

CORPORATE GOVERNANCE IN VENEZUELA

Promoting an agenda based on ethics, transparency and accountability



Good Corporate Governance as a mean to implement effective processes in the administration, structures and functioning of government institutions, for the benefit of citizens

State-Owned Enterprises

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“.....Taking into account the two challenges faced now by the Member Countries to overcome the internal social gap and facilitate an effective and inclusive international insertion, the efforts made to promote a sound development agenda, focused on productivity, competitiveness and sustainability,.....We invite the sub region companies to adopt the "Andean Code of Corporate Government" prepared by the Andean Development Corporation for the application of good government practices. It constitutes a vital instrument for the development, competitiveness and efficiency of the business sectors of our countries.....”

The Presidents of Bolivia, Colombia, Ecuador, Peru and Venezuela, gathered in the city of Quito, Republic of Ecuador, on the occasion of the XV Andean Presidential Council. July, 12 2004.

Introduction

In the Venezuelan Association of Executives, AVE, (www.ave.org.ve), ever since our foundation in 1957, more than 45 years ago, we have maintained our commitment of serving as a national reference in corporate and management practices based on our local realities.

During the last few years, despite going through very difficult circumstances in our country, we have assumed the responsibility of sending a message to society, to our government, to regional governments (both andean and latinamericans), and to the rest of the international community: the message that the management and business sector in Venezuela are contributing to the country's development with analysis and constant evaluation of the best management and business practices.

We are aware of our role in society, being a point of encounter of the public and private management sectors by promoting the best business practices based on inclusion, ethics and transparency.

We are promoting Corporate Governance in our country since the year 2000, both locally and internationally, through our Corporate Governance Comittee, (www.ave.org.ve/comitegc) created under our Board's comitement, and counting with the participation of representatives of the banking sector, small and medium enterprises, big companies which participate in the stock markets, the family enterprise and the regulatory agencies of our country, mainly the National Stock Commission (Comisión Nacional de Valores).

In the international scene we participated as members of the Latinamerican Regional Roundtables that led to the creation of the "White Paper on Corporate Governance for Latin America" produced by the Organisation for Economic Cooperation and Development (OECD) (www.oecd.org), and we also play as the Venezuelan counterpart of the Andean Project of Corporate Governance led by the Andean Finance Corporation (Corporación Andina de Fomento) (www.caf.org) which also led to the production of a material known as the "Guidelines for an Andean Corporate Governance Code".

In the local aspect, we lead the Corporate Governance chapter of the National Competitiveness Network promoted by the National Commission for the Promotion of

Investments, CONAPRI (www.conapri.org) as members of this institution. We also have constructed many alliances through our committee, and have also done research and compilation of the Venezuelan regulation regarding Corporate Governance.

As members of the Advisory Council to the National Stock Commission (CNV), which is an institution created to enhance the markets development and for the approval of Corporate Governance rules, we participated in the production of an agreement of self regulation of corporate governance rules with the offering companies, officially published in the National Gazette No. 37.286, of february 17th, 2005.

This activity was operational under the focus made on the large capital market companies, but due to our local circumstances, we have pointed our interest towards non listed companies, small and medium enterprises (SME's), aswell as state owned enterprises.

In the SME's sector¹ as partner of the Venezuelan Confederation of Industries CONINDUSTRIA (www.conindustria.com), an institution that represents the small and medium entrepreneurs in our country, we have analyzed the application of corporate governance principles in this area. We have also analyzed it under the context of the guidelines for the democratization of capitals and legitimation of markets, in benefit of the economic and social actors, proposed by the National Stock Commission, where the state owned enterprises play a key role.

State owned enterprises have always played a key role when studying the enterprise figure, because of the immense space that occupies in the Venezuelan company sector.

To explore the importance, problems and tendencies of state owned enterprises in Venezuela is our main goal, and to place a good point of view of what role can Corporate Governance can be in our local and regional situation.

For AVE, every organisation no matter its composition, size, ends or goals, will all be more competitive when applying good Corporate Governance practices.

¹ Beyond Capital Markets: Corporate Governance for non-listed companies / S.De Paola march 2005/ Paper produced for the OECD, International Meeting of Non-listed Companies, 19-20 april, Istanbul, Turkey.

State owned Enterprises in Venezuela

It is well known news that Venezuela is struggling through a very deep institutional and social crisis. In such conditions, it would seem obvious to assume the fact that subjects such as Corporate Governance would be put aside in the priority scales of our country. However, we do live in a world where globalization grows in importance in a day to day basis, and concepts of such importance cannot be left unnoticed in Venezuela, for its insertion in the global economy.

The last twenty years of the past century were marked by a clear sign of privatization of state owned enterprises in the western world. In some cases these companies were well managed and other were not so well managed. Now, in the first years of the present century, we observe a series of opinions (and specially in Latin America) against globalization, and of course privatizations.

The OECD Guidelines on Corporate Governance of State-Owned Enterprises (April, 2005. The first international initiative towards helping governments with the corporate practices of the companies) were made under such context.

The credibility and transparency of governments have been seriously damaged by the corruption scandals, creating a negative perspective towards the political sector which clearly undermines the confidence in democratic systems.

The establishment of Corporate Governance practices, not only in the public commercial sector, but in the government area itself either or both national and local levels, will generate without a doubt more stability to democratic governments.

At the same time we sense a growing interest in the business sector of everything related to Corporate Governance as an alternative for growth, expansion and enhancement of business, that is why the Venezuelan Association of Executives consider of great importance the global thrust given to this subject in order to apply it to the Venezuelan culture.

One of the lessons learned from our international experience is that these principles and guidelines should not be applied as received and known. They must undergo an adaptation process to every region in order to suit in every countries necessities.

We sustain the idea that the principal challenge for Latin American countries, and particularly for Venezuela, is the designing of long term economic policies, previously negotiated with the different components of our society, and one of those policies without a doubt is the adaptation of our markets and organizations to the international standards in order to achieve a greater competitiveness. For that it is imperative to develop aspects such as "Corporate Governance for State Owned Enterprises".

State owned Enterprises in Venezuela Relevance

State-owned enterprises has always played a key role in the analysis and study of the company sector. This would sound evident if assumed the fact that the Venezuelan Administration has always shown its interest in participating in the economy. It is not strange to admit that the Administration conducts the economic path of the country, since it occupies a large portion in the entrepreneurial map in Venezuela.

This behavior responds to a series of factors that led the intervention of the Venezuelan Administration in the economy. Ever since the birth of the industrial sector in our country, in the beginning of the XX century, the Administration has always shown its interest in occupying large spaces in the area, with the creation of different organizations with productive means such as Banco Obrero and Banco Agrícola in 1928.

Throughout the following years, this interest will grow, and will reach it's peak by 1974 and 1975 with the nationalization of the oil industry. This obviously determines an ample participation of the State in economic sector of the country. Such affirmation is made knowing the fact that the oil industry is without a doubt the largest in the country. It represents almost 18% of the country's Gross Domestic Product GDP.

Gross Domestic Product (GDP)² (in millions of Venezuelan Bolivares)			
Year	Total	Oil Industry	Percentage
2004	42.035.809	7.225.472	17,1
2003	35.667.526	6.472.229	18,1
2002	38.650.110	6.595.672	17,0
2001	42.405.381	7.688.643	18,1
2000	41.013.293	7.757.605	18,9

In this context, Venezuela implemented a social market economy characterized by the right of freedom of economic activity, but limited by a considerable intervention by the State. This intervention is materialized in the creation of numerous state owed enterprises. However, this tendency of the State occupying more and more spaces in the country's economy has been overturned in many times, into privatization processes. As an example, the rounds of "Apertura Petrolera", in which an opening process of the oil industry was underway.

Moreover, in the middle 90's, the structure of the state itself was modified, with the only end of making it more effective and efficient. This process was initiated under two main subjects: The decentralization and the privatization.

With the first one, many aspects that where in the sphere of decision of the Central State, would now be translated to different levels of Government (State and Counties), this would derive in a complex network of institutions that would favor the country's development. In

² Source: Venezuelan Central Bank. (www.bcv.org.ve)

the other hand, privatization was conceived to open spaces for the intervention of private investment, and to relieve the State of numerous activities that were appointed to it in the last few years. Both were partially executed.

With the new constitution of 1999, this process is overturned and, new interventions were produced, caused not only because of the State's ambitions but also due to constitutional mandates. This certainly produced the creation of numerous state owned enterprises that participate in the economy as another player, competing with the private sector.

There lies the importance of state owned enterprise, because of the often use of State owned enterprises in order to achieve all the public services appointed by the Constitution.

At the present time, the tendency is to observe the growth of State Owned enterprises, an to this date we count with 95 state owned enterprises approximately. This organization form an area of great importance in the conformation of the country's GDP, which is the public sector. It is of such importance that in the year 2004, the public sector represented around 30% of the GDP, which denotes the real dimension of the State, and this helps to determine the necessity of a good management in the companies and organization that forms it.

Gross Domestic Product (GDP)³ (in millions of Venezuelan Bolívares)			
Year	Total	Public Sector	Percentage
2004	2.035.809	2.767.513	30,37
2003	5.667.526	1.335.299	31,7
2002	8.650.110	1.474.127	29,68
2001	2.405.381	2.907.820	30,43
2000	1.013.293	2.983.067	31,65

Facts and Tendencies

In many times state owned enterprises has been a subject of analysis, what is its nature, and ideal means and ends. There is clearly no unanimous position in this debate. Nonetheless in Ave, we have an open and general perspective on the subject, and if we are referring to State owned enterprises we are referring to a wide concept no matter its size, or ends. This conception is inspired in the fact that we believe that Corporate Governance is a set of rules applicable to any form of organization regardless of it composition.

In Venezuela, after the passing of the two recent constitutions (1961 and 1999) the tendency (and even more so in the constitution of 1999) has pointed to the creation of state owned enterprises under the form of a company, but also using other types of organization. As an evident result of this actions, we now count with a wide fleet of state owned companies, through which various commercial and non commercial activities are developed.

³ Source: Venezuelan Central Bank. (www.bcv.org.ve)

Recent policies implemented by the Government, reveal a clear strategy and may define a tendency as far as organization and development process is concern. One of them, perhaps the most significant is produced in the hydrocarbons field, often using not only normal companies, but mixed companies. We analyze the Hydrocarbons law of 2001. Such piece of legislation states that the exploration and extraction activities of all hydrocarbons will be done by the State, but the could be made through state owned enterprises in which the State maintains at least 51% of the equity capital, these are the mixed companies. An specific scenario of this forms can be seen in the enterprises that operate in the "Faja del Orinoco", where at the present date operates approximately 22 foreign companies, in the exploration and extraction activities. Now, according to the said legislation, this companies are to be held under the form of mixed companies. In order to do so, the State must invest a large amount of resources in order to fulfill the law's mandate, in the end it would become the great owner not only of the hydrocarbons, but also of the means of exploration and extraction. At the present time, 8 of the companies operate under such figure, and it is expect that all of the 22 companies assume this structure by the end of 2006.

Another policy that reveals a tendency is of recent development and consists in the application of combined management, and self management companies, involving of course the participation of the labor force of the company in its managing structure. Several pieces of legislation that includes this concepts are being discussed in the legislative branch (National Assembly).

Knowing the evolution of the Venezuelan industries and observing the recent tendencies, it is a clear fact that Corporate Governance rules are of great importance for these structures not only because it would obviously benefit every organization that applies them, but also because these public enterprises can provide a benefit that can go beyond it's particular interest. By applying this principles and guidelines to the state owned enterprises, would produce enormous benefits to the community because they will be able to offer a better service to the population.

Corporate Governance if applied to the State as a whole and not only to their commercial structure favors no only the performance of its management but also projects an image con confidence and transparency in both the domestic and foreign community.

Local and Regional scenario

As we live in a global world, the global concepts that arise in our times require a certain degree of development and evolution. Being Corporate Governance one of those concepts, it is no different than other alike. It is clearly evidenced that international organizations that lead the initiative of it promotion, mainly the OECD, is to diverse its scale and objectives to subjects and aspects that go beyond the general principles

Recently in April 2005, the OECD presented a series of principles and guidelines of Corporate Governance for State Owned enterprise, after holding significant space for discussion and comments.

This tendency is not only observed on international organizations, it also reaches the national grounds, both public and private. Every organization is looking after the guidelines

that suits better its business. That is why a deeper analysis and diversifications is required. It is obvious that Corporate Governance has a growing interest, but it will evidently be more attractive if it is found a way to specified in order to be more suitable for every kind of organization.

Venezuela is not the exception of this problems, and nowadays AVE is undergoing a series of studies in order to achieve a level of understanding and to produce an attractive scenery for investors in future times. AVE leads for more than 3 years every initiative of promotion and diffusion of Corporate Governance in our country, as we have identified it as a competitiveness factor in our community in order to enhance and improve the business community. This is a process of creating culture. We are creating a culture of good governance, culture based on ethics, transparency and will, and that can only be achieved with the commitment of every organization and person that participates in this process.

Along with the Andean Finance Corporation (CAF) and the National Stock Commission (CNV), we are developing different measure in order to promote Corporate Governance as a whole. We participate in the makings of seminars, congresses and forums that can help to spread the knowledge of this principles. Our tendency has always been to observe Corporate Governance as a whole, but due to our local realities and scenarios we have paid special attention to non listed companies and State Owned enterprise.

We believe that this approach is similar to those that can be made in other similar countries. Many countries are under a serious plan of privatization, and the application of Corporate Governance is recommended for that process. We observe with great interest the situation of ECOPETROL S.A., which is the Colombian oil company which Board recently announced the adoption of a Corporate Governance Code. The initiative of the OECD guidelines would obviously help such projects because it would make more suitable the transition to competitive open markets, and to meet the necessary standards that are required in such scenarios.

In Venezuela the state owned enterprises operate around the gas, mining and oil sector, mainly because it is the tradition. Companies such as ALCASA and VENALUM, electric companies such as CADAFE and certainly Petróleos de Venezuela PDVSA, represent the wide variety of state owned enterprises in our country.

For this group, the adoption of good corporate governance guidelines will depend on the context of public policy in which they operate, because that is where the strategic interest are determined, however we maintain that such practices can add value in terms of transparency, trust, and credibility in order to achieve the necessary success in politics.

The Voice of local Players

“The National Stock Commission has initiated a program consisting in the promotion of capital markets, with the prospect of including not only active sectors of the economy but also other numerous actors in the dealing activities typical of capital markets; all of this under the parameters set by the President in the Strategic Plan of the Nation, in which is highlighted the aspect referred to as “Democratization of Capital”

Among those initiatives adopted for the markets development, we can count with the enhancement of the institutions and the activity as a whole, through accepted practices of management and direction in the publicly held companies through the adoption of Corporate Governance principles, and general principles and not abiding rules, combined with an education process which tries to explain the benefits of its application, not

only on local basis but on international grounds, once the investor can select where it wants to invest, having more confidence in those that operate with these principles. (materialization of the social control).

The way in which these principles are conceived, makes possible the application in every company that wishes to invest in capital markets, from small and medium sized ones, to those large ones that are publicly held by the State, if the political guidelines are followed for entering in open markets.

The National Stock Commission has adopted such principles as they are identified as an effective tool for achieving transparency in the companies management, and this will certainly cause more competitiveness in all economic instances.”

Fernando De Candia
President National Stock Commission
(www.cnv.gov.ve)