Organisation for Economic Co-operation and Development
In Co-operation with The World Bank Group

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The Latin American Corporate Governance Roundtable

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It is an honor and a great personal pleasure for me to open this first meeting of the Roundtable on behalf of the World Bank Group. IFC has been involved in the preparation for this event since December 1998 when the CVM first asked the IFC for help in putting together some sort of regional event on this topic. When Bovespa, the CVM and the Brazilian Institute of Corporate Governance got together with OECD and decided to sponsor a regional roundtable, all of us at the World Bank Group were very encouraged and redoubled our efforts to help it succeed. It is gratifying to see such an impressive set of leaders from the Region on the agenda and in attendance. OECD and all the sponsoring institutions can be justly proud to have brought this effort to such a successful fruition.

I would like to use these brief opening remarks to raise some key questions I think we should be asking ourselves this morning:

First - Why is this happening now? Why has corporate governance become such an important part of the agenda of both the public and private sectors?

Second, What are the special challenges of this period in history that the companies, governments and private sector institutions represented here must face when they think about improving corporate governance in Latin America?

And finally - What should we be hoping to accomplish together in the next three days?

Why is this Happening Now?

Clearly the recent East Asian and Russian crises re-focused the attention of *international* investors on the shortcomings of corporate governance in many developing (and even OECD) countries. In Latin America, several well-publicized scandals, like the ones surrounding the sale of Chile's Enersis to Endesa-España or TV Azteca's support of the private ventures of its controlling shareholder in Mexico, remind both domestic and foreign investors of the importance of transparency and good corporate governance for shareholder value. But the high-profile events of the last three years are more responsible for accelerating the re-examination of corporate governance in the region than they are for instigating it. More fundamental shifts were already underway in the economies of

the region, and just as importantly in the attitudes and expectations of companies, investors and policy makers. These shifts continue to drive the policy dialog on how companies should be managed and how outside sources of capital should expect to be treated.

In my view, the emphasis on the corporate governance regime we see reflected here today is part of a broader maturation process. The thinking about the proper role of public institutions, rules and standards has changed since the region first began moving toward more market-driven economies in the 1980s. In the 1980s many people understood a market economy as implying no government involvement and only the bare minimum of rules and standards. Everything would be left to private contracting, market discipline and caveat emptor.

Experience has taught that this view is too extreme. Gradually, both the public and the private sectors have come to realize just how rule-dependent markets, particularly financial markets, are. Without clear, appropriate and enforceable rules and standards, markets become fragmented and inefficient. Transaction costs escalate. Participants' expectations start to diverge in unpredictable ways. There are just too many variables, too many risks to keep track of and to discount.

Please don't misunderstand the direction of these remarks. We at IFC do not believe that policy makers in the region should use the need for clear rules and standards as a pretext for re-introducing government control of the economy. Far from it. Government is very often the wrong party to be formulating rules and setting standards. It usually lacks sufficient knowledge of how specific markets work and how the participants in such markets will react. Formulating appropriate rules of conduct, like those affecting corporate governance and the treatment of investors and other stakeholders, should be a joint effort involving both the public and private sectors. The roles left to each of them in formulating and enforcing rules and standards necessarily vary from country to country and from time to time in a single country. Historical experience, level of economic development and the relative capacities of public and private sector institutions are critical factors in determining the respective roles of government and non-governmental institutions in this process. Getting it right is one of the key challenges we face.

Current Challenges

These sorts of opening remarks are not the place to get into each of the legal, regulatory and practical issues that must be addressed when we think about ways of improving corporate governance. These will be covered quite systematically, and more than adequately, by the impressive collection of experts on the panels assembled for this round table. But perhaps this is a good point to touch on what I think is the key challenge at this point in history that governments and the private sector must face in formulating responses to the need to improve corporate governance. That challenge is the challenge of globalization.

As I mentioned earlier, policy makers cannot ignore the special historical, economic, political and legal circumstances of their jurisdictions in designing the elements of an appropriate corporate governance regime. But neither can policy makers ignore what is happening outside their jurisdictions. We live in an increasingly economically integrated world. And even in the political and legal arenas, there are important trends toward convergence and harmonization. For those of us assembled here, recognition of the fact of globalization means at least three things:

First, that all parties involved - companies, investors, other stakeholders, and even governments - are increasing accountable to parties outside the domestic economic, political and legal arena;

Second, that the rules and standards of one country must therefore take into account those prevailing elsewhere; and

Third, that national actors, including governments and private sector institutions, cannot fully control the content or process of domestic rulemaking and standard setting.

I am afraid that these three factors greatly complicate the work of people and institutions like those who have come together for this round table.

In Latin America, as in virtually every other part of the world, the domestic economy is less and less closed off every day. Every element of human activity is increasingly cross-border. Trade in goods, trade in services, savings and investment, and now even ownership of companies and financial institutions are more unfettered by the artificial boundaries established by treaties than at any time in the past. But the fact that economic activity knows no boundaries does not mean that it recognizes no

authority. The company, investor or financial institution that does business cross-border exposes itself to the demands of multiple national and sometimes multi-national authorities and must somehow find a way to structure its activities to meet the requirements of all of them.

I am, of course, not just talking here about rules established and enforced by governments. Naturally, domestic companies that raise equity in foreign markets subject themselves to the formal rules of the exchanges on which their securities are traded as well as the accounting and auditing rules required in such markets. But companies that borrow money from or sell shares to foreigners also expose themselves to the customs and practices of disclosure and transparency that lenders and investors in such jurisdictions expect from those to whom they provide financial resources. Likewise, investors and financial institutions that reach across borders also need to accommodate the laws, rules and folkways of the countries in which their monies are put at risk. In every case, the capital provider or capital consumer operating cross-border has a wider set of "accountabilities" than it ever had in the now distant time when it could operate exclusively within a closed domestic environment with a single set of rules and expectations.

The unavoidable multiplication of "accountabilities" created by globalization is one reason there are, and need to be, standards for both domestic and international capital markets. And what this means for legislatures, agencies and private standard-setting institutions is that they need to take into consideration international standards in everything they do. Because if domestic rules vary too much from them, domestic actors might find themselves disadvantaged. In the financial markets, they may get cut off from important sources of capital, or important investment opportunities. It also means that national institutions, public and private, must participate in the process of international standard setting.

So certainly one of the most daunting challenges, if not <u>the</u> most daunting challenge, facing the people in this room and particularly the public institutions represented here is: How can we further the goals of better corporate governance, when each of us controls only a part of the whole framework?

There is no simple answer. Globalization generates complexity. But clearly, active participation by both public and private institutions in the continuing process of developing and strengthening international as well as national standards is an important part of the answer. In view of the structure of international capital markets and the events of the last three years, there clearly needs to

be a closer relationship and greater cooperation between OECD and non-OECD countries. Events like this one, and the continuing character of the OECD-sponsored Roundtables process, respond to this need.

Goals of the Round Table

So what are we trying to accomplish in these three days? Well, certainly we are here to learn from each other. Much learning has already been assembled and disseminated from the various national and bi-national events that have taken place – in Santiago and Rio last year, and more recently at the Buenos Aires seminar sponsored by the Argentine and Spanish securities regulators. But this will be the first major event to bring together knowledge on a region-wide basis. These next three days will give us a chance to talk about has been tried, what is being tried and what the record has been so far in the region's efforts to improve corporate governance. We will all certainly come away from these next three days better informed about what is happening outside our own countries than we are this morning.

But learning alone cannot be the goal of this event. This is not an academic conference. The people who will be participating in this event are important opinion makers and policy makers. They have come here to exchange ideas, that it true. But more importantly I believe they have come to Sao Paulo to better equipped themselves to change the expectations of companies, investors, stakeholders and the public about how companies should govern themselves and how they should treat investors and other stakeholders.

This process of changing expectations requires a not insignificant amount of coordination of thinking. It requires the building of some sort of consensus about priorities and how to address the key problems. Building consensus requires information sharing, cooperation, and broadening the dialog to include all those public and private sector institutions that have a role to play and more emphasis on public education. The OECD Round Table process can serve as an important tool for building the needed consensus. Those represented here today and who will be participating over the next three days are uniquely positioned to advance this process, and through changing expectations about corporate governance improve the incentives and the performance of companies and financial markets.