person, rather than a collegial executive body (61% or 52 out of 85 JSCs, who responded to this question).

- Position of Corporate Secretary is widely used by JSCs. 86% (or 77 out of 90) of JSCs have a Corporate Secretary or other officer responsible for corporate governance. However, only 28 out of 77 JSCs have a full-time Corporate Secretary. In most cases the Corporate Secretary is working part-time in order to combine other functions in the company (34 companies).

- Internal documents defining the status and rights of the Corporate Secretary and governing his/her activities are in place in 67% (or 48 out of 72 JSCs). 4% (3 out of 72) of JSCs are planning to adopt such internal documents. The remaining 29% (or 21 out of 72 companies) do not plan to adopt internal documents regulating the activities of a Corporate Secretary.

- The corporate governance principles in JSCs are not properly formalized. Out of 63 JSCs that have responded to this question, the Code of Corporate Governance as a single document providing the principles of corporate governance in JSCs and regulating all major activities of the JSCs is adopted in only 3 companies (5%). 78% (or 49 out of 63) of the surveyed joint stock companies do not see the need for adoption of such internal documents and do not plan their adoption in future.

- There is an unbalanced approach to improving the corporate governance practices. JSCs focus their efforts on improving the practice of information disclosure as the most developed part of the legislative requirements (i.e. the introduction of International Financial Reporting Standards (IFRS)), while improving organizational management structures and procedures for interaction between the management are paid little attention, as there are no any strict legislative requirements in this area of relations.

- The JSCs assess the level of corporate governance in their companies as satisfactory. This was stated by 80% (or 61 out of 76 companies) of JSCs that responded to this question. As factors preventing the improvement of the corporate governance system, companies more often mentioned the lack of qualified professionals (37 companies) and lack of knowledge (33 companies). 29 JSCs believe that there is a need to revise the legislation of the Kyrgyz Republic in the field of corporate governance. Only 45% of JSCs (or 40 companies out of 89) received advisory services on corporate governance from external consultants.
1.2. MANAGEMENT OF JOINT STOCK COMPANIES: GENERAL MEETINGS OF SHAREHOLDERS, BOARD OF DIRECTORS AND EXECUTIVE BODY

General Meeting of Shareholders
- In all of the surveyed joint stock companies the annual general meetings of shareholders are held within the timeframe established by the legislation.
- Procedures for notifying shareholders. In 89% of cases (80 companies out of 90) notify their shareholders through the mass media, i.e. shareholders are informed of the general meeting using the sources stipulated by the legislation.
- Practically all JSCs (97%) inform shareholders of the agenda of the general meeting of shareholders; however the accompanying documentation to the agenda are provided by 16% of the respondents and explanatory notes – only by 18% of joint stock companies.
- 100% of JSCs provide shareholders with the outcomes of the annual general meetings of shareholders directly at the meeting. 3% of companies stated that they did not inform on the decisions of general meetings only those, who did not attend the general meeting of shareholders.
- A common practice is voting by proxy, i.e. via representatives. This practice is common in 76% of joint stock companies.
- In 75% of companies, the quorum at the general meetings of shareholders is more than 75% of shareholder votes, which might indicate either of: 1) high activity of shareholders, or 2) high concentration of shares with a small group of shareholders.
- The majority (77%) of general meetings of shareholders last for 1 to 4 hours, which indicates either of: 1) a properly prepared agenda and excellent organization of the meeting, or 2) that the decisions are actually known in advance due to high concentration of shares with a limited number of shareholders.
- More than half of JSCs (52) inform the public about the outcomes of the general meetings. For this purpose JSCs commonly use the mass media (49 companies) or their branches, representative offices and subsidiaries (2 companies). 40 joint stock companies do not inform the public about the outcomes of their general meetings.

Extraordinary General Meeting of Shareholders
- 39% of JSCs held extraordinary general meetings over the past two years. The reasons for holding extraordinary meetings are different; however the three most common reasons are as follows: approval of major transactions – 16 cases, changing the charter – 15 cases and re-election of members of the Board of Directors – 9 cases.
- Most often the extraordinary general meetings are initiated by either the Board of Directors (in 17 cases) or executive body (13) (in cases when a JSC does not have a Board of Directors). In 6 cases extraordinary general meetings were initiated at the request of a large shareholder, which was normally caused by the change of the owner and therefore the need to change composition of the Board of Directors, as well as to make some changes to the authorities of companies’ management.

Board of Directors
- In most joint stock companies functions of the Boards of Directors are to regulate the activities of the executive body. The Board of Directors is authorized to select, appoint and dismiss the head of the executive body and its members (55 and 51, respectively), as well as to determine the amount of their remuneration (54). Boards of Directors are involved in drafting companies’ development strategies only in half of the surveyed companies (51%).
• Only 29% of companies apply the practice of membership of independent directors, however, this data is questionable since there is no understanding of the ‘independence’ criteria. Some respondents, for example, reported that three out of three board members are employees of the JSC and at the same time they are independent directors as well.

• Only two companies have committees: one has the Committee on Corporate Governance and Audit Committee, and the other one has the Committee on Appointments and Remuneration and the Committee on Ethics. Only one JSC intends to establish committees in future.

• In general, the authority of the Board of Directors and executive body in JSCs is distributed in compliance with the legislative norms. As stated by the respondents, the authority of the Board of Directors in 55 JSCs include the election/appointment and dismissal of heads of executive bodies; in 54 companies – approval of remuneration for heads and members of the executive body. The respondents from 51 JSCs stated that appointment and dismissal of members of the executive body was the competence of the Board of Directors as well and 46 believe that the key directions of companies’ activity should be determined by the Board of Directors.

• The work of the Board of Directors is rather formal. 69% of JSCs have internal documents regulating the work of Boards of Directors. In 60% of companies members of the Board of Directors receive the materials for the meeting several days to two weeks in advance. Only in 9% of JSCs, members of the Board of Directors receive the materials during the meeting. In most cases members of the Board of Directors are provided with the agenda – in 74% of companies, financial statements – in 59% of companies and draft decisions subject to approval – in 48% of companies. The Annual Report is considered by the Board of Directors only in 1 company.

• In the majority of JSCs (38%) the Board of Directors meets at least once a quarter, this is absolutely in line with the legislation. In 12% of companies the Board of Directors meets even more often than as prescribed by the law. Only in 22% of the surveyed JSCs the Board of Directors meets less frequently than prescribed by the law.

• Usually (in 18 cases) members of the Board of Directors receive a fixed monthly remuneration, while only in 2 cases the amount of their remuneration depends on attending the meetings. In 14 companies, remuneration of members of the Board of Directors depends on income gained by the company, while in 11 companies it is established based on the performance.

**Executive Body**

• *In most cases executive bodies are in JSCs represented by one person (58%).* In cases where there is a collegial executive body (37%), the main person having practically a sole control is Chairperson of the company’s Board. 5% of JSCs did not answer the question.

• The executive body is predominantly formed by the Boards of Directors. Thus, in 51 JSCs, the appointment and dismissal of members of the executive body is within the competence of the Board of Directors, as well as the appointment and dismissal of the head of the executive body (in 55 JSCs). The above issues are within the competence of the general meeting of shareholders in 14 and 21 companies, respectively. In 8 cases the respondents stated that the executive body appointed its members, while one respondent stated that the head of the executive body has appointed himself. The executive body is elected by the general meeting in cases where the JSC does not have a Board of Directors. In some cases, although the company has the Board of Directors,
the executive body is formed by the general meeting of shareholders. This indicates that some joint stock companies apply the norms of the previous legislation, which were in force before the adoption of the KR Law On Joint Stock Companies.
The survey results indicate that in the majority of JSCs (59), the functions of the executive body are limited to approval of internal documents regulating the activities non-management bodies, while in 55 cases the respondents stated that functions of the executive body is to represent the JSC.
- Only in 36% of companies the executive body reports to the Board of Directors in writing.

1.3. Disclosure of Information and Transparency of Companies’ Activities

Financial reporting in compliance with IFRS
- *The process of transition to International Financial Reporting Standards (“IFRS”) in accordance with the requirements of the KR Law on Accounting.* 74% of companies stated that they have already switched to preparing financial statements in accordance with IFRS.

Disclosure of information
- In most cases JSCs prefer to disclose only information which must be disclosed by JSCs in accordance with legislation. For example, 49 companies publish their profit and loss accounts; annual reports are published by 47 companies; and balance sheets – by 43 JSCs. The JSCs that do not disclose information stated different reasons for non-disclosure. 22 JSCs responded that they have no need to disclose the information; other companies (11) do not disclose information as there are no legal requirements to do so.
A set of annual reports being presented to shareholders at the general meetings is similar in many companies. For 77 companies these include the audit report, as well as the report on financial activity (68). 50 JSCs provide shareholders with the information on companies’ goals and strategies. 48 companies inform their shareholders on external auditor’s report, dividend policy related issues and ownership structure.
The Board of Directors reports to shareholders at the general meeting in 44% of the surveyed companies. 39% of companies disclose to shareholders the information on the amount of remuneration.
- *Minimal dissemination of information on the corporate governance principles.* Only 8% of joint stock companies inform their shareholders about corporate governance principles and policies.
- 73% of JSCs responded that the transactions with affiliated persons shall be approved by various management bodies. In 45 companies, transactions with affiliated persons are approved by the general meeting of shareholders; in 37 JSCs such transactions are approved by the Board of Directors; and in 11 companies – by the executive body. However, 11% of JSCs believe that the approval of transactions with affiliated persons is not required and 17% never made such transactions.
1.4. MONITORING AND AUDITING OF FINANCIAL AND OPERATIONAL ACTIVITIES

External control system
• External audits are carried out in 76% (68) of JSCs. In 96% of the total number of companies, which have responded to this question, the audit was conducted by local audit company or individual auditor. Only 4% use services of international auditors.
• 21% of JSCs mentioned that they have had negative experience of cooperation with external auditors. Over the past three years external auditors have been changed in 19 companies. However, in 8 cases this was due to prices for the auditors’ services, while in other 5 cases the respondents were dissatisfied with the quality of services provided by the external auditors and in 3 cases this was due to a conflict of interest.

Internal control system
• There is a lack of understanding of the nature of internal audit. 47% of companies do not have an internal audit service. 34% of companies responded that they have established the internal audit service, however 23% of them confused the internal audit with the revision commission. In addition, many respondents perceive the internal audit as a controlling and advisory body.

It should be noted that in most cases (in 17 out of 31 companies that responded to this question) assignments for the internal auditors are given either by the Board of Directors or by the executive body or its head (9 cases).

1.5. COMPLIANCE WITH THE KYRGYZ REPUBLIC LEGISLATION ON CORPORATE GOVERNANCE

Companies’ compliance with the current legislation
• The JSCs poorly understand the requirements of the legislation related to corporate governance, with resulting violation of the legislative norms. 10% of companies stated that issuance of shares is within the competence of the Board of Directors, and 3% stated even that it is within competence of the executive body, while this issue falls within the exclusive competence of the general meeting of shareholders.
• Transactions with affiliated persons do not need any approval in 11% of companies. 10% of companies do not have the internal documents regulating general meetings of shareholders; 17% of companies do not have the internal rules regulating the activities of the Board of Directors. The requirements of the legislation regarding the internal documents regulating corporate relations are violated as there is no need for such documents, as well as due to the lack of responsibility in the legislation for non-compliance with the above norms.
• Many provisions of the legislation on JSCs are outdated and cannot fully regulate the relationships that are the subject of regulation. For the management structure of JSCs and in accordance with the norms of the current KR Law On Joint Stock Companies, a Revision Commission shall be established. The practical use of such a body is minimal, as the revisions do not help to prevent possible problems, but only ascertain the accomplished facts. This is the reason why JSCs in practice fulfill these standards only formally.

Protecting shareholders’ rights to dividends
• Timely payment of dividends is typical for joint stock companies. The dividend policy of companies is dictated by law prescribing a mandatory distribution of net profit regardless of its amount. The law requires that 25% of companies’ net profit be paid out
as dividends. Over the past three years only 21% of companies did not pay dividends for the last one, two or three years.

- In practice there are situations where JSCs’ costs associated with payment of dividends several times exceed the amount of the dividends being paid.
- Analysis of the responses shows that issues related to shareholders’ rights are better discussed compared to other aspects of corporate governance. Presumably, this was the result of the fact that shareholders’ rights are more strictly regulated by the legislation and the majority of companies have, as a rule, a small number of influential owners.

1.6. IDENTIFYING AREAS OF CONCERN IN THE CORPORATE GOVERNANCE PRACTICES

- The regulatory framework governing corporate governance was assessed as satisfactory and above by 50% of respondents, 23% of respondents consider it as unsatisfactory, and 27% of respondents were unable to assess it.
- With regard to effectiveness of the current legislation in respect of various procedures, JSCs assessed the procedure on general meeting of shareholders as the most effective, with 83% recognizing it as positive. Also, a significant number of respondents highly assessed both the procedure of convening shareholders to attend the general meeting and the procedure of forming the Board of Directors’ activity - 76% and 70%, respectively. The procedure relating to the protection of shareholders’ rights was recognized by the respondents as properly developed at the legislative level and it was positively assessed by 50% of companies.
- There is a low level of companies’ awareness of some procedures. More than half of the surveyed joint stock companies (54%) were unable to assess the procedure of forming committees of the Board of Directors and 33% of companies were poorly informed about the issuance of securities.
- A high percentage of respondents, namely 39%, do not know the mechanisms for settlement of corporate conflicts. During the interviewing, some respondents made statements about raider attempts, conflicts with minority shareholders, pressure by major shareholders, attempts to give direct instructions to executive management avoiding the established procedures, as well as the corruption of the judiciary bodies.
A significant problem of the current legal regulation of corporate relations in the Kyrgyz Republic is inconsistency of certain norms prescribed in various legislative acts and contradictions that result in conflict when applying these norms.

The current KR Law On Joint Stock Companies is in many respects contradictory. The norms are not aligned and there are numerous inaccuracies. The law enforcement practice has revealed many weaknesses in the current legislation. We will further focus on specific issues and problems in details.

1.1. GENERAL INFORMATION ON JOINT STOCK COMPANIES

Acquiring a status of a joint stock company
Organizational forms of companies such as joint stock company appeared in the Kyrgyz Republic in 1991 with the adoption of the KR Law on Joint Stock Companies. Privatization was the main impulse for the formation of JSCs. This fact is illustrated in Figure 2. 86% of surveyed companies were transformed into JSCs as a result of privatization. And only 9% of companies were originally registered as JSCs. 5% of companies that were transformed into JSCs had originally different legal forms.

![Figure 2. Methods of acquiring the status of a JSC](image)

**Total number of employees in a company**
In terms of the number of employees, most companies have between 51 and 100 employees. This situation characterizes the level of companies’ economic development in the country.

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2 This section does not include banking (financial and credit) institutions.
In terms of the number of shareholders, there is a tendency to a sharp reduction in their number. At the time of privatization of state-owned companies, almost all workers became shareholders, while another part of shareholders of companies came as a result of the mass coupon privatization, when 25% of shares were sold through auctions. 10% of companies have more than 500 shareholders, and therefore they fall under a more strict regulation and are obliged to disclose information in the print media and submit the reports to the oversight body for securities market.

The responses regarding the ownership structure of the company were sufficiently informative. In addition, the respondents referred either to a lack of understanding or direct prohibition by shareholders, or confidentiality of the information on companies’ owners.
Major shareholders
The respondents could not give clear answers to the question regarding the number of shareholders and shares held by them, therefore, the provided responses make it impossible to assess them objectively. Some respondents noted that there are 2 to 10 shareholders in the company owning more than 66.7% of shares.

The respondents noted that in most cases major shareholders are members of the Board of Directors and executive body.

The degree of affiliation of major or controlling shareholders with each other
In terms of degree of affiliation of major or controlling shareholders of the company with each other, in most cases the respondents noted their kinship relationships, however, the majority noted that there was not any affiliation. This is explained by the fact that JSCs often do not attach importance to this issue and/or do not track cases of affiliation in their companies, because in practice the degree of affiliation in companies is quite high.

1.2. COMMITMENT TO BEST PRACTICES IN CORPORATE GOVERNANCE

Corporate governance principles
The respondents were asked about their awareness of the OECD Principles of Corporate Governance, their attitude towards corporate governance in general and their willingness to take steps to improve corporate governance practices in their company in particular.

Based on findings of the survey, the majority of JSCs (79%) are not aware of the OECD Principles. The companies apply the definitions of corporate governance, which are set out in the legislation and build the relationships in line with the prescribed norms.

The results of this survey enabled to us understand the goals sought by the JSCs with regard to corporate governance. Each respondent could select up to three responses.

Figure 5. The number of affiliated persons in companies (people)

| No affiliated parties | 71 |
| Family               | 14 |
| Partners in other business activity | 4 |
| Other               | 3 |
Among the priority goals of improving corporate governance practices, the JSCs most frequently included the following: increasing the investment attractiveness of the company and improving the decision-making process (28 responses on each statement) and improving company’s reputation (26 responses). Striving to improve the transparency of activities of the Board of Directors and executive body are the priority for 9 JSCs. Only 4 JSCs cited prevention and settlement of corporate conflicts.

**Figure 6. Priority goals for improving corporate governance practices**

- Improving investment attractiveness of the company: 28 responses
- Improving the decision-making process: 28 responses
- Improving company’s reputation: 26 responses
- Protection of shareholders’ rights: 24 responses
- Ensuring the compliance with the legislation: 19 responses
- Reducing business risks: 19 responses
- Ensuring free access to the capital markets in the KR: 17 responses
- Improving operational performance: 14 responses
- Reducing cost of loan capital and investment: 14 responses
- No response: 10 responses
- Improving transparency of activities of the BD executive bodies: 9 responses
- Establishing effective relations between shareholders and the Board of Directors: 8 responses
- Protection of stakeholders’ rights: 4 responses
- Prevention of corporate conflicts: 4 responses
- More effective disclosure of information: 2 responses

In terms of adherence to generally accepted principles/codes of corporate governance, which is expressed in the presence of certain internal documents in the company, the situation is as follows:

A Code of Corporate Governance was adopted only by 3 companies. 11 JSCs are planning to adopt such a document in the near future and 49 companies would not adopt a code of corporate governance for settlement of corporate issues in their JSCs.

Figures 7–9 show that the majority of companies have some internal regulations governing certain aspects of corporate governance. As a rule, they include those documents that are prescribed by the legislation and regulatory bodies (e.g., the Charter or the Regulations of the Revision Commission). Other internal documents describing the corporate governance, such as Code of Ethics and Corporate Code are rarely used. For example, the internal documents
on disclosure of information are in place in 27 companies, and the Code of Ethics – in 14 companies.
Most companies stated that they realize the importance of corporate governance, however, only a few of them have a person or committee responsible for implementing corporate governance throughout the organization. Only one JSC has a committee on corporate governance in the Board of Directors and 6 JSCs have a special document on corporate governance.

86% of companies have a Corporate Secretary. In 34 JSCs the Corporate Secretary works on part-time basis and combines his/her functions with other responsibilities in the company. 28 JSCs have a full-time Corporate Secretary.
The usual functions of the Corporate Secretary in the surveyed companies are far from the best international practices and in many ways are similar to the functions of an ordinary Secretary-Assistant.

**Using services of external consultants**

Despite the adherence of JSCs to the corporate governance principles, only 45% of companies used paid consultations of professional organizations specializing in providing services on corporate relations.

More often the JSCs used services on preparation and holding of general meetings of shareholders (27 cases). This is due to the requirement in the legislation on mandatory participation of representatives of an independent registrar in the general meeting of shareholders. In addition to registrar’s representative participation in the meeting, many JSCs entrust him/her with some issues related to preparations for the meetings. 19 companies use services of external consultants on the development and bringing the internal documents in compliance with the current legislation. For this purpose, they often use services of the registrars. 12 JSCs used registrar’s services in preparing the annual reports. Issuance of securities (shares and bonds) (9 responses) and development of a financial and management strategies (7 responses), as well as assistance in attracting investment (6 responses) are subject of activities of professional securities market participants engaged in the brokering functions and providing underwriting services to JSCs.

**Factors hindering the improvement of corporate governance in JSCs**

Regarding the factors hindering the improvement of the corporate governance practices, most JSCs responded that this was due to the lack of qualified specialists (37 JSCs) and lack of information/knowledge (33 JSCs). Deficiencies in the legislation on corporate governance were mentioned by 29 JSCs. 12 companies responded that increased transparency might increase the risk (the risk of bankruptcy, merger, etc.) and the same number of JSCs believe that the cost of improvement of corporate governance will not generate any profit.
The level of corporate governance in companies and in the country as a whole

61 JSCs out of 76 that responded to this question, or 68% of the total number of the surveyed JSCs, assessed the level of corporate governance in their companies at a 5-point scale. The majority of JSCs (34 responses) assessed the level of corporate governance as satisfactory, 22 JSCs assessed it as good and 5 companies consider it excellent. 15 JSCs recognized that the level of corporate governance in their companies was unsatisfactory, while 14 companies could not answer this question.

At the same time regarding the level of corporate governance in the country as a whole, 37 companies or 41% failed to answer this question, while 28% reported it as unsatisfactory.
Protecting shareholders’ rights
Protecting the rights of shareholders is the goal of corporate governance in 24 JSCs. JSCs do not consider it important to protect stakeholders’ rights, as only 4 companies strive to protect their rights in their activities. Settlement and prevention of corporate conflicts did not raise any interest either (only 4 companies gave positive answers) as the respondents believe that the norms of the legislation on corporate governance make it impossible to avoid such conflicts.

Transactions with affiliated parties
A number of questions during the survey were aimed to identify knowledge of the legislation on certain aspects of corporate relations in companies. Different answers were received regarding the transactions with affiliated persons. Most joint stock companies (72%) responded that there was the need to settle this issue. 17% of JSCs have never had or heard about this kind of transactions, and only 11% of JSCs believe that such transactions need no any approval. The responses suggest that this issue is largely resolved in accordance with applicable regulations of the KR.
In most cases the management bodies of JSCs authorized to approve transactions with the affiliated parties are the general meetings of shareholders (as responded by 45 companies), followed by the Board of Directors (37 companies) and in 11 companies such transactions are approved by the executive body.

**Kinship relations between the controlling shareholders and the management**

The following responses were received in answer to the question whether family members/relatives of existing controlling shareholders are members of the company’s Board of Directors and/or executive body:
There are even less cases when family members/relatives of the controlling shareholders are in the JSC's executive body.

**The presence of an independent registrar**
In 97% of companies, the register of shareholders is maintained by an independent Registrar, as in accordance with the requirements of the legislation the register of all open joint stock companies shall be maintained by an independent Registrar. The exception is for closed companies that can maintain the register themselves.

**Attracting investments**
The vast majority of companies (90%) did not attract external investment over the past 5 years.

The majority of companies attracted external funds in the form of loans – 7 companies. During the survey there was only one case of investment in capital.

Nevertheless, according to the survey, 57% of companies plan to attract investment over the next five years. At the same time, 16 companies responded that they would attract direct foreign investment. Many companies gave more than one response, which suggests that companies are planning to attract investment from various sources.

Out of 43% of companies (39 responses) that do not plan to attract external investment, 9 expressed concern that the investment conditions would be unfavorable for them, while 13 companies are not planning to expand their activities.
1.3. MANAGEMENT OF JOINT STOCK COMPANIES

General Meeting of Shareholders (GMS)
All of the surveyed JSCs hold annual general meetings of shareholders within the period stipulated by the legislation and often hold such meetings at their place of registration.

Notification of Shareholders Meeting
Most companies (59) notify their shareholders within 20 days before the upcoming meeting as established by the current legislation. Only 33% (30) of the surveyed JSCs do not comply with terms of notification of their shareholders.

Open JSCs are obliged to advertise in the mass media and send notification of the general meeting directly to shareholders. 89% of companies comply with this requirement. Shareholders of closed joint stock companies are notified of the general shareholders’ meeting by sending them a written notice.
Materials to the shareholders’ meeting

The Kyrgyz legislation for JSCs in the non-banking sector requires that JSCs provide shareholders with the agenda of the meeting. 97% of joint stock companies act in compliance with this legal requirement. As for all other materials of the upcoming meeting, JSCs may provide such materials during the meeting. Some companies (27) additionally send the instructions to shareholders for voting by proxy at the general meeting of shareholders. 24 JSCs normally send to shareholders the annual report as well. In addition to the agenda, 22 companies also send the financial reports to their shareholders.

Outcomes of the general meeting of shareholders

All JSCs announce the adopted decisions directly at the meeting. This is due to the fact that some issues on the agenda cannot be discussed without adopting the above decisions. With respect to the response of 3% of respondents who stated that shareholders are not informed about the results of the meeting, it is likely that they do not inform those shareholders who did not attend the meeting.
Voting by proxy
Voting by proxy is common for JSCs. 76% of companies responded that such cases are quite common.

Quorum and duration of the general meetings of shareholders
The general meeting of shareholders is eligible (has a quorum) if at the end of registration for the general meeting, shareholders (their representatives) who collectively have more than 60% of outstanding voting shares were registered. If the meeting is not held, the new general meeting of shareholders convened instead of the failed one shall be eligible, if at the end of registration, shareholders (their representatives) having in aggregate at least 40% of the outstanding voting shares of the company were registered. In this case, the charter of a company with the number of shareholders exceeding 10,000 can provide for a smaller quorum for holding a general meeting of shareholders instead of the failed one, but at least 30% of the outstanding voting shares of the company.

The survey showed that in most JSCs (75%) quorum at the general meetings exceeds the 75% threshold, which may indicate either of a high sense of responsibility and interest of shareholders or a high concentration of shares with a small group of shareholders. Nevertheless, some companies had quorums up to 65%. This means that not all questions could be addressed at such meetings, as, for example, introduction of changes to the charter requires a quorum of two thirds of those shareholders, who may decide to change the charter. One respondent stated that the quorum was less than 50%, i.e. the annual general meeting either did not take place, or there was a repeated meeting, where a quorum was limited to 40% of the votes.
A typical indicator is the amount of time required for conducting a general meeting of shareholders. In most cases (77% or in 69 companies) the meetings last one to four hours, while in 17 cases meetings of shareholders last even less than one hour. This indicates an appropriate preparation and holding the meeting or, more likely, is a consequence of concentration of controlling shares with a limited number of persons represented in the Board of Directors or executive body, who virtually take decisions before holding the meeting, and just formalize the decisions during the meeting.

**Information on outcomes of the general meeting of shareholders**

In accordance with the legislation of the Kyrgyz Republic, JSCs either with more than 500 shareholders or publicly trading at least 1 issue of securities shall publish their financial statements within two months after the annual meeting of shareholders, but no later than July 1 following the reporting year.

The JSC may decide to publish in the print mass media summarized financial statements consisting of a balance sheet as of December 31 of the reporting year, the profit and loss account and auditor’s report on the summarized financial statements prepared in accordance with the requirements of the International Auditing Standard.

Such companies shall publish their annual financial reports after assurance of reliability of the provided information (its compliance with IFRS) by individual independent auditors and (or) audit organization and approval of the annual balance sheet and profit and loss account by the annual general meeting of shareholders. The auditor’s report shall be included in the financial statements being published.

Most of the surveyed companies are not required to publish their financial reports and they are not obliged to inform the public about the outcomes of the general meeting of shareholders. Nevertheless, more than half of the surveyed companies (57%) publish outcomes of the latest meeting and decisions in the print mass media.

**Extraordinary general meeting of shareholders**

In the past two years, 39% of companies held extraordinary general meetings of shareholders for various reasons. The reasons for convening extraordinary meetings are different the three most common reasons are as follows: approval of major transactions – 16 cases, changing the charter – 15 cases and re-election of members of the Board of Directors – 9 cases.
Initiators of an extraordinary general meeting of shareholders

In most cases extraordinary meetings are initiated by the Board of Directors (17) or the executive body (13). In 6 cases it was the requirement of major shareholders.

1.3.2. BOARD OF DIRECTORS

The Board of Directors is a body responsible for the development of strategic directions of company’s activity. It determines the style of work and approves the system of relations to be followed by him/her, JSC’s management and staff. It establishes and ensures the limits of responsibility and accountability throughout the organization. This is the requirement of the legislation on corporate governance. In more than half of cases (51%) it is the Board of Directors that determines JSC’s development strategy.

Below are some quantitative and qualitative characteristics of the Boards of Directors.

In most companies there are not any formal contracts with the Chairperson (48 responses) and members of the Board of Directors (45). In 7 cases there is a civil law contract with the Chairperson of the Board of Directors, and in 15 cases – an employment contract. A similar situation is with members of the Board of Directors (4 and 11 responses respectively).
In the course of the survey it was difficult to determine the number of companies’ independent directors and members in the Boards of Directors. 29% of JSCs stated that they had independent directors in the Board of Directors. However, some respondents stated, for example, that out of three members of the Boards of Directors, three were company’s employees and at the same time independent directors. It means that in reality there are just a few independent directors.

Some Boards of Directors are fully composed of company’s employees while in others vice versa – only of shareholders, who are not company’s employees. Just a few of the interviewed respondents could clearly formulate the concept of an independent director.

According to the survey, only two companies have formed the committees in the Board of Directors: in one company this was the Audit committee and Corporate Governance Committee, in the other one – the Ethics Committee and the Committee on Appointments and Remuneration. One more company intends to establish a Committee on Appointments and Remuneration under the Board of Directors.

**Meetings of the Board of Directors**

78 responses were received in answer to the question regarding frequency of meetings of the Board of Directors. Of these, 34 respondents stated the frequency of meetings complied with the legal requirement – at least once a quarter. In 11 companies the Board of Directors meets even more often than is required by law. In 20 companies the Boards of Directors violates the legal requirement and meets less times than required by legislation.
It is also important to analyze the responses to questions regarding how far in advance of the meetings members of the Board of Directors receive notification and what thematic and other materials are provided for their consideration at the meeting. 76 responses were received in answer to question regarding the timing of the notification.

As shown in Figure 31, in most companies (37%) members of the Board of Directors receive notification of the meeting up to one week prior to the event; in 12% of JSCs members receive notifications more than two weeks in advance; in 8% of joint stock companies – one to two weeks in advance; in 14% – one day in advance, and in 13% of the surveyed JSCs – on the day of the meeting. Only 16% of JSCs do not have an established practice for this procedure. Thus, in most JSCs members of the Board of Directors are informed about the meeting in advance.

The largest number (67) of JSCs that responded to this question, provide members of the Board of Directors with the agenda of the meeting, followed by JSCs (57) that attach company’s financial reports to the agenda. Some companies even provide members of the Board of Directors with draft decisions to be approved (43) and explanations for each item on the agenda (33).
Remuneration for members of the Board of Directors

In answer to the question regarding incentives to encourage the Board of Directors, the surveyed JSCs use various incentives. The most frequent response (18) was that members of the Board of Directors receive a fixed monthly remuneration, while only in 2 cases their remuneration depends on the attendance of meetings. In 14 JSCs remuneration of members of the Board of Directors depends on company’s performance, while 11 JSCs set the amount of remuneration based on the performance results. It should be noted that companies may apply a few material incentives to encourage members of the Board of Directors (see Figure 33).

1.3.3. EXECUTIVE BODY (EB)

The vast majority (58% of the surveyed JSCs) have a single-person executive body represented by the Director (Director General). In some JSCs, even if it has a collective executive body, in practice the powers of the head of such body are rather broad and do not depend on collective decisions.

Encouraging the activity of the executive body

The majority of members of the Executive Body (40 responses) receive a monthly fixed remuneration, however other incentives are also applied, such as interest payments from company’s income (12), or depending on performance of the head himself (9). Sometimes shareholders encourage members of the executive body by including them in the list of company’s owners through targeted sales of shares to them (8).
Accountability of the executive body

The question regarding accountability of the executive body to the Board of Directors related only to the collective executive bodies, therefore answers were that in general the executive body reports at the meetings of the Board of Directors. In most JSCs (26 responses) the executive body reports at the meetings of the Board of Directors on a quarterly basis. Normally, such reports are submitted in writing (18 responses).

In 16 JSCs that responded to this question, the executive body reports to the Board of Directors once a week or once a month, which indicates either of unnecessary care by the Board of Directors that does not trust the executive body, or weakness of the executive body, which thus shifts the responsibility for company’s performance to the Board of Directors.

Figure 35. Frequency of the executive body’s reporting to the Board of Directors (by number of responses)

1.3.4. AUTHORITIES OF COMPANY’S MANAGEMENT

Respondents from the surveyed JSCs were asked to distribute a number of authorities between certain management bodies. This question enabled to determine knowledge of the mandatory requirements of the current legislation. The responses also enabled to understand in whose jurisdiction are certain issues that in accordance with the legislation can be entrusted to various management bodies at shareholders’ discretion. This distinction helps to identify the dominating management bodies in the JSCs.

It should be noted that in analyzing the responses, certain assumptions were made, as not all JSCs that responded to the questionnaires had Boards of Directors. Therefore, to some extent the results are distorted. For example, the exclusive authority of the Board of Directors, in its absence, can be attributed both to the general meeting of shareholders and the executive body (EB). Nevertheless, in our case the unavoidable distortions are insignificant, as there were only five companies that did not have Boards of Directors.

The respondents were asked some questions concerning the authorities of their management bodies.
In accordance with the current legislation, only EBs may represent the company (i.e. act in order to acquire rights and obligations of the company). However, some companies responded that the Board of Directors (17 responses) and even the general meeting of shareholders (11 responses) have such authorities as well.

In general, the responses suggest that in most JSCs, at least formally, the authorities of management bodies are defined in accordance with the legislation. In 48 JSCs the authorities of the general meeting include selecting a Chairperson of the Board of Directors. The respondents state that transfer of this function to the general meeting of shareholders increases responsibility of the Chairperson the Board of Directors. However, on the basis of the established practice, one can suggest the following – the Chairperson of the Board of Directors approved by the general meeting of shareholders is virtually non-replaceable, even if he/she does not fully perform his/her duties. In addition, he/she has an additional incentive, as in 13 companies Chairpersons of the Boards of Directors receive remuneration for the presidency.

**Separation of authorities of the management bodies**

As shown in Figure 37, some authorities are strictly defined by applicable law, such as issuance of shares, approval of transactions for the amount exceeding 50% of the book value of company’s assets, approval of the annual report and financial statements, and approval of

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![Figure 36. Authorities of management bodies (number of responses)](image-url)

<table>
<thead>
<tr>
<th>Authority</th>
<th>EB</th>
<th>BD</th>
<th>GMS</th>
</tr>
</thead>
<tbody>
<tr>
<td>Approval of remuneration for the EB head and members</td>
<td>5</td>
<td>19</td>
<td>53</td>
</tr>
<tr>
<td>Approval of remuneration for the BD Chairperson and members</td>
<td>8</td>
<td>31</td>
<td>59</td>
</tr>
<tr>
<td>Approval of internal documents regulating the activity of management bodies</td>
<td>5</td>
<td>24</td>
<td>32</td>
</tr>
<tr>
<td>Approval of internal documents regulating the activity of non-management bodies</td>
<td>10</td>
<td>27</td>
<td>59</td>
</tr>
<tr>
<td>Representation of the company</td>
<td>17</td>
<td>11</td>
<td>50</td>
</tr>
<tr>
<td>Define and approve priority directions of development</td>
<td>14</td>
<td>27</td>
<td>45</td>
</tr>
<tr>
<td>Appointment and dismissal of the EB members</td>
<td>8</td>
<td>14</td>
<td>50</td>
</tr>
<tr>
<td>Election/appointment and dismissal of the EB head</td>
<td>1</td>
<td>21</td>
<td>54</td>
</tr>
<tr>
<td>Election and termination of term of the BD members</td>
<td>1</td>
<td>2</td>
<td>68</td>
</tr>
<tr>
<td>Election and dismissal of the BD Chairperson</td>
<td>24</td>
<td>24</td>
<td>48</td>
</tr>
</tbody>
</table>
dividends, which are exclusively the competence of the general meeting of shareholders. Nevertheless, with regard to the issuance of shares, 13 respondents indicated other management bodies that take decisions; this indicates poor knowledge of the legislation, on the one hand and, on the other hand, the respondents indicate those who really make decisions in their companies.

The situation was similar with the other three questions relating to exclusive authorities of the general meeting of shareholders. The respondents in 15 companies stated that approval of transactions for the amount exceeding 50% of the book value of company’s assets was within the authority of the Board of Directors and executive body. 21 and 15 JSCs respectively incorrectly stated that approval of annual reports and financial statements, as well as approval of dividends was the authority of the general shareholders’ meeting.

The responses also revealed some violations related to exclusive authorities of the Board of Directors, even with the account of those companies where its authorities are partly transferred to the executive body, as they do not have the Board of Directors. Thus, the choice of an external auditor cannot be the competence of the executive body (22 responses), as the auditor’s task is to assure reliability of accounting by the executive body. It means that the executive body would therefore check its own activity.
1.4. DISCLOSURE OF INFORMATION AND TRANSPARENCY

Financial Reporting Standards

The KR Law on Accounting of the Kyrgyz Republic provides that JSCs’ financial statements shall be in line with IFRS. According to the schedule approved by the KR Government in 2009, all JSCs must maintain financial records in accordance with IFRS. 75% of companies stated that they maintained the accounting in line with IFRS.

Disclosure and transparency of information are crucial for companies that shall publish their financial statements. The survey covered just a few of such companies. Requirements of the legislation shall apply to such companies above all; however, supervisory authorities try to extend them to all companies. In this situation, about half of the JSCs disclose their financial information in the mass media to the extent required by IFRS.

Below is the information which is commonly disclosed by companies in the mass media.

**Figure 38. Information disclosed in the print media (number of responses)**

<table>
<thead>
<tr>
<th>Information</th>
<th>Number of Responses</th>
</tr>
</thead>
<tbody>
<tr>
<td>Profit and loss account</td>
<td>49</td>
</tr>
<tr>
<td>Annual report</td>
<td>47</td>
</tr>
<tr>
<td>Balance sheet</td>
<td>43</td>
</tr>
<tr>
<td>Cash flow statement</td>
<td>32</td>
</tr>
<tr>
<td>None of the above</td>
<td>27</td>
</tr>
<tr>
<td>Report on equity change</td>
<td>24</td>
</tr>
</tbody>
</table>

The majority of JSCs disclose to the public their profit and loss accounts (49 companies), Annual Reports (47) and balance sheets (43). Companies that do not disclose their information to the public provided a number of reasons for non-disclosure. Some of them (22 companies) do not see the need for disclosure, 11 companies do not disclose information as there are no legislative requirements for this, and 6 JSCs do not see any economic benefit in such disclosure.

**Figure 39. Reasons why information is not disclosed in the mass media (number of responses)**

<table>
<thead>
<tr>
<th>Reason</th>
<th>Number of Responses</th>
</tr>
</thead>
<tbody>
<tr>
<td>There is no need in disclosure</td>
<td>22</td>
</tr>
<tr>
<td>There are no any legislative requirements</td>
<td>11</td>
</tr>
<tr>
<td>It does not bring any economic benefit</td>
<td>6</td>
</tr>
<tr>
<td>Confidentiality of information</td>
<td>4</td>
</tr>
<tr>
<td>Lack of resources</td>
<td>4</td>
</tr>
<tr>
<td>Fear of interference by state bodies</td>
<td>3</td>
</tr>
<tr>
<td>Other</td>
<td>1</td>
</tr>
</tbody>
</table>
With regard to information received by shareholders in the form of an annual report, it consists mainly of the report of the Revision Commission (77 responses), audited financial statements (43) including notes to the financial reports and the EB’s analysis of the financial performance (68), which characterize company’s activity.

The report also includes the strategic goals and objectives of the company (50) and dividend policy (48). Quite often the report of the EB is supplemented by a report of the Board of Directors.

1.5. monitoring and auditing of financial and operational activities

External audit
External audits are carried out in 76% (68) of the surveyed companies. The majority of auditors are local audit companies (45) or individual auditors (20).
Only 27% of companies mentioned their negative experience of cooperation with the external auditors. As stated by the respondents, over the past three years auditors have been changed in 19 out of 68 companies, the reason for the change of an auditor in 8 companies was not a high price for services, while in 8 cases this was due to a conflict of interests or lack of auditor’s qualifications.

![Figure 42. Problems with external auditors (number of responses)](image)

<table>
<thead>
<tr>
<th>Problem</th>
<th>Number of Responses</th>
</tr>
</thead>
<tbody>
<tr>
<td>High price for services</td>
<td>8</td>
</tr>
<tr>
<td>Unsatisfactory quality of work</td>
<td>5</td>
</tr>
<tr>
<td>Conflict of interests</td>
<td>3</td>
</tr>
<tr>
<td>Other</td>
<td>3</td>
</tr>
</tbody>
</table>

**Internal Audit**

The respondents were asked about the nature of the internal audit. It should be noted that the legislation does not provide for mandatory internal audit for JSCs that are not financial and credit institutions.

![Figure 43. The nature of the internal audit (number of responses)](image)

- Independent specialist/body that provides reasonable guarantees and company’s consultancy developed to increase the cost and improve company’s performance: 15
- Specialist/body implementing internal control functions and company’s systematic methodology use for analyzing business processes or organizational problems and recommends the solutions: 13
- Internal controller supervising the activity of company’s staff: 11
- Specialist/body supervising the compliance of company’s activity with the government regulations and established terms: 6
- Specialist/body registering company’s business processes: 3
- Revision commission: 2

Nevertheless, the respondents from 35 companies stated that they had an internal audit function; in addition, the nature of the internal audit was described by those respondents who did not have any internal audit. The respondents who stated that they had internal audit in place likely meant a Revisions Commission. Indirect evidence suggests that the so-called “internal audit service” is tasked by the executive body.
1.6. IDENTIFYING AREAS OF CONCERN IN THE CORPORATE GOVERNANCE PRACTICES

The respondents were asked to assess the current legal and regulatory framework governing corporate governance as a whole. In addition, the respondents were asked to assess each of the proposed procedures in order to understand the overall effectiveness of the existing legislation. A 5-point scale was used for the assessment, however the survey team added the answer “I do not know” as some respondents were unable to assess some procedures due to lack of awareness of such procedures.

Regulatory framework
In general, 50% of respondents assessed the regulatory framework on corporate governance as satisfactory and above, 23% considered it unsatisfactory, and only 27% of respondents were unable to assess it.

The procedure of company’s registration/start-up was assessed quite high (31 JSCs out 66 rated the procedure as “good”), this was due to the recent changes in the legislation on registration. Regarding the procedure for JSCs liquidation, few companies have had such experience, and therefore, for quite understandable reasons, there was a great number of responses “I do not know” (33). Knowledge of this procedure is mainly theoretical and only a few respondents have such experience.
The legislation on protection of shareholders’ rights and disclosure of information to them is improved. There were changes in the legislation on JSCs in summer 2008 to a greater extent helped to change the situation in this area. Less understandable (21 responses) was the question regarding disclosure of information to stakeholders – who are they, if not shareholders. Some respondents did not understand such categories of persons.

Procedures related to corporate events were assessed in more details. This is normal, since all companies hold general meetings of shareholders and can assess effectiveness of the procedure. The majority of JSCs believe that these procedures are adequate and understandable.
Procedures for the formation of the Board of Directors and executive body are generally available and understandable; the respondents consider these procedures as properly designed. With regard to the formation of committees of the Board of Directors, the answer “I do not know” by 54% of respondents most closely reflects the current situation, as we saw earlier, there are actually no committees of the Board of Directors, moreover that these norms are not covered by the legislation.
Quite a high percentage of respondents, 39% or 35 companies, do not know about the mechanisms of settlement of corporate conflicts. The respondents assessed this issue from the perspective of general understanding of the legislative requirements, execution of which may help to resolve possible conflicts. Many respondents were unable to assess the legislation from this point of view. At the same time, 45% of respondents believe that strict adherence to the norms of legislation can help to overcome potential conflicts.

It was also difficult for the respondents to assess the procedure on issuing securities (stocks and bonds). 33% of companies do not know how to assess this procedure because they never had any practical experience. It should be noted that the initial issue was not taken into account, as its procedure substantially differs from the procedure on additional issuance of shares or other securities. 54% of respondents believe that this procedure is properly prescribed and 13% responded that it is unsatisfactory – this was stated by those companies that have applied this procedure in practice.

Based on the responses we can conclude that there are some gaps and shortcomings in the legislation of the Kyrgyz Republic. It is important to carefully review the existing norms in order to introduce changes and amendments that would streamline and simplify the procedures. It is also important to introduce international principles of corporate governance in JSCs of the Kyrgyz Republic.
Corporate relationships in the banking sector (financial and credit institutions) of the Kyrgyz Republic are regulated both by the general norms of legislation and are subject to special regulation by the NBKR. The activities of banks are subject to much more regulation and the regulatory framework in the field of banking activities is much broader. It includes documents such as the OECD Principles, Principles of Corporate Governance of the Bank for International Settlements (Basel Committee), Principles of Basel II (2004) and Recommendations on Banking Supervision of the Basel Committee (BCBS).

1.1 AWARENESS AND COMMITMENT TO CORPORATE GOVERNANCE

Banks are well aware of corporate governance principles. The surveyed banks This is not a complete list, however, other types of information are published quite rarely.

- Demonstrated good knowledge of the documents describing the corporate governance principles.
- The level of formalization of the corporate governance principles within banks is almost one hundred percent. Banks have all internal documents required in accordance with legislation. 80% of banks have adopted the Code of Ethics, and 40% have their own Code of Corporate Governance, although the existence of these documents is optional.
- Position of Corporate Secretary is weak and not sufficiently in demand. 40% of the banks have a Corporate Secretary. The role of the Corporate Secretary is not properly understood due to a small number of shareholders in banks.
- Improving the decision-making process is one of the priorities for the banks. The surveyed banks mentioned gaps between the corporate documents defining the interaction between the management bodies and reality. A typical response was that to achieve the goals of corporate governance, the key requirement (80%) is training on corporate governance for members of the Board of Directors.

1.2 MANAGEMENT BODIES OF A BANK

General Meeting of Shareholders

- The annual general meetings of shareholders are held on a regular basis. In all the surveyed banks, the annual general meetings of shareholders are held within the timeframe provided by legislation.
- Procedures for informing shareholders are observed. All banks provide their shareholders with the agenda of the general meeting and other necessary information.
- Outcomes of the annual general meetings of shareholders are circulated directly during the meeting and are later communicated to shareholders who did not attend the meeting.
- A common practice is voting by proxy through the representatives (100% of respondents). In 40% of the banks, the quorum at the general meeting of shareholders is 75–85% of shareholder votes, and in 40% – more than 85% of votes. This is due to a high concentration of shares with a limited number of shareholders. Only in 20% of JSCs the quorum is less than 75% of shareholders.
Extraordinary general meeting of shareholders
- 60% of the surveyed banks convened extraordinary general meetings over the past two years. The reasons for convening extraordinary meetings were different. The most common reasons are as follows: re-election of members of the Board of Directors and changing the charter and size of the authorized capital. Extraordinary general meetings of shareholders are initiated by the Board of Directors, executive body and major shareholders.

Board of Directors
- In the majority of banks, the Board of Directors is the governing body that actually performs operational management of the bank. The formal aspects of governance are clearly defined. Banks experience some difficulties in defining the appropriate functions of the Board of Directors.
- The banks’ Boards of Directors meet quite often. This is due to the need to direct the work of the internal audit, risk-manager and compliance officer who are appointed, tasked and are accountable to the Board in accordance with the Article 24 of the Law On Banks and Banking Activity, which requires that meetings of the Board of Directors in banks be held at least once a month. A common practice is that the banks’ management includes full-time Board members, that are directly involved in operational management.
- The structure of the Board of Directors is very simple. It has a mandatory audit committee. Most of the surveyed banks do not have any other committees under the Board of Directors.

Executive body
- Executive bodies of banks have difficulties when interacting with the Boards of Directors. Banks have collegial executive bodies.
- Executive bodies are formed by the Boards of Directors with obligatory approval of the NBKR. Respondents noted that they had problems when obtaining such approval from the regulator.
- Mandatory reporting of executive bodies. Executive bodies report to the Board of Directors in writing at least once a month, in addition to oral reports at each meeting of the Board of Directors and before full-time members of the banks’ Boards of Directors.

1.3. DISCLOSURE OF INFORMATION AND TRANSPARENCY OF BANKS’ ACTIVITIES

Disclosure of information
- Financial statements of all banks are in accordance with IFRS.
- All banks disclose their financial statements in the mass media, to the extent required by the legislation. In accordance with Regulation No 125-03 “On requirements to the formation of financial statements by commercial banks in the Kyrgyz Republic” dated December 29, 2003 and approved by the Resolution of the National Bank’s Board, the financial statements of banks shall include the following 5 components: 1) profit and loss account; 2) balance sheet reflecting the financial position; 3) cash flow statement; 4) statement of changes in capital structure; and 5) accounting policy and explanatory
1.4. MONITORING AND AUDITING FINANCIAL AND OPERATIONAL ACTIVITIES

- The internal audit function is mandatory and is in place in all banks. The respondents have a unanimous opinion regarding the functions of internal audit.
- Requirements on mandatory external audit for banks were established by the NBKR and banks strictly comply with the requirements. In most case (80%), the auditor is a local auditing company and 20% – international auditors.

1.5. COMPLIANCE WITH THE LEGISLATION OF THE KYRGYZ REPUBLIC IN THE FIELD OF CORPORATE GOVERNANCE

- Banks comply with legal and regulatory requirements on the formation of the management structure. Management bodies, including Board of Directors and the executive body, are formed in all banks in accordance with the requirements of the legislation.
- Weakness in terms of corporate governance in banks was noted in the distribution of authorities between the management bodies. Authorities of companies’ management formally comply with the legislation; however, there is a practice of interfering in operational activities.
- Banks rated the regulatory framework governing corporate relations in the Kyrgyz Republic as satisfactory. Problems are seen not in the normative component of corporate governance, but in the psychology of shareholders, who fear loss of control and thus dominate over the executive bodies.

Protecting shareholders’ rights

- There is a timely payment of dividends. The dividend policy of banks is regulated by the law prescribing mandatory distribution of net profit, regardless of its amount. In addition to the mandatory dividend payment, banks often use profits for capitalization. The requirement on mandatory payment of dividends leads to a situation when shareholders receive dividends and then use them for buying shares of the additional issue, in order to comply with the NBKR’s norms on capitalization.

1.6. IDENTIFYING AREAS OF CONCERN IN CORPORATE GOVERNANCE PRACTICE

- Representatives of the surveyed banks mentioned gaps and inconsistencies in the KR legislation. During the interviews, the respondents particularly complained about the Regulator’s norm-making activity. Strict regulation by the NBKR has both positive and negative aspects. There is a need to analyze the existing legal norms and improve the legislation.
- The current legislation, to some extent, helps to prevent and resolve corporate conflicts.
- The procedure for establishing committees of the Board of Directors was assessed differently due to the limited practice of establishing such committees.
The survey covered banks officers; half of respondents were companies’ managers and members of the executive body, the remaining respondents were banks employees.

**Figure 51. Companies officials that were interviewed and responded to questionnaires (number of respondents)**

<table>
<thead>
<tr>
<th>Role</th>
<th>Number of Respondents</th>
</tr>
</thead>
<tbody>
<tr>
<td>Head of executive body</td>
<td>2</td>
</tr>
<tr>
<td>Member of executive body</td>
<td>2</td>
</tr>
<tr>
<td>Corporate Secretary</td>
<td>1</td>
</tr>
<tr>
<td>Financial Director</td>
<td>1</td>
</tr>
<tr>
<td>Head of legal department</td>
<td>1</td>
</tr>
</tbody>
</table>

**1.1. GENERAL INFORMATION ON BANKS**

For the purpose of survey, banks that meet the following criteria were selected: (a) the proportion of state and foreign ownership is 0 or less than 50%; (b) all banks at the time of the survey were active; (c) all banks had staff of at least 25 employees. A set of questions covered some qualitative and quantitative characteristics of banks.

**Acquiring status of a joint stock company by banks**
The KR Law on Banks and Banking Activity sets requirements that all banks shall be joint stock companies. The surveyed banks were originally established as JSCs.

**The total number of bank employees**
By number of employees, banks with staff of 51 to 100 employees prevail. This situation characterizes the level of economic development of companies in the country.

**Figure 52. The number of banks’ employees (in %)**

- 101-150: 40%
- 151-250: 40%
- > 250: 20%
Number of banks’ shareholders
In terms of the number of shareholders, it is clear that banks do not yet tend to a sharp increase in their number. As stated by the respondents, a small number of shareholders contributes to maintaining control of the bank by a group of shareholders who are either bank’s founders or acquired a controlling stake from former owners.

The ownership structure of the surveyed banks is quite similar – the absolute control has a group of individuals or local companies.

Major shareholders
The respondents could not answer the question regarding the number of shareholders with equity participation. However, the following conclusions can be drawn. The largest shareholders are individuals who own 20 to 75% of shares. In one case, the controlling share was owned by legal entities. Some of the major shareholders are members of the Board of Directors and executive body.

Affiliation of major or controlling shareholders with each other
In terms of affiliation of banks’ major or controlling shareholders with each other, more often the respondents indicated that they were relatives (in three banks).

Transactions with affiliated persons
Transactions with affiliated persons in banks shall be approved by the Board of Directors and executive bodies.

The responses suggest that this issue is addressed in accordance with applicable legislation.

Kinship relationship between the controlling shareholders and management bodies
In answer to the question whether family members/relatives of the existing controlling shareholders are members of the Board of Directors and/or executive body of banks, 40% of respondents said “yes” for both categories.
The presence of an independent registrar

The register of shareholders in the surveyed banks is maintained by an independent registrar. In accordance with the legislation the register of shareholders in all open joint stock companies shall be maintained by an independent registrar. Closed joint stock companies can maintain the register themselves.

Attracting investments

Two-thirds of banks (60%) attracted foreign investment.

In two out of three cases, banks that have attracted external funds publicly offered their shares on the stock market and in one case these was direct investment of a local investor under a private offering.

Nevertheless, all interviewed banks plan to attract investment in the next three years. Two-thirds of the surveyed banks intend to attract direct domestic investment under a private offering. One bank intends to attract funds through public offerings on the stock market and the other one will borrow funds in the form of foreign loans.

1.2. COMMITMENT TO BEST PRACTICES IN CORPORATE GOVERNANCE

Banks were asked about their awareness of the OECD Principles and other documents, their attitude towards corporate governance in general and their commitment to take steps to improve corporate governance practices in their banks.

Understanding of main objectives of corporate governance

Most bank managers know the basic guidelines on corporate governance.

The most important objectives of corporate governance

Banks believe that good corporate governance is an important aspect of their activities. The respondents listed various objectives of the corporate governance. Each respondent could select up to three responses. Fifteen responses were received in total.
Improving the decision-making process in the bank and operational efficiency, increasing investment attractiveness and ensuring bank’s compliance with the legislative requirements on corporate governance are the most important objectives for 40% of banks. Other objectives, such as protection of shareholders’ rights, access to capital markets, preventing and resolving corporate conflicts and reduction of business risks are important for 20% of the banks.

Ways to achieve corporate governance related objectives
80% of respondents believe that for achieving the above objectives, they need training on corporate governance for members of the Board of Directors. 40% of respondents also believe that it is necessary to develop and adopt a Code of Corporate Governance, train members of the executive management and implement internal control systems. These activities will help banks to achieve the objectives of corporate governance.

Internal documents on corporate governance
As for commitment to generally accepted principles/codes of corporate governance expressed in the presence of certain internal documents in the banks, the picture is as follows.
As shown in Figure 56, the degree of formalization of corporate governance in banks differs significantly from the degree of formalization in other JSCs. This is due to the requirements of the NBKR which requires that the majority of these documents be in place.

**Corporate Secretary**

2 out of 5 surveyed banks have a Corporate Secretary working part-time, i.e. he/she combines his/her functions with other responsibilities in the bank.

**Using services of external consultants**

None of the surveyed banks used paid consultations of professional organizations providing services in the field of corporate relations.

**Factors hindering the improvement of corporate governance in banks**

In answer to the question regarding factors that hinder the improvement of corporate governance practices, most companies (60%) responded that this was due to a lack of information/knowledge, and that increased transparency can lead to increased risk (risk of bankruptcy, merger, etc.). Gaps in the legislation on corporate governance were mentioned by 40% of the respondents.
The level of corporate governance in banks
In general, banks have assessed the level of corporate governance as satisfactory and above.

The level of corporate governance in the country as a whole was ranked by all banks as satisfactory.

1.3. BANKS’ MANAGEMENT BODIES

1.3.1. GENERAL MEETING OF SHAREHOLDERS

All of the surveyed banks hold annual general meetings of shareholders within the period prescribed by the legislation and the meetings are held at their place of registration.

Notification of Shareholders Meeting
The majority of banks notify their shareholders in accordance legislation, namely, the management of the JSCs shall send a notification to shareholders at least 20 days prior to the forthcoming meetings in the open joint stock companies and 10 days in advance – in closed joint stock companies. Thus, all surveyed banks comply with the requirement of legislation (4 of the surveyed banks are open JSCs, and 1 is a closed JSC).
Banks shall advertise in the mass media and send notifications of the general meetings directly to shareholders. All banks comply with this requirement and additionally notify their shareholders using other means.

Materials for the Shareholders’ Meeting
In accordance with the legislation, joint stock companies of the banking sector shall provide shareholders with all materials of the upcoming meeting. However, banks do not fully comply with this requirement.

Outcomes of general meeting of shareholders
All banks announce the decisions of the general meeting of shareholders directly at the meeting. This is explained by the fact that some items of the agenda cannot be considered without approving the above decisions. In addition, banks inform their shareholders who did not participate in the meeting, for example, by e-mail.
Voting by proxy
Voting by proxy at the general meeting of shareholders is common for the banks.

Quorum and duration of general meetings of shareholders
The survey showed that the quorum at the general meetings in most banks exceeds the 75% threshold, which in our case indicates a high concentration of shares with a small group of shareholders.

A typical indicator is the duration of the general meetings of shareholders. All meetings in the banks last for 1 to 4 hours. During the interviews the respondents mentioned that the average duration of the meetings is almost four hours. This means that the meetings are fairly concise, although shareholders have also some discussions, and it is not just a formalization of decisions adopted by a group of controlling shareholders.

Dividends
In accordance with the current legislation of the Kyrgyz Republic, banks that have gained financial income in the past year shall distribute 25% of the net profit, regardless of its amount. Most banks are profitable and they do pay dividends; the remaining profit is capitalized, increasing authorized capital of the banks. This practice was developed in connection with the requirements of the NBKR on the minimum capital (authorized capital). Some banks pay dividends in the form of shares of additional issue, thus increasing the bank’s authorized capital.
Outcomes of the general meeting of shareholders
80% of banks publish outcomes of the last meeting and adopted decisions in the print mass media. In addition, the banks post information on their official websites.

Extraordinary general meeting of shareholders
60% of the surveyed banks held extraordinary general meetings of shareholders over the past two years. Such meetings are held for various reasons, as listed in Figure 65:

In most cases extraordinary meetings in the banks are initiated by the Board of Directors or executive body.
1.3.2. BOARD OF DIRECTORS

The Board of Directors is a body implementing control of the bank’s management and its financial condition. The Board of Directors determines bank’s strategy and policy, major risks and their acceptable level, oversees the activities of the Board, and monitors the effectiveness of the internal control systems. This is the requirement of the legislation in respect of corporate governance. Most Boards of Directors (80%) define the banks’ development strategy.

Below are quantitative and qualitative characteristics of Boards of Directors.

Banks do not have any specific formal contracts with Chairpersons and members of the Board of Directors.

Independent directors are well represented in the Boards of Directors in line with the requirements of the KR Law on Banks and Banking Activities. The percentage of independent directors on the Boards range from 33% to 80%.

The number of members in the Board Directors varies from 5 to 9 people, with the lower limit being defined by the law. The average age of directors varies in different companies from 35 to 45 years. Most members of the Board of Directors are men with 20% of women on average.

Under the current legislation of the Kyrgyz Republic, banks shall mandatory have credit and audit committees within the Board of Directors. The regulatory documents (Article 24, paragraph 9 of the KR Law on Banks and Banking Activity) also provides for the right of the bank’s Board of Directors to establish an advisory board, audit committee and other committees to implement business policy of the bank.

In accordance with the requirements of the banking legislation, the Boards of Directors in each bank have audit committees, while other committees are in place only in one bank, and they do not correspond to any of the recommended ones.

Meetings of the Board of Directors

Most Boards of Directors (60%) meet once a month, while others meet even more often. Boards of Directors are well informed. This is clear from answers to the questions regarding how long prior to the meetings of the Board of Directors its members receive notification and what thematic and other materials are distributed among members of the Board of Directors for consideration at the meeting.

<table>
<thead>
<tr>
<th>Figure 67. Terms of notification of the meeting of the Board of Directors (in %)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Up to one week prior to the meeting</td>
</tr>
<tr>
<td>One day prior to the meeting</td>
</tr>
<tr>
<td>There is no established practice</td>
</tr>
</tbody>
</table>
As shown in Figure 67, 40% of members of the Board of Directors receive notification a few days prior to the meeting, and the other 40% – one day prior to the meeting, the remaining members also receive notifications in advance, depending on the urgency of the meeting, but no later than one day prior to the meeting.

*Figure 68. Materials for the meeting of the Board of Directors (number of responses)*

<table>
<thead>
<tr>
<th>Material</th>
<th>Number of Responses</th>
</tr>
</thead>
<tbody>
<tr>
<td>Agenda of the BD’s meeting</td>
<td>5</td>
</tr>
<tr>
<td>Explanation to each point of the agenda</td>
<td>4</td>
</tr>
<tr>
<td>Draft decisions to be approved</td>
<td>3</td>
</tr>
<tr>
<td>Financial reporting for the last reporting period</td>
<td>2</td>
</tr>
</tbody>
</table>

**Remuneration for members of the Board of Directors**

In terms of incentives to encourage the work of members of the Board of Directors, in general, banks apply similar approaches. The most frequent responses were that members of the Board of Directors receive a fixed monthly remuneration (80% of the surveyed banks). In one case, only independent Board members receive remuneration, and the rest receive remuneration based on the annual performance.

It should be noted that banks may apply various material incentives for members of the Board of Directors.

**1.3.3. EXECUTIVE BODY**

All surveyed banks have a collective executive body represented by the Board.

**Remuneration for the executive body**

Members of the executive body receive a fixed remuneration, however in addition to fixed payments other incentives are also applied, such as a percentage of the company’s revenues (20%), or payments based on bank’s performance as a whole (20%).

**Accountability of the executive body**

In most cases the executive authority reports at meetings of the Board of Directors. Moreover, this report is provided in writing.

In some banks the executive body reports to the Board of Directors on a weekly basis, indicating excessive oversight by the Board of Directors, which does not completely trust the executive body.
1.3.4. AUTHORITIES OF BANKS’ MANAGEMENT BODIES

Banks were asked questions regarding authorities of their management bodies.

Representation of the company in the function of the executive body only. In general, the responses suggest that at least formally the authorities of the banks’ management bodies are defined in accordance with the law.
Respondents from banks were asked to distribute authorities between various management bodies of banks. The responses enabled us determine their knowledge of the mandatory requirements of the current legislation, as well as the authorities of various JSC’s management bodies to deal with certain issues. This distinction helps to identify dominant management bodies in the banks.

**Separation of authorities of the management bodies**
As shown in Figure 21, some authorities are strictly defined by the current legislation. For example, issuance of shares, approval of transactions exceeding 50% of the book value of company’s assets, approval of the annual report and financial statements and approval of dividends are the exclusive competence of the general meeting of shareholders. All surveyed banks comply with the requirement of the legislation.
1.4. DISCLOSURE OF INFORMATION AND TRANSPARENCY

Financial Reporting Standards
All banks apply IFRS.

Disclosure and transparency of information are crucial for the banks. Banking regulations define the list of mandatory information to be disclosed. In this situation, all banks disclose their financial information in the print mass media in the amount required by IFRS. The following information is disclosed in the print media by the surveyed banks.

<table>
<thead>
<tr>
<th>Information disclosed in the print media (in %)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Audited financial reports</td>
</tr>
<tr>
<td>Balance sheet</td>
</tr>
<tr>
<td>Cashflow statement</td>
</tr>
<tr>
<td>Profit and loss account</td>
</tr>
<tr>
<td>Annual reports</td>
</tr>
<tr>
<td>Quarterly reports</td>
</tr>
<tr>
<td>Report on changes in equity</td>
</tr>
<tr>
<td>Information on major shareholders</td>
</tr>
<tr>
<td>Reports on significant events</td>
</tr>
<tr>
<td>External audit results</td>
</tr>
</tbody>
</table>

Nearly all respondents provided similar responses to the question on how a potential investor may obtain information about the bank. All banks are ready to provide information directly to the investor. Another source of information about the bank can be the published annual reports, quarterly reports and information on the bank’s website.

1.5. MONITORING AND AUDITING OF FINANCIAL AND OPERATIONAL ACTIVITIES

External audit
Banks’ obligations to pass external (independent) audit is prescribed in legislation. In 80% of cases, these functions are performed by local auditing companies, and in one case – by an international auditing company.

Internal Audit
Each bank has an internal audit service appointed and supervised by the Board of Directors. The internal audit service is tasked and shall report to the Board of Directors. The respondents were asked a question which was to disclose the function of the internal audit service. It should be noted that all banks perceive the internal audit as a body which performs the functions of the internal control, uses bank’s systematic methodology for the analysis of the bank’s business processes or organizational problems and recommends the solutions.
1.6. IDENTIFYING AREAS OF CONCERN IN THE CORPORATE GOVERNANCE PRACTICES

Representative of banks were asked to assess the overall legal and regulatory framework governing corporate governance; they were suggested to separately assess a number of procedures in order to understand the overall effectiveness of current legislation. A 5-point scale was used during the assessment.

**Regulatory framework**

In general, 80% of banks rated the legal and regulatory framework on corporate governance as satisfactory and 20% as excellent.

The procedure of a bank’s registration/start-up was assessed as a whole as unsatisfactory (60%). One concern was the approval procedure of the NBKR. It is quite complicated to establish a bank as there are inconsistencies in the legislation on state registration of legal entities and the procedure of approval by the NBKR. Regarding the procedure of liquidation of JSCs, only a few respondents have had such an experience, and therefore the variation in assessment is quite understandable. The respondents have mainly theoretical knowledge of this procedure and only a few can refer to their experience.

80% of respondents believe that procedures on protection of shareholders’ rights and disclosure of information are well developed. Changes in the KR Law on Joint Stock Companies in the Kyrgyz Republic in summer 2008 have to a greater extent improved the situation in this area.
The most complete assessments were provided on the procedures related to corporate events. This is natural since all companies hold general meetings of shareholders and can assess the effectiveness of procedures. Banks consider these procedures adequate and understandable.

In general, the procedures for the formation of the Board of Directors and executive body are understandable and clear. 80% of banks consider these procedures as well developed and understandable. As for the formation of committees of the Board of Directors, the variation in assessments most accurately reflects the current situation. As we saw earlier, there are virtually no committees of the Board of Directors, except for the audit committee. In addition, these norms are practically not provided in the legislation.
60% of respondents believe that the procedure for control of the banks’ financial and economic activities is well developed.

60% of banks stated that settlement of corporate conflicts is not provided by the legislation. The respondents rated this procedure from the perspective of general understanding of the legislative requirements, implementation of which may help to resolve potential conflicts.

80% of respondents easily assessed the procedure on issuance of securities (stocks and bonds). Banks face this in practice almost every year and have an established pattern of interaction with the registration agencies.

Representatives of banks, as well as JSCs from the non-banking sector noted that there are gaps and inconsistencies in the legislation. Especially a lot of criticism was expressed during the interviews with regards to the rule-making activities of the NBKR. Strict regulation by the National Bank has both positive and negative aspects. There is a need for the analysis and improvement of the current legislative norms in this area.