THE REVISED OECD PRINCIPLES OF CORPORATE GOVERNANCE AND THEIR RELEVANCE TO NON-OECD COUNTRIES

By Fianna Jesover and Grant Kirkpatrick[1]

ABSTRACT

The OECD Principles of Corporate Governance were revised in 2004 to respond to corporate governance developments including corporate scandals that further focused the minds of governments on improving corporate governance practices. Since they were first issued in 1999, the OECD Principles of Corporate Governance have gained worldwide recognition as an international benchmark for sound corporate governance. They are actively used by governments, regulators, investors, corporations and stakeholders in both OECD and non-OECD countries and have been adopted by the Financial Stability Forum as one of the Twelve Key Standards for Sound Financial Systems. The 2004 revision of the OECD Principles reflects not only the experience of OECD countries but also that of emerging and developing economies. This article shows how the revised Principles take into account the recent lessons and conclusions from non-OECD countries so that they continue to maintain their global relevance. This article was prepared for

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Introduction

The *OECD Principles of Corporate Governance,* originally adopted by the 30 member countries of the OECD in 1999, have become a reference tool for countries all over the world. Following an extensive review process that led to adoption of revised *OECD Principles of Corporate Governance* in the spring of 2004, they now reflect a global consensus regarding the critical importance of good corporate governance in contributing to the economic vitality and stability of our economies. Good corporate governance – the rules and practices that govern the relationship between the managers and shareholders of corporations, as well as stakeholders like employees and creditors – contributes to growth and financial stability by underpinning market confidence, financial market integrity and economic efficiency. Recent corporate scandals have further focussed the minds of governments, regulators, companies, investors and the general public on weaknesses in corporate governance systems and the need to address this issue.

The *OECD Principles of Corporate Governance* provide specific guidance for policymakers, regulators and market participants in improving the legal, institutional and regulatory framework that underpins corporate governance, with a focus on publicly traded companies. They also provide practical guidance and suggestions for stock exchanges, investors, corporations and other parties that have a role in the process of developing good corporate governance. They have been endorsed as one of the Financial Stability Forum twelve key standards essential for financial stability. The *OECD Principles* have become the international benchmark for corporate governance, forming the basis for a number of reform initiatives, both by governments and the private sector. The OECD began a review of the *Principles* in 2003 to take into account recent developments through a process of extensive and open consultations. The new *Principles* were agreed by OECD governments in April 2004.

The revision of the Principles reflects not only the experience of OECD countries but also that of emerging and developing economies, including those involved in the policy dialogue of the Regional Corporate Governance Roundtables established by the OECD in co-operation with the World Bank Group. Consultations with non-member partners were first undertaken through meetings of Roundtables held in Asia, Eurasia, Latin America, Russia and Southeast Europe. Lessons and conclusions emerging from this work were summarised in the publication, "Experiences from the Regional Corporate Governance Roundtables", OECD 2003. Additional input was obtained from a special meeting attended by 43 non-member countries organised in cooperation with the Global Corporate Governance Forum. This article shows how the Principles take into account the lessons and conclusions from non-member countries so that the Principles can continue to be relevant globally.

Relevance of the *Principles* to non-OECD countries

The OECD *Principles* are highly relevant to non-OECD economies. The experiences of economic transition and financial crises in developing and emerging market economies have confirmed that a weak institutional framework for corporate governance is incompatible with sustainable financial market development and growth (Claessens, 2003). Good corporate governance helps to bridge the gap between the interest of those that run a company, including a major shareholder, and the shareholders more generally, increasing investor confidence and lowering the cost of capital for the company. Good corporate governance also helps ensure that a company honours its legal commitments, and forms value-creating relations with stakeholders including employees and creditors. To support corporate governance reform worldwide, the OECD in co-operation with the World Bank Group, established the Regional Corporate Governance Roundtables in five regions: Asia, Russia, Latin America, Eurasia and South East Europe. Over the last five years, the OECD has organised 30 meetings of the Regional Corporate Governance Roundtables in 18 countries. Thirty-eight non-member countries (see Table 1 excerpted from "Experiences from the Regional Corporate Governance Roundtables, "OECD 2003) participate in the Roundtables, as do a majority of OECD member countries. The Roundtables also receive support from national and multilateral donors.

Table 1. Non-member countries participating in the Roundtables

	Population *Millions*	Per Capita Income *Purchasing power parity gross national income per person in US dollars*	Market Capitalisation of Listed Companies *%GDP*	Credit to Commercial Sector *%GDP*
		ASIAN ROUNDTABLE		
Bangladesh	133.3	1,700	2.5	24.7
China	1,271.9	4,400	53.8	124.6
Chinese Taipei	22.6	18,000	NA	NA
Hong Kong, China	6.7	26,000	383.5	158.8
India	1,032.3	2,540	32.4	29.0
Indonesia	209	3,100	17.6	21.6
Malaysia	23.8	9,300	129.9	140.6
Pakistan	141.4	2,100	10.8	29.8
Philippines	77.0	4,200	69.0	44.5
Singapore	4.1	24,000	164.8	109.4
Sri Lanka	18.7	3,700	6.6	28.9
Thailand	61.1	6,900	24.4	108.7
Vietnam	79.5	2,250	NA	35.3
		EURASIAN ROUNDTABLE		
Armenia	3.0	3,800	1.4	10.6
Azerbijan	8.1	3,500	0.1	5.9
Georgia	5.2	3,100	NA	8.8
Kazakhstan	14.8	6,300	7.3	11.2
Kyrgyz Republic	4.9	2,800	NA	4.2
Moldova	4.2	2,500	3.2	12.7
Mongolia	2.4	1,840	3.5	8.1
Ukraine	49.1	4,500	6.0	11.2
Uzbekistan	25.0	2,500	0.4	NA
		LATIN AMERICAN ROUNDTABLE		
Argentina	37.4	10,200	58.4	23.9
Bolivia				
Brazil	172.6	7,600	38.1	35.1
Chile	15.4	10,000	80.0	63.5
Colombia	43.0	6,500	11.5	26.9
El Salvador	6.4	4,700	15.5	41.6
Peru	26.1	4,800	25.9	19.8
Uruguay	3.3	7,800	0.8	51.2
Venezuela	24.6	5,500	6.7	12.0
		RUSSIAN ROUNDTABLE		
Russia	144.7	9,300	15.0	11.9
		SOUTH EAST EUROPE ROUNDTABLE		
Albania	3.1	4,500	NA	4.5
Bosnia-Herzegovina	4.0	1,900	NA	NA
Bulgaria	7.9	6,600	4.9	11.9
Croatia	4.3	8,800	14.4	36.2
FYR of Macedonia	2.0	5,000	0.2	17.8

Romania	22.4	7,400	2.8	7.2
Serbia and Montenegro	10.6	2,370	NA	0.1

Per capita income 2002 estimate, all other figures for 2001.

Source: World Bank, CIA World Fact Book, Chinese Taipei National Statistics.

The Roundtables have revealed a wide range of corporate governance challenges across the five regions. Many of the participating individuals from the countries concerned have taken the lead in proposing and implementing reforms to respond to these challenges. Nonetheless, substantial work remains. The regional Roundtables have produced regional corporate governance White Papers identifying priority areas for reform; the Roundtables will continue to assist in developing and implementing these reform priorities. Some of the main findings of the Roundtables are summarised below. One of the critical findings of the Roundtables is the usefulness of the *Principles* as a guide for multilateral policy dialogue. The Roundtables also confirmed the adaptability of the *Principles* as a reference in varying legal, economic, and cultural contexts.

This experience has highlighted a number of characteristics. For example, a number of countries have witnessed insider boards that have become a part of management, rather than an active monitor of its performance. In other cases, boards appear to act simply as rubber stamps, responding to the wishes of a controlling shareholder. In a number of cases controlling shareholders have pursued their interests at the expense of minority shareholders. Complex financial institutions and complex corporate structures around the world have also thrown into stark relief the question of conflicts of interest, which have been most apparent in some brokerage research and in funds management. The *Principles* have always addressed these issues, but the revised version gives them more emphasis.

What are the *Principles* and what key issues do they address?

The *Principles* cover six key areas of corporate governance – ensuring the basis for an effective corporate governance framework; the rights of shareholders; the equitable treatment of shareholders; the role of stakeholders in corporate governance; disclosure and transparency; and the responsibilities of the board (see Box 1). Explanatory annotations for each area also indicate the range of policy measures which have proved useful in achieving them. Key to the success of the *Principles* is that they are principles-based and non-prescriptive so that they retain their relevance in varying legal, economic and social contexts including those features characteristic of non-OECD countries that participated in the Roundtables.

Box 1. The main areas of the OECD Principles

I. Ensuring the basis for an effective corporate governance framework

The corporate governance framework should promote transparent and efficient markets, be consistent with the rule of law and clearly articulate the division of

responsibilities among different supervisory, regulatory and enforcement authorities.

II. The rights of shareholders and key ownership functions

The corporate governance framework should protect and facilitate the exercise of shareholders' rights.

III. The equitable treatment of shareholders

The corporate governance framework should ensure the equitable treatment of all shareholders, including minority and foreign shareholders. All shareholders should have the opportunity to obtain effective redress for violation of their rights.

IV. The role of stakeholders in corporate governance

The corporate governance framework should recognise the rights of stakeholders established by law or through mutual agreements and encourage active co-operation between corporations and stakeholders in creating wealth, jobs, and the sustainability of financially sound enterprises.

V. Disclosure and transparency

The corporate governance framework should ensure that timely and accurate disclosure is made on all material matters regarding the corporation, including the financial

situation, performance, ownership, and governance of the company.

VI. The responsibilities of the board

The corporate governance framework should ensure the strategic guidance of the company, the effective monitoring of management by the board, and the board's accountability to the company and the shareholders.

The basic requirements of the institutional and legal/regulatory framework needed to support effective corporate governance are an integral part of the *Principles.* This first section includes principles for developing such a framework and addresses the need for laws and regulations which are both enforceable and are backed by effective enforcement agencies. Experience around the world shows that although the powerful concept of a listed joint stock company has been successfully introduced in many countries, the accompanying legal and regulatory system has often lagged, leading in some cases to abuse of minority shareholders and to reduced growth prospects when financial markets lose credibility -- or fail to achieve it in the first place.

Other areas covered by the *Principles* can be grouped according to key issues that cut-across the other five sections. For example, they are aimed at establishing an effective system of checks and balances between boards and managers. Professional managers have a key role to play in the modern listed or widely held company but to avoid possible misuse of their position requires, *inter alia*, effective monitoring by the board. The *Principles* stress that such monitoring should not involve day to day management but rather ensure strategic guidance of the company and the oversight of internal controls.

But who monitors the monitors? The board in turn is accountable to shareholders who, the *Principles* maintain, should be able to exercise their fundamental ownership rights, including appointing and removing board members, and should be treated equitably by the company. Effective use of ownership rights to monitor and influence the board requires basic standards of disclosure and transparency, another area which is considered. Reality is, however, often more complex with companies and their management controlled by a dominant shareholder – a somewhat different case for monitoring, but one that is also covered by the *Principles*. Finally, if the enterprise is to be successful, the board will also have to consider stakeholders such as employees and creditors who supply the firm with resources and who also need access to timely and relevant information. The *Principles* already addressed this issue but now they offer more guidance on improving the enforcement of creditor rights and building an effective insolvency framework.

What do the Roundtables and *Principles* say about strengthening enforcement?

Perhaps the most widespread sentiment expressed in the Roundtables was the importance of improving the enforcement of existing law and regulations. While legal traditions vary across countries, there is a broad consensus that the structure, vigilance, and capacity of the regulatory and judicial framework forms an integral part of the corporate governance environment. All Roundtables have emphasised the need to "close the gap" between formal provisions and actual implementation.

Proper implementation and effective enforcement create an obvious challenge in countries where the required human and financial resources are in short supply. Overall, shareholder suits are rare or non-existent, and actions taken by regulators, stock exchanges and other relevant bodies not common or effective enough. Improved enforcement will require broad reform to improve the performance of the judiciary, empower securities regulators while preserving accountability, and increase the effectiveness of self-regulatory bodies. Enforcement and implementation will also be enhanced by a clear and functional distribution of powers among authorities and greater consistency, clarity and predictability in the legal and regulatory framework. Most important of all, legal and regulatory measures must be based on reality of the resources available for enforcement.

Some countries are also considering greater use of private actions, such as derivative and class action lawsuits, to make it easier for shareholders to receive redress for violation of their rights. The Asian White Paper discusses ways to introduce responsible class actions. More generally, each White Paper discusses mechanisms that encourage market discipline and "self-enforcement" that can provide alternative options within a weak judicial and regulatory framework.

Although a number of features advocated by the *Principles* require action by boards, investors and others, there is also an important role for governments to play with respect to improving the framework for enforcement. For example, boards will usually be able to adopt a structure consistent with effective supervision of management and effective accountability to shareholders. However, desirable features such as cooperation between investors and protection of minority shareholders may depend to a great extent on government action to remove regulatory barriers and to enforce rights. In addition, private actions alone might not lead to desirable corporate governance practices. Where management is entrenched and capital markets are weak, for example, boards may continue to avoid their responsibilities unless the authorities take remedial action.

The *Principles* offer broad guidance for governments to follow when reviewing whether their corporate governance framework is compatible with establishing the corporate governance they want.

Policymakers are encouraged to develop the governance framework with a view to its impact on overall economic performance, market integrity and the incentives it creates for market participants and the promotion of transparent and efficient markets. This should help improve implementation and enforcement, reduce the risk of costly over-regulation and minimise the unintended consequences of policy measures. To underpin market integrity, the legal and regulatory requirements that affect corporate governance practices should be consistent with the rule of law, transparent and enforceable.

The *Principles* also cover the types of mechanisms that should be established for parties to protect their rights. Supervisory, regulatory and enforcement authorities should have the authority, integrity and resources to fulfil their duties in a professional and objective manner. However, where institutional resources are constrained, the legal and regulatory requirements could be adjusted. For example, where courts are weak, more reliance might have to be placed on other mechanisms to protect shareholder rights such as low shareholding thresholds for calling meetings and proposing board members or high voting thresholds for major decisions and pre-emptive rights that are less burdensome to enforce. Rulings should be timely, transparent and fully explained.

What do the Roundtables and *Principles* say about minority shareholder protection?

Across the five Roundtable regions there is a high degree of concentrated ownership and control in individual companies or groups of companies. While concentrated ownership is often seen as the solution to the fundamental principal/agent problem of corporate governance, in the absence of a credible legal and regulatory framework, the expected gains may not be realised. This is especially true when control is exercised through control pyramids and cross-holdings, which lead to a separation of cash rights and voting rights. This is often aggravated by insufficient information about ultimate ownership and the use of opaque control structures. The potential problems that arise from this combination of concentrated ownership, weak shareholder protection and insufficient disclosure has been highlighted in all the Regional Roundtables.

When minority shareholder protection is inadequate, controlling shareholders may extract *private benefits* from the company. For the individual, the private benefits of control might be substantial but at significant macro cost such as crises and country risk premium thus delaying financial market development. . At the micro level, not only the minority shareholders are harmed, but also the companies' access to capital is limited. Therefore, a poor corporate governance environment will ultimately cost the controlling shareholder, making it difficult to manage succession.

The *Principles* emphasise the need to protect minority shareholders, most notably where there are controlling shareholders whose interests might diverge from those of the others. This is particularly a source of concern in jurisdictions where the legal and regulatory framework for minority protection is weak. The *Principles* reaffirm that it is reasonable for investors to expect that the abuse of insider power, including by controlling shareholders, be prohibited. In cases where such abuses are not specifically forbidden by legislation or where enforcement is not effective, the *Principles* call on policymakers to consider the economic costs involved and to fill such gaps.

Perhaps the most important problem that follows directly from the combination of concentrated ownership, opaque control structures, weak minority protection, and insufficient disclosure is the frequent abuse of related party transactions. Curbing such transactions is one of the top priorities for corporate governance reform across the five Roundtables and a prerequisite for attracting minority investors on a long-term basis.

The Roundtables discussed in some depth the appropriate regime for related party and major transactions. The White Papers call for significant improvements in disclosure of related party transactions--particularly the identity of related parties and their material interests in the transaction--and recommend direct shareholder approval of major transactions, expanded appraisal rights, pre-emptive rights with respect to capital increases, and other mechanisms that can deter abusive transactions. Similarly, the Roundtables also discussed the board's role in these transactions, and the importance of having independent directors in a position where they can evaluate, and when necessary block, related party transactions.

Due to the importance for the market to know whether the company is run with due regard to the interests of all its investors, the *Principles* state that it is essential for the company to fully disclose any material related party transactions. Such transactions are typically between the company and entities in which it or its management have an interest, or with significant shareholders, including their close relatives and associates. The *Principles* call for the beneficiary of such a transaction to be obliged to inform the board, which in turn should make a disclosure to the market. This should not, however, absolve the firm from maintaining its own monitoring.

While most controlling shareholders are individuals or families, in many cases the state remains a major owner of commercial assets in spite of extensive privatisation over the last ten years. Both continuing state ownership and the legacy of privatisation present significant corporate governance challenges, especially improving the governance of still state owned firms, and protecting minority shareholders in partially privatised ones. The ownership function of the state in companies where it is a shareholder has yet to be fully resolved, even after taking into account the beneficial effects of partial privatisation, which in many countries has opened the way to unprecedented restructuring initiatives and increased exposure to competition from private entities. The OECD Working Group on

Privatisation and Corporate Governance of State-Owned Enterprises is developing a set of Guidelines that, once completed in 2005, should allow countries to better benchmark the ownership functions of the state. This work is subject to an open consultation process.

How to strengthen the ownership role of shareholders?

In some Roundtable countries, improving shareholder protection requires better protection for basic rights, like the right to secure share ownership, or to attend and participate in the general shareholders meeting. In other countries, these basic rights are protected, but full shareholder participation still faces various barriers. These barriers are particularly high for shareholders, including foreign ones, who would like to vote by proxy.

In many cases, shareholders could do more to improve the governance of the companies they own. Some controlling shareholders have experienced large increases in valuation, and personal wealth, after taking voluntary steps to improve corporate governance. Institutions that allow controlling shareholders to credibly signal improved governance, such as special stock market tiers, can facilitate this process. As pension funds, foreign funds, and other institutional investors gain prominence in many markets, they should also take a more prominent role in the governance of the companies they invest in.

With respect to exercising ownership rights, the *Principles* advocate that shareholders should have the right to remove board members and to participate in nominating them. Shareholders should be able to ask questions of the board at the general meeting and to place items on the agenda, something that is often effectively denied. The *Principles* call for the board to formulate and disclose a remuneration policy for board members and key executives, highlighting the link between remuneration and performance. Shareholders should be able to make their views known about this policy and any equity component, such as share options, should be subject to their approval.

Even for institutional investors, the informed use of ownership rights is costly. In many instances, institutional investors feel that their stakes in individual companies are not large enough to justify these costs and prudential considerations go against holding more shares. To overcome this situation, the *Principles* recommend that the authorities allow or even encourage institutions (and other shareholders) to co-operate and co-ordinate their actions. However, there is an important caveat that such co-operation is not aimed at manipulating the market or obtaining control of the company without going through accepted takeover procedures. Better co-ordination in nominating and electing board members, placing proposals on the agenda and holding discussions directly with a company are all welcome as valid methods of improving corporate governance.

The *Principles* take the view that the costs of effective ownership can and should be reduced. One way of doing so is for countries to lift unnecessary regulatory barriers to a continuing dialogue between investors and companies. At the same time, recognising that such close relations can degenerate into abuses, particularly in situations where there are inherent conflicts of interest, the *Principles* recommend that general disclosure of information to the market should remain the practice. Any additional information released by a company to institutional investors should be aimed at helping them understand the background to such information.

How do the Roundtables and *Principles* deal with conflicts of interest?

An effective corporate governance framework needs to be backed by effective ways to ensure the integrity of those such as financial analysts, brokers and rating agencies that provide information or advice which could influence investors' decisions. This is necessary since there have often been close relationships between service providers and their client companies which introduce conflict of interests.

Debt is frequently the principal source of external finance for companies in the Roundtable regions, but poor protection of creditors' rights and an aversion to exercise bankruptcy procedures limit access to normal commercial loans in many countries and raises costs. Effectively restricting abusive transactions and enforcing loan agreements would enhance creditor protection and facilitate access to commercial loans, with the overall goal to not only protect creditor rights after insolvency but also to facilitate risk management and ensure fair treatment of creditors before insolvency.

The *Principles* state that the corporate governance framework should be complemented by an effective, efficient insolvency framework and by effective enforcement of creditor rights. Especially in emerging markets, creditors are a key stakeholder and the terms, volume and type of credit extended to firms will depend very much on their rights and enforceability. Companies with good corporate governance are often able to borrow larger sums and on more favourable terms than those with poor records or which operate in non-transparent markets.

In many of the Roundtable countries, banks have ownership structures and other features that may create conflicts of interest and undermine their own governance, as well as their role as monitors; for example the same owner may control both the lending bank and the borrowing company. This can lead to related lending that harms the banks' minority shareholders, in many cases its depositors, and ultimately the government, which usually offers explicit or implicit deposit insurance. When borrowing companies do not own banks, the state frequently does, which presents its own challenges in terms of soft lending. Fortunately, banking reform is advanced in many countries.

One of the most striking lessons of recent years is that conflicts of interest are widespread and can often lead to behaviour detrimental to shareholders, investors and stakeholders. Since conflicts of interest take many different forms they are dealt with in several different sections of the *Principles*. As a general approach, the

Principles advocate both full disclosure and an explanation by the parties involved as to how the conflict of interest is being managed.

Managing conflicts of interest is particularly important with respect to external auditors, whose independence is crucial for financial market integrity. Given the potential limits of self-regulation, various regimes to ensure auditor independence have been developed in Roundtable countries. Roundtable participants felt that while self-regulation should be improved, the clear limits of self-regulation warranted more effective government oversight. There was widespread support for better disclosure of the relationship between the company and the external auditor, including the specific contract, fees, and other services provided by the audit firm. Beyond this, some countries, including Brazil, have acquired mandatory rotation of the audit firm, and limits on the non-audit services the audit firm can provide. Increasing the effective liability of auditors is also clearly a priority.

The *Principles* support the Principles of Auditor Oversight issued by the International Organisation of Securities Commissions (IOSCO) in 2002. These recommend creating a body, acting in the public interest, to provide oversight of the quality and implementation of audits. The *OECD Principles* recognise the importance of recent provisions introduced by many countries to deal with the skewed incentive structure that arises when the external auditor provides non-audit services or when they might be involved in auditing their own work. Managing the relationship with the external auditor so as to ensure a high quality independent audit is also identified by the *Principles* as a key duty of the board.

How do the Roundtables and *Principles* seek to strengthen company oversight by boards?

The company board serves as the fulcrum that balances the ownership rights enjoyed by shareholders with the discretion granted to managers. Good corporate governance requires that the board, whatever its structure, focus on long-term issues, such as assessing corporate strategy, and activities that might involve a change in the nature and direction of the company, rather than taking on day-to-day operational responsibilities. However, boards as a whole and their individual members must have clearly-defined incentives and duties to ensure that the board effectively exercises its functions.

Roundtable participants described most company boards as either passive "rubber stamps" or as active participants in furthering the interest of only the controlling shareholder. While countries have established the legal duties of board members to exercise care and act in the interest of the company and *all* shareholders in each region--though the origin and exact nature of board members' duties vary across countries--these legal requirements often have limited influence on actual board practices. This reflects both concentrated ownership and the limitations of the judicial system: many countries participating in the Roundtables have never had a successful suit filed by minority shareholders against a board member.

One widespread response is mandating greater use of "independent" board members. The definition of "independence" varies, but increasingly includes independence from the controlling shareholder. For these mandates to be truly effective, however, the pool of potential independent directors capable of exercising informed and objective judgment needs to expand substantially in a number of countries. In some countries, institutions offering board member training have emerged to facilitate this process.

Beyond requiring that certain board members be independent, there has been great interest in having a certain portion of the board chosen more directly by minority shareholders. The main method suggested for doing this is cumulative voting. While some Roundtable participants supported the possibility for cumulative voting, others were concerned that it reinforced the notion that board members should act as "delegates" of certain groups. And the system is extremely complex in practice with outcomes that are not entirely clear cut. Board members that represent all shareholders, not just some, will better serve the company and its shareholders' overall interests. As the role of independent board members increases, greater attention will also have to be paid to their nomination, remuneration, and replacement.

Board structures vary across countries, with some countries having unitary board, others having supervisory boards, and many having complementary company organs, such as boards of "statutory auditors". Outside of committees of executive board members, specialised committees are only widely used in some of the countries that participated in the Roundtables. However, the Roundtables supported much greater use of committees, especially audit committees, that can allow independent board members to oversee the company's disclosure practices and evaluate the fairness of related party transactions.

The *Principles* specify clearly defined responsibilities for the board, that include establishing a code of corporate ethics, ensuring compliance with laws and standards, and oversight of internal control systems for financial reporting. The board should also be responsible for formulating and disclosing a remuneration policy that highlights the link between remuneration and performance for key executives and board members. Many countries now regard as best practice the creation of a remuneration committee with independent directors.

Since the board and its members have a fiduciary duty to the company and all its shareholders, the *Principles* embrace a general notion of board independence and objectivity, rather than referring simply to independence from management. When a company is part of a group, the board's duty is to the company, not the group. Boards should review related party transactions using independent board members and provide confidential access for whistleblowers who may be in a position to identify unethical conduct and abusive transactions. Although board committees for tasks such as audit, remuneration and nomination have spread in the past few years, the underlying concepts are not always well understood and committees often serve quite different roles in different companies. To avoid confusion and to inform investors, the *Principles* advocate that the composition, mandate and remit of committees be clearly defined and fully disclosed.

How was the review of the *Principles* carried out?

OECD ministers in 2002 called for an assessment of the OECD Principles by 2004, a year earlier than previously intended, in the wake of a series of corporate scandals that had undermined confidence in the integrity of corporations, financial institutions and markets. To support this work, the ministers requested a survey of corporate governance developments in OECD countries with a view to identifying lessons to be learned and possible implications for the *Principles*.

The assessment was carried out under the responsibility of the OECD Steering Group on Corporate Governance with the active participation of observers from key international institutions, including the Bank for International Settlement, International Monetary Fund, World Bank, Financial Stability Forum, International Organisation of Securities Commissions and the Basel Committee. Leading business and labour representatives, including the OECD's Business Industry Advisory Committee and the Trade Union Advisory Committee also participated in the Steering Group's meetings on an ad-hoc basis.

The Steering Group sent a questionnaire to member countries requesting information about corporate governance issues, the forces at work and proposed policy measures. The responses, together with a review of practices in member countries by the OECD formed the basis of the *Corporate Governance: A Survey of Developments in OECD Countries* and informed the discussions of the Steering Group.

In addition to the input from non-member countries mentioned at the beginning of this article, the assessment process also included extensive consultations with the private sector, labour and civil society at large. Three major consultative meetings with broad participation were held in conjunction with the Steering Group meetings. In addition, the OECD Secretary General convened two informal roundtable meetings with senior representatives from key international organisations, business and labour.

In January 2004 a draft of the revised principles was posted on the Internet for comments from the general public. Some 75 submissions were received from private individuals, professional associations, business and trade unions and, where permission was given, they were posted on the OECD website for public access.

What happens next?

The *Principles* should be considered a living document. It is an OECD priority to make sure that they are widely disseminated and actively used. This will include a continuing policy-dialogue where policy-makers, regulators and standard setters will be able to exchange practical experience of implementing the *Principles*. The OECD will also continue to monitor developments and identify new trends and challenges that deserve attention. As an important part of future work, the OECD will host an international multi-stakeholder dialogue on corporate governance. This dialogue among corporations, investors, service providers, labour and others will be as inclusive as possible and provide an important opportunity to ensure that the *Principles* remain relevant and are actively used in the private sector. Beyond the *Principles*, once the Guidelines for Corporate Governance of State Owned Enterprises are agreed they will also become an aspect of the dialogue.

As for non-OECD countries, the next stage of the Regional Roundtable process is already underway. In the case of the Russian Roundtable, the participants have agreed to create two ad hoc Task Forces to examine policy options in two priority areas: the transition towards internationally recognised financial reporting standards, and problems arising from related party transactions, transparency of beneficial ownership and control. The Asian, Latin American and Southeast Europe Roundtables will also focus on implementation and enforcement of White Paper recommendations. The Eurasian Roundtable has issued a Comparative Overview of corporate governance in the region, containing priorities for further action to be pursued in the follow-up phase.

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The full text of the Principles can be obtained in pdf format from our website:

www.oecd.org/daf/corporate/principles/

Experiences from the Regional Corporate Governance Roundtables:

www.oecd.org/daf/corporate-affairs/

OECD Guidelines for Multinational Enterprises:

www.oecd.org/daf/investment/guidelines

BIOGRAPHICAL INFORMATION

Ms Fianna JESOVER, Corporate Governance Specialist, Corporate Affairs Division, OECD Directorate for Financial and Enterprise Affairs

Since 1996, Fianna Jesover works in the OECD primarily on outreach activities. Over the past six years she has helped promote sound corporate governance practices around the world. She manages the Russian Corporate Governance Roundtable and was the principal author of the White Paper on Corporate Governance. She is initiating work on corporate governance of non-listed companies. Ms. Jesover contributed to the recent review of the OECD Principles of Corporate Governance. She has published articles on corporate governance policies and participates in international conferences on the subject. From 1993-1996, she was a trade specialist in the US government.

Mr. Grant KIRKPATRICK, PhD (Christian Albrecht University, Germany), Senior Corporate Governance Specialist, Corporate Affairs Division, OECD Directorate for Financial and Enterprise Affairs

Mr. Kirkpatrick is presently Senior Economist in the Corporate Affairs Division of the OECD's Directorate for Financial and Enterprise Affairs where he has been responsible for overseeing the review of the Principles of Corporate Governance and in bringing into the review process the experience gained from the Regional Corporate Governance Roundtables organised in cooperation with the World Bank. He is currently responsible for monitoring developments in OECD countries and in analyzing implementation issues concerning the Principles.

Address:

OECD

2 rue Andre Pascal

75016 Paris France

[1] The views expressed in this paper are those of the authors and do not necessarily reflect the view of the OECD or its member countries.