



**Organisation for Economic Co-operation and Development**  
*In co-operation with the World Bank Group*

# **SECOND SOUTH-EASTERN EUROPE CORPORATE GOVERNANCE ROUNDTABLE**

**“Transparency and Disclosure”**

*Meeting Hosted By*  
**The OECD Centre for Private Sector Development**  
*and*  
**The Turkish International Co-operation Agency (TICA)**

*Sponsored By*  
**Deutsche Gesellschaft Für Technische Zusammenarbeit (GTZ)**  
*and*  
**The Global Corporate Governance Forum**

**SYNTHESIS NOTE**

**Istanbul,  
30-31 May 2002  
Yali Kosku Cad., 19 Mayıs  
Ishani 3. Kat, Eminonu**

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**I. Background**

The South-Eastern Europe Corporate Governance Roundtable was launched in September 2001, and is organised by the OECD in co-operation with the World Bank Group and key regional partners. It is also a Flagship Regional Program of the Investment Compact<sup>1</sup> and receives financial support from the Deutsche Gesellschaft Für Technische Zusammenarbeit (GTZ) and the Global Corporate Governance Forum.

The second meeting took place on 30-31 May 2002 in Istanbul. It was hosted by the OECD Centre for Private Sector Development and the Turkish International Co-operation Agency (TICA). The meeting focused on disclosure and transparency, which is the fourth chapter of the OECD Principles of Corporate Governance.

The Roundtable brought together a group of about 100 highly qualified senior policy-makers and private sector practitioners, both from South East Europe (Albania, Bulgaria, Croatia, FYROM, Bosnia-Herzegovina, FR Yugoslavia, Moldavia, and Romania) and OECD countries (Germany, Greece, Spain, Turkey and the US). Participants from International Organisations included experts from the OECD secretariat, the World Bank, the Global Corporate Governance Forum, the European Bank for Reconstruction and Development, the European Commission, UNCTAD, the Stability Pact for South-East Europe, as well as the Black Sea Business Council and the Small Enterprises Assistance Fund.

The meeting was opened by: Mr. Rainer Geiger, Deputy Director of the Directorate for Financial, Fiscal and Entreprises Affairs at the OECD; Mr. Nihat Kaya, the Vice-President of the Turkish International Co-operation Agency; Ms. Miarta Capaul, Senior Specialist in the Private Sector Advisory Services of the World Bank; and Mr. Tihomir Domazet, Assistant Minister of Finance of Croatia. The opening remarks underlined the importance of corporate governance for financial market development and access to equity capital, thus making corporate governance a key element of the Stability Pact for Southeastern Europe.

**Documentation from the SEE Roundtables, including the agenda, presentations, background papers and the draft White Paper, can be found on the OECD website at [HTTP://WW.oecd.org/daf/corporate-affairs](http://www.oecd.org/daf/corporate-affairs).**

**II. Discussions and Main Conclusions**

The meeting started with a general discussion about the importance of transparency and disclosure for an efficient capital market. It was pointed out that transparency and disclosure is a prerequisite to improve the investment climate as well as efficiency of financial markets. It also gives shareholders means and data to act in an informed fashion and pursue their rights more efficiently. Last but not least, it provides managers with quantitative tools allowing them to manage better. Good transparency and disclosure is based on two pillars. Firstly, it needs a reliable and enforceable legal and regulatory framework. Secondly, it relies on the integrity and diligence of professions such as accountants and auditors, security analysts, credit rating agencies, investment banks and law firms.

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<sup>1</sup> The Investment Compact, adopted in February 2000, is a vital part of economic reform activities to be carried out under Working Table II of the Stability Pact for South Eastern Europe, dealing with Economic Reconstruction, Co-operation and Development.

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The opening session also contained a presentation of the work by the European Commission regarding transparency and disclosure that will be part of the *acquis communautaire* for accession countries. The numerous initiatives under consideration include management and board responsibility in financial disclosure, the adoption of IAS, consolidated accounts, insider trading and auditors' independence.

The remaining sessions focused on:

- the present situation and main issues regarding financial and non financial disclosure (sessions 3 and 4),
- the reform of the accounting and auditing regulatory framework (session 2),
- the respective roles of auditors, board members and management (session 5),
- the role and monitoring power of enforcement bodies, including securities commissions and stock exchanges (session 6).

Each session included a discussion among the experts, giving an excellent opportunity to:

- gather substantial information and share experience on the respective countries' situations,
- consider impediments to the implementation of better disclosure practices,
- identify key areas for improvement in the regulatory domain and in private practice,
- present, discuss and analyse various solutions and policy measures to current disclosure and transparency challenges.

Building on these discussions, the meeting fulfilled its three main purposes; firstly, to raise awareness and knowledge about the role of disclosure and transparency in corporate governance; secondly, sharing experiences on potential remedies to specific problems related to disclosure and transparency in SEE; and thirdly, providing elements to guide the drafting of the White Paper.

Discussions revealed a broad consensus on the following priorities for improvements and reforms:

- 1) improving accounting and auditing practices;
- 2) strengthening the supervision of the accounting and of the auditing professions;
- 3) enhancing disclosure regarding ownership structure and material events;
- 4) using efficiently audit committees;
- 5) improving compliance by companies.

*1) Improving accounting and auditing practices*

Transparency and disclosure firstly depends on the quality of financial information that is provided by accountants and checked by auditors. Difficulties in this area derive from the inheritance of a socialist system where accounting primarily served statistical and tax purposes. Participants underlined that a significant change in mindset is required in order for financial statements to be considered as a tool instead of a burden, and that potential EU accession is a principal driving force in the process of adopting IAS. However, while most countries have adopted or are in the process of adopting IAS for large enterprises, implementation of these standards is still problematic. Participants identified and discussed major issues in this area, including inflation accounting, undisclosed liabilities and valuation of assets. Speakers and discussants exposed how inadequate amortization and lack of provisions, in particular for doubtful receivables, are highly distorting, while valuation of inventories often lead to significant hidden losses. Finally, the quasi absence of consolidated financial statements was highlighted and explained by the lack of clearly defined criteria for consolidation and the complexity of value adjustments in the transition context. Considering what is at stake, some participants called for a significant and practical assistance in helping SEE countries to implement accounting and audit reforms, especially with regards to the training of accountants and auditors.

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*2) Strengthening the regulation of the accounting and auditing professions*

Participants noted that adopting accounting and auditing standards is not enough. Equally important is the monitoring of compliance and enforcement of such standards. All participants agreed that the regulation of the accounting and audit profession must be strengthened, which implies building up adequate incentives and sanctions. It was noticed that public oversight of professional associations is justified by the fact that the audit should be considered not as a private contract but as a public good. Strong emphasis was put on the necessity to strengthen the capacity of regulatory bodies in terms of resources, qualification and most of all independence from the professions. The adequate incentive structure that would encourage this independence was discussed. In this context, it was noted that the governance of the audit firms themselves and particularly the regulation of international audit networks have to be considered.

*3) Significantly enhancing the disclosure of ownership structure and material events*

The disclosure of ownership and control structures is a weak point in SEE corporate governance practices. Such disclosure is however crucial for investors to assess who is controlling the enterprise and evaluating their own position and interest in providing equity. It is also necessary for fighting against prevailing abusive related parties transactions and insider dealings. The participants thoroughly discussed the respective responsibilities of investors, companies, managers, stock exchanges, depositories/registrars and Securities Commissions in declaring, collecting, checking and making available ownership information. These responsibilities have to be examined and clarified in each national context. It was also underlined that such disclosure has to encompass indirect holdings and beneficial ownership. Another weak point in SEE disclosure practices is the lack of disclosure of material events. Some participants highlighted the necessity to disclose fully, accurately and on a timely basis all material information. The specific features of such disclosure were also discussed extensively.

*4) Using audit committees efficiently*

The meeting participants agreed that the board should include independent, qualified and experienced members to ensure that appropriate accounting, auditing and disclosure standards are applied. They advocated the creation of specialized audit committees that could help in carrying out this crucial responsibility of the board. It was suggested that such committees could be responsible for selecting the external auditor, receiving and approving the auditors' report, and communicating the results to the shareholders.

*5) Improving compliance by companies*

The discrepancy between legal and regulatory requirements regarding transparency and disclosure and actual practices is huge. To narrow this gap, participants agreed that a significant modification of the incentive structure of companies has to be made, using both "carrots and sticks". This implies an increased awareness of the benefits that transparency brings to the company. But participants underlined the necessity to significantly improve the enforcement capacity of Securities Commissions. This includes an increase in their financial and human resources as well as in their legal capacity to sanction companies. This also requires an enhanced role for Stock Exchanges in disseminating and identifying lack of disclosure. Last but not least, participants called for a clarification of responsibilities between the different company officials, and more specifically between the management and the board members. They also discussed whether the personal liability of management and board members for lack of disclosure should be revised.

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### **III. White Paper discussion**

The Roundtable has decided to issue a regional White Paper. This White Paper will propose a set of practical recommendations and should serve as a means for setting priorities and implementing reform at national or corporate level. A draft of the first two chapters of the White Paper (on shareholders rights and equitable treatment) had been distributed prior to the meeting. This draft was discussed during the last half-day of the meeting.

Discussions allowed for modifying and fine-tuning some draft recommendations, in particular: thresholds for using independent registrars; the access of all shareholders to ownership information; the quorum for shareholders meetings and major transactions approval; the own transparency and governance of institutional investors and the effective use of pre-emptive rights during new issues. Some recommendations were more thoroughly discussed, for example the enforcement obstacles for abusive related parties transactions and the possibility to reinforce redress mechanisms. Finally, some additional recommendations along with specific references were also suggested by participants, especially regarding the definition and disclosure of beneficial ownership and the necessity of independent appraisal processes.

Furthermore, a first discussion was held on priorities and some specific recommendations in the area of disclosure and transparency. This discussion summarized the main achievements of the meeting and will guide the drafting of the related chapter of the White Paper. The main points of this discussion are described in part II of this note.

### **IV. Next steps**

The next meeting of the Roundtable on Corporate Governance in South East Europe will take place on 21-22 November 2002 in Zagreb, co-hosted by the Zagreb Stock Exchange. It will focus on the two remaining chapters of the OECD Principles of Corporate Governance, namely the responsibilities of the board and the role of stakeholders in corporate governance.

The drafting process for the White Paper will be as follows:

- An amended version of the chapter on shareholders' rights and equitable treatment will be circulated to the Roundtable participants in July.
- The chapter on disclosure and transparency will be drafted during the summer and circulated to participants at the beginning of September. Participants will be given one month to provide some written comments on this first draft. The draft will be modified accordingly and circulated two weeks before the third roundtable, in order to be discussed at the meeting.
- Following the third Roundtable, a draft of the two chapters on the responsibilities of the board and the role of stakeholders will be submitted to the Roundtable's participants for their written comments.

A final meeting will be organized beginning of 2003 to discuss and approve the final version of the White Paper.