



Corporate Governance in India: The IFC Perspective

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New Delhi, October 18, 2004



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important to IFC**

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*IFC's mission is to promote **sustainable** private sector investment in developing countries, helping to reduce poverty and improve people's lives*

Why Corporate Governance Matters for IFC

- **The trigger**
 - East Asian crisis
- **The re-confirmation**
 - Corporate scandals in America and Europe

Corporate Governance risk mitigation fits well with IFC's developmental role and commercial orientation

Why Corporate Governance Matters for IFC

- **De-risking the Investment.** As an investor, it is in IFC's interest to reduce the operational, environmental and social risk.
- **Mobilizing capital.** IFC's stamp of approval on a company's corporate governance practices leads to other investors deriving comfort. This contributes to the development of the public and private capital markets.
- **Enhancing value.** With all the risks mitigated, the company is sought after by investors, leading to improved valuations.

IFC is uniquely positioned to contribute in this area because of its presence / experience / participation in governance in all types of companies worldwide

What is IFC Doing about Corporate Governance?

- **Advocacy**

- Global Corporate Governance Forum
 - Secretariat to its Private Sector Advisory Group
- Co-organizers of OECD/WBG roundtables
 - uniquely positioned to bring investors, companies, intermediaries to the table

- **Direct Intervention**

- CG systematic part of appraisal/ supervision
 - CG evaluation methodology has been established
- Technical Assistance to clients before/after investments
- Qualified / trained IFC nominated directors on boards of investee companies

IFC is spreading awareness about corporate governance through non-investment work, as well as ensuring good corporate governance practices in its investments

**Why is CG
important to IFC**

**IFC's
methodology**

**IFC's experience
in India**

IFC CG Methodology

- Four principal paradigms
 - Public, listed companies
 - Private, family companies
 - Financial institutions
 - Privatized, transition economy companies
- 
- Relevant for
India

Each of these have a matrix, questionnaire and supporting materials

IFC Corporate Governance questionnaire is provided in Annex A

IFC CG Methodology

- Companies are evaluated on four criteria....
 - Commitment to good CG
 - Shareholder rights
 - Boards of Directors
 - Transparency and disclosure
- To achieve four levels of evolution
 - Level I: Acceptable CG practices
 - Level II: Extra steps to ensure good CG
 - Level III: Major contribution to improving CG nationally
 - Level IV: Leadership

Output = Corporate Governance Improvement Program whereby IFC advises companies to graduate to the next level and beyond

IFC Methodology

- IFC carries out comprehensive audit of the company as part of its appraisal process
- Improvement suggestions are provided based on deficiencies observed.
- Compliance with suggestions is ensured through covenants built into investment agreements

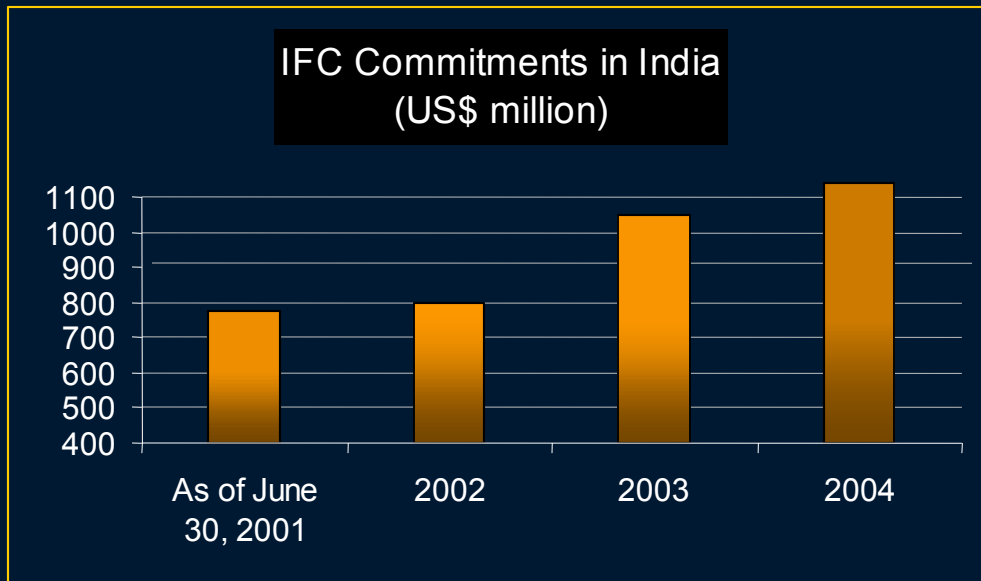
Over the last three years, we have seen a change in attitude of sponsors towards corporate governance improvements from initial reluctance to a realization of its importance and benefit now.

**Why is CG
important to IFC**

**IFC's
methodology**

**IFC's experience
in India**

IFC's business is growing in India



- India is IFC's second largest exposure after Brazil
- As a part of its appraisal, IFC is advising companies on implementing global best practices on
 - Technical and market issues
 - Environmental and social impact management
 - Corporate governance

IFC is encouraging companies to improve their corporate governance practices as part of their restructuring initiatives. IFC's CG audit plays a key role in companies being able to enter new market and forge new partnerships

Our sample size

- Since 2001, IFC has made investments in about 30 companies in India
- Prior to that, there were about 20 companies in the portfolio
- A sample size of about 50 companies to study the corporate governance practices

These companies represent the Indian corporate sector, and are well diversified in terms of size, sector, family owned and professionally managed

Key observations...

- **Most of the Indian companies are a hybrid of family owned and publicly listed companies**
 - Ownership and management are not segregated
 - Informality of governance policies and inadequate controls
 - Succession planning
- **Corporates need improvement on**
 - The constitution and functioning of the Board
 - Self dealings and regard for minority shareholder rights
 - Transparency and disclosure
- **Financial Institutions**
 - Could do with tighter norms than prescribed by RBI

Like any other emerging market, there is a lot of scope to improve the corporate governance practices of the corporate sector in India

Key Observations

Importance given by companies to the four criteria...

	Commitment to good CG	Minority Shareholder rights	Boards of Directors	Transparency and disclosure
Public, listed companies	***	**	**	**
Private, family companies	**	*	*	**
Financial institutions	***	**	***	**

*** Very Important

** Important

* Not so important

The diagnostic questionnaires are designed according to the importance of criteria vis-à-vis the type of company

IFC's value add...some examples

- **Corporates**

- **Minority shareholders protection rights**

- Advised a company on structuring a transfer pricing agreement to take care of related party transaction
- Ensured that the equity offer based on the market price of a stock is a true value
- Charge market based fee for guarantees provided to group companies

- **Transparency and disclosure**

- Insisted on change of auditors / implementation of IFRS accounting standards
- Improved reporting / disclosure norms
- Separated ownership from management: Appointment of professional management eg CFO

- **Constitution and functioning of the Board**

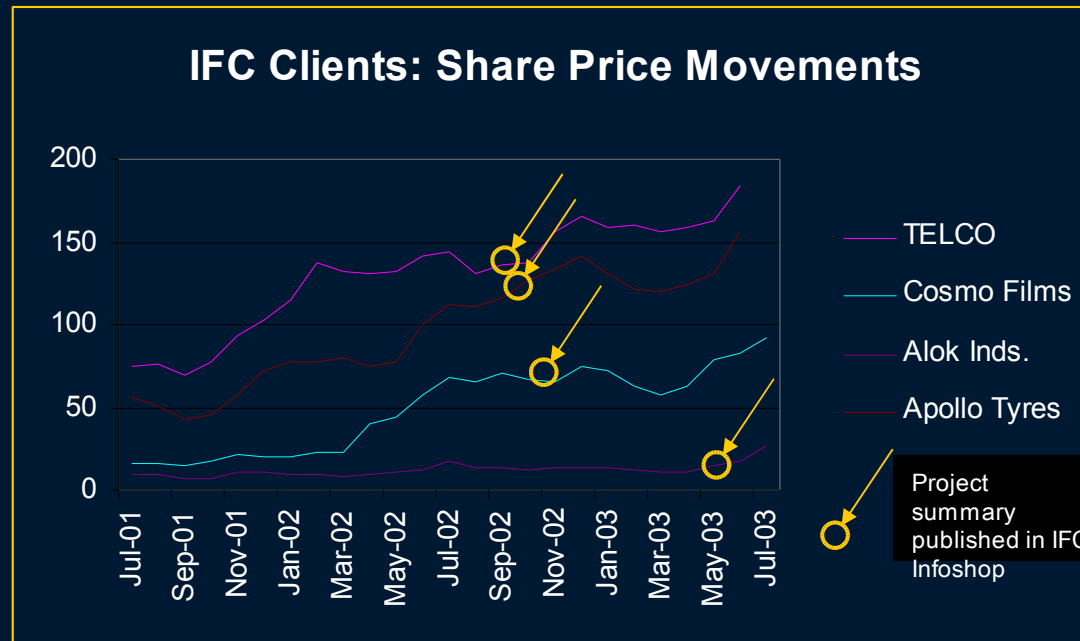
- Insisted on induction of independent directors / composition of audit committee by independent directors

- **Commitment to good corporate governance**

- Ensured appointment of a senior level staff to ensure implementation of good corporate governance practices in companies
- Reducing / eliminating cross holdings

IFC has built a track record of demonstrable benefits to companies. It has become easier to convince a willing client about the benefits of ensuring good corporate governance by quoting the above mentioned examples

The Reward: Stock Price Movements for IFC's Clients



Good corporate governance results in improved valuations for clients

Thank you

Annex A: IFC CG questionnaire

IFC Scorecard for Evaluating Corporate Governance (PUBLIC LISTED FIRMS)

1. Commitment to Corporate Governance (Section Weight - 10%)	Notes	Max. Score	Score
1 Does the company have a written corporate governance (CG) policy or manual? Does the Annual report outline steps for improving CG?		15	
2 Does the CG code or manual specify the major stakeholders, whose interests must be taken into account?		15	
3 Is the CG policy or manual easily available to the regulators and the general public in the case of a publicly listed company?		30	
4 Is there an identified officer of the company tasked with the responsibility of ensuring that the company follows their own CG policy or manual, and does this officer report directly to the compliance committee or other appropriate sub-committee of the Board?		40	
	Section Score	100	

IFC Scorecard for Evaluating Corporate Governance

(PUBLIC LISTED FIRMS)

2. Structure and Functioning of the Board (Section Weight - 30%)	Notes	Max. Score	Score
1 Does the Board have a sufficient number of independent directors? Are the board members qualified to discharge their duties? Do they dedicate enough time?		30	
2 Does the Board have a written code for the guidance of directors regarding their rights and duties, their prerogatives and responsibilities? Is there a Code of Ethics for the entire corporation?		10	
3 Does the Board have an Audit Committee, composed of independent directors, that chooses the external auditor, receives reports directly from the external auditor, oversees the work of the internal auditor, and makes sure that audit and Regulator's findings are duly and properly acted upon? Does the Board have actively functioning committees or sub-committees (compliance, nomination, compensation, risk management), composed mainly of independent directors?		30	
4 Is the Board provided with all relevant information, within sufficient time for study and analysis, to enable directors to exercise their duties of guiding corporate strategy, monitoring performance and providing oversight to top management? Are Board meetings held according to a regular schedule, agendas prepared in advance, minutes prepared and approved?		20	
5 Does the Board have a performance evaluation system to evaluate its own performance?		10	
Section Score		100	

IFC Scorecard for Evaluating Corporate Governance (PUBLIC LISTED FIRMS)

3. Minority Shareholder Rights (Section Weight - 30%)	Notes	Max. Score	Score
1 Are all shareholders treated equally for subscription rights or repurchases? - Can the company issue shares with varying voting rights (e.g. founder shares, non-voting shares, multiple voting rights, removable voting rights and options)? - Do all shareholders have the right to register and freely transfer shares?		20	
2 What is the history of the Company in dealing with the rights of minority shareholders? - Are shareholders allowed to participate and vote at shareholder meetings? - Are minority shareholders able to pool their votes for certain candidates to the board (e.g. through cumulative or block share voting)? - Are there provisions negotiated under shareholders agreements to protect minority shareholders or non-voting shareholders during changes of control?		20	
3 Are all shareholders given regular and adequate disclosure reports on time?		20	
4 Are the related party transactions governed by arms length principle? - Are there corporate guarantees provided to companies owned by the major shareholders? Does the company get a market based return on such guarantees? - Are the transactions between group companies (such as sales to group companies, loans and advances) based on prudent, commercial principles?		40	
Section Score		100	

IFC Scorecard for Evaluating Corporate Governance (PUBLIC LISTED FIRMS)

4. Transparency and Disclosure (Section Weight - 30%)	Notes	Max. Score	Score
1 Is an internationally recognized accounting and auditing system in place?		20	
2 Is the audit performed by a recognized national/international firm?		15	
3 Does the company publish meaningful quarterly reports, containing segment reporting as well as results per share, consistent with IAS form? Is there a detailed analysis of any deviation from previously announced earnings, targets and strategic goals?		20	
4 Does the Annual Report discuss the company's risk management system and its corporate governance practices?		5	
5 Is the company's annual financial statement published no later than 3 months and the quarterly report no later than 2 months after the end of the reporting period?		10	
6 Does the company's Annual Report contain information on significant cross shareholdings (say 5% or more)?		10	
7 Are conflicts of interest fully revealed through a clear and well-established mechanism, approved by the regulatory authorities? Are conflicts of interest disclosed due to the involvement of auditing firms in the provision of non-audit services to the company?		10	
8 Are all financial analysts treated equally regarding information dissemination (is there fair disclosure)? Are regular analyst meetings held (e.g. quarterly or semestrally)? Is this information, along with the financial calendar, readily and regularly available? Is it put on the internet?		10	
Section Score		100	
TOTAL SCORE			