



ORGANISATION  
FOR ECONOMIC  
CO-OPERATION  
AND DEVELOPMENT



# *THE 2007 MEETING OF THE LATIN AMERICAN CORPORATE GOVERNANCE ROUNDTABLE*

***10 - 11 OCTOBER 2007  
MEDELLÍN, COLOMBIA***

## **Code Report: the Andean Corporate Governance Code**

The OECD asked several consultants, regulators, corporate governance institutes and other relevant stakeholders to elaborate reports regarding the development and implementation of voluntary corporate governance codes in each of their countries/regions. The reports, as well as a synthesis report elaborated by the OECD Secretariat based upon them, is provided to the Roundtable participants as background for the meeting's discussion.

The Andean code report was developed by **IAAG Consultoría & Corporate Finance**, a Spanish consultancy firm and the code's author, with collaboration of the OECD Secretariat. For any comment or specification regarding the report, please contact Paola Gutierrez at: [pgutierrez@iaag.com](mailto:pgutierrez@iaag.com)

Further information regarding the code as well as its integral text can be found at:  
<http://www.iaag.com/>

Copyright © OECD 2007, All rights reserved

Corporate Affairs Division, Directorate for Financial and Enterprise Affairs  
Organisation for Economic Co-operation and Development  
2 rue André-Pascal, Paris 75116, France  
<http://www.oecd.org/daf/corporate-affairs/>

## OUTCOMES FOR A CORPORATE GOVERNANCE ANDEAN CODE

### I. INTRODUCTION

The Outcomes for a Corporate Governance Andean Code (Lineamientos para un Código Andino de Gobierno Corporativo) (the Code or LCAGC hereinafter) provides a Corporate Governance framework for the five Andean countries (Bolivia, Colombia, Ecuador, Peru and Venezuela).

The Code is the most visible product of a Corporate Governance Project, financed in 2003 by the Corporación Andina de Fomento - CAF, which was divided into three main stages:

**Stage 1: Domestic Legal and Regulatory Framework Assessment**

**Stage 2: Development of the LCGAC**

**Stage 3: Implementation in a selected company per country**

The Project was conducted by the Spanish Firm IAAG Consultoría & Corporate Finance S.A. ([www.iaag.com](http://www.iaag.com)), and it involved well recognized counterparts in the five countries of the Andean Region.

On behalf IAAG, the Corporate Governance Team of IAAG was composed by:

- D. Juan José Fernández-Armesto, Project Supervisor.
- D. Alfredo Ibargüen, Director of the Project.
- D. Javier Zapata, Corporate Governance Expert and Lawyer.
- D. José Gómez-Zorrilla, Corporate Governance Expert. Lawyer and Economist.
- D. Jaime Hergueta. Engineer
- D. Miguel Vela, Communications Expert

The counter-parts of each one of the countries of the Andean Region were the following ones:

- **Bolivia:** Bolivian Stock Exchange; Mr. Armando Álvarez and Miss. Sandra Serrate; Mr. Nabil Miguel.
- **Colombia:** Confecámaras; Mr. Eugenio Marulanda, Mr. Andrés Bernal and Miss. Paola Gutiérrez.
- **Ecuador:** Stock Exchange of Quito; Mr. Patricio Peña and Miss. Mónica Villagómez.
- **Perú:** Procapitales; Mr. Guillermo Garrido and Miss. Cayetana Aljovín.
- **Venezuela:** AVE, Association of Top Executives; Dr. Italo Pizzolante, Dra. Sonia de Paola and Dr. Desmond Dillon.

According to terms of reference, CAF underlines the fundamental and authentic centre of the Project as the *"Drafting of the Guidelines for an Andean Corporate Governance (the Code hereinafter) based upon the OECD Principles of Corporate Governance of 2004 and the Latin-American White Paper of Corporate Governance"*.

The Code, according to the terms of reference, takes into consideration the main areas of the OECD Principles, - both original and revised version – related to Shareholders Rights, Equitable Treatment, Transparency and Disclosure as well as Board responsibility.

### II. STAGE 1: DOMESTIC LEGAL AND REGULATORY FRAMEWORK ASSESSMENT

The main purpose of this stage was to define the following:

1. The possibilities to encourage good corporate governance standards.
2. The differences between the several local basic laws.
3. The reforms carried out in local Corporate Governance standards, if any.

4. The need for Corporate Governance enforcement, based on the protection to shareholders provided by the different local legal frameworks in force.

In order to get an informed opinion about the preceding issues, the Project Director, Mr. Alfredo Ibargüen, made a mission trip to the five countries of the Andean Region, where he met with all the relevant counterparties with something to say in corporate governance. Some of those counterparts involved key players such as supervisors, regulators, investors, law firms and business associations among others.

In this line, the first phase was based upon a process of data collecting and analysis regarding the economic and legal reality of Andean companies under the scope of previous international experiences in the field of Corporate Governance and new regulatory measures.

### **III. STAGE 2: DEVELOPMENT OF THE LCGAC**

The main objective to achieve in this stage was to write down and develop a Corporate Governance Andean Code, applicable to the five countries of the Andean Region. The Code was first released as a version for public comments in April 2004. The final version was released in April 2005 (go to: <http://www.iaag.com/Codigo.pdf> to get a copy).

Obviously, this stage was to be based on Stage 1 findings, taking into account that the conclusions of the previous stage would provide the frame in which the Code would have to be implemented and operative.

Therefore, the Code would have to be carried out with an inclusive and consensus-driven approach, in collaboration with local counterparts. Otherwise, the Code might be seen as a foreign imposition, and could face several difficulties to be effective. Nevertheless, even though the Code has been developed with the collaboration of several local counterparts, the corporate governance standards proposed are highest internationally accepted standards.

#### **Philosophy of the Code**

The philosophy of the Code is based on the following principles:

- **Target:** THE CODE WAS MAINLY AIMED AT COMPANIES. This is the main difference between OCED Principles and other international guidelines that are addressed to guide public policy and regulators. However, The Code specifically address the legal barrier for many of the international standards of Corporate Governance to be implemented within the companies of the five countries of the Andean Region; therefore, annotations may be useful for law and regulation.
- The Code addresses the importance of adopting these standards throughout the internal regulation such as By-Laws, Internal Chart and Rules and of course to develop specific internal actions in order to achieve compliance with the provisions.
- The main driver for companies to implement those recommendations is the fact that it helps them to improve international competitiveness, performance and allows in consequence that capital providers, banks, financial institutions and particular foreign and local investors operating in capital markets value the commitment of companies to Corporate Governance and its compliance with the internal system as an effective rule for Risk Management.
- In line with recommendations of corporate governance, it seems that the Code's standards, should be adopted at least by those companies looking to expand their horizons towards different sources of finance, such as heavily-regulated collective schemes. Their securities will need to become an optimal instrument for those schemes to achieve the minimum coefficients of their investments that they are obligated to meet among provisions contained in special regulation, or just because they have strong risk management policy.

- Along these lines, the initiative undertaken by Colombia to require companies to have their own Corporate Governance Code in line with legal provisions in order to be suitable for Pension Funds' investments within the financial markets is interesting. However, we do understand that a set of unified standards should be required in the form of a Country Code along with the principle of "Comply or Explain". That way the market will be able to note which of the standards are being adopted by the company through its major corporate documents.
- However, because of its Andean scope, a special notice had to be made specifying the more relevant national legal incompatibilities with some corporate governance standards of the Code.
- Corporate Governance is conceived as a means, not an end in itself (a tool, not a dogma).
- The traditional scope of Corporate Governance, usually focused on large listed companies, should be extended to four types of companies:

**a) Large listed companies:** (significant free float and/or fixed income securities issuer, with at least fifty (50) shareholders)

**b) Listed companies:** (any company that is compulsory listed because of legal provisions, with no fundamental intention to become an issuer)

**c) Large private companies:** (any unlisted company not controlled by a family and that does not use capital markets for financing)

**d) Privately-held companies:** (Close and family controlled company)

- The Corporate Governance standards had to be turned into practically-oriented specific Measures and Recommendations, explicitly applicable selectively to the four types of companies, pursuing their effective implementation. Corporate Governance exigencies should not be the same for any company no matter its type. At the same time, entrepreneurs have to understand: (i) the logic; (ii) the *rationale*, and (iii) the benefits of what they are being asked to implement in terms of Corporate Governance, if we want them to best comply with it.
- The recipients, the entrepreneurs, should understand what they are doing and why, and not feel it is an imposition, but an opportunity.
- Including highest internationally accepted CG standards, while reporting the current legal barriers that a material implementation may face. In this sense, even though the Code is mainly addressed to entrepreneurs, there are some remarks made to the Regulatory Bodies and official entities, in terms of some issues that should be governed by law (i.e., rights and duties of the members of the Board, legal regime of takeovers, etc.). Besides, whenever we have observed a major incompatibility with a domestic law, we have made a reference to it.
- Emphasis and focus on the implementation as the most critical goal to be achieved. There is a huge literature on corporate governance, in the form of Voluntary Codes, which however has never been implemented in any company. We always thought of the implementation as the critical goal to achieve. That's why the Code is written in clear Spanish, and the Measures and Recommendations are explicitly applicable and concrete.

#### **IV. STAGE 3: IMPLEMENTATION IN A SELECTED COMPANY PER COUNTRY**

The main objective of the Code was to be effectively implemented. That is what explains the absolutely pragmatic and practical approach followed by the Code.

The implementation of the Code is to be made through the company documentation (Bylaws, General Assembly Rules, Board Charters, etc.) and, in some special cases, Shareholders Agreements.

Within the context of the CAF Projects, (both the first one finalized and the one currently on-going), IAAG provided the technical assistance for the implementation of the Code's Corporate Governance practices to fifteen (15) companies, which voluntarily participated in the implementation program and who had been previously selected by the CAF:

- Four large listed companies
- Five Family-Owned and private companies
- Four Financial Institutions (Banks and Insurance)
- Two large non-listed companies

From the group the companies that were involved in the CAF project, six processes are still on going. The five companies of the first project were totally sponsored by CAF. In the case of the ten companies of the second project, costs were assumed in equal part by CAF and the company.

IAAG has developed and still is executing other processes of implementation and assessment of Corporate Governance in more than ten companies under the sponsorship of the Inter American Development Bank; the International Finance Corporation and through bilateral contracts directly with the clients.

Attached hereto, is the Row Chart of IAAG's Methodology of Implementation plan for companies as well as a specific example of implementation in a large listed company (Graña y Montero).

#### **Comply or explain**

The Code adopts the "*comply or explain*" principle. Therefore, the Board of Directors has to respond every year and be responsible—through a corporate governance annual report—for the compliance with each of the Measures and Recommendations of the Code. Hence, the stakeholders are the ones that have to appraise the governance of the firm, and thus adopt their own decisions.

The use of the "*comply or explain*" principle offers without any doubt huge advantages. First of all, it's an optimal mechanism for the company to adopt those standards of the Code that are applicable according to the type and the ownership structure, and therefore disclose progress in corporate governance to interested third parties (such as shareholders, investors, banks, supervisors etc.). Secondly, it's a mechanism that harmonizes commitment and flexibility simultaneously.

We say it is a **commitment** since it involves a Corporate Governance Report and an Annual Report that are both the responsibility of the Board of Directors, who will have to be specially disciplined with the information that goes public regarding the level of observance of the standards. And we also say is **flexible** as it allows the company to explain the reasons why it hasn't adopted a specific standard either because it feels it's not convenient or because it doesn't agree with the content of the measure.

#### **Scope and object**

The Code includes a set of measures that should be incorporated in the By-laws of the company and other internal regulation related to its governance. Therefore, it refers to the regime of notice of the General Shareholder Meeting, its preparation, support information, attending, development and voting rights among others.

The same variables are applied to the Board of Directors, where composition, structure, independence, duties and responsibilities, are also addressed.

Transparency and Disclosure is also included in the scope of the Code. Accounting standards, material information and independence and professionalism of the external auditor are some of the specific subjects covered therein.

Alternative Dispute Resolution is as well included in the Code as a convenient way to resolve controversies between the shareholders and the company; the company and the directors and executives; the shareholders and the directors and the executives, and so on.

### **Promotion**

CAF has developed a series of activities directed to promote corporate governance around the Andean Region and to take abroad the knowledge of the Code as well as the processes of implementation.

For these purposes, CAF has set several seminars in all countries with the collaboration of the counterparts and other key players of local markets, inviting not only the consultancy firm, but the companies who have been subject to the implementation process of Corporate Governance.

On the other hand, CAF has prepared more than 150 consultants through what were called "Workshops for Consultants" where independent consultants and firms were trained not only in the substance of the Code, but in the implementation methodology and the use of the Corporate Governance Due-Diligence Software®

During the first semester of 2007, CAF will be hosting in each of the countries an ambitious seminar to promote its second project. The topic of these seminars may vary between countries; however, the case-studies of the pilot cases and the Andean Survey on Corporate Governance practices will be presented.

## **V. AREAS CONSIDERED IN THE ANDEAN CORPORATE GOVERNANCE CODE**

The Code analyses five (5) different areas of interest in the company, and proposes fifty-one Measures and ninety-two Recommendations, selectively applicable to the four types of companies aforementioned.

The Code includes a wide report explaining the fundamentals of each one of the measures proposed as well as a glossary of terms. The index of subjects covered by the Code is attached hereby.

The breakdown of Measures and Recommendations is as follows:

- 1. RIGHTS AND EQUITABLE TREATMENT OF SHAREHOLDERS** (6 Measures, 15 Recommendations)
- 2. SHAREHOLDERS MEETING** (12 Measures, 19 Recommendations)
- 3. BOARD OF DIRECTORS** (24 Measures, 46 Recommendations)
- 4. FINANCIAL AND NON FINANCIAL INFORMATION** (8 Measures, 11 Recommendations)
- 5. ARBITRATION AS CONFLICT RESOLUTION PRACTICE** (1 Measure, 1 Recommendation)

## **VI. OUR WARNINGS**

The Code means a strategic step forward towards the establishment of a unique corporate governance framework in the region.

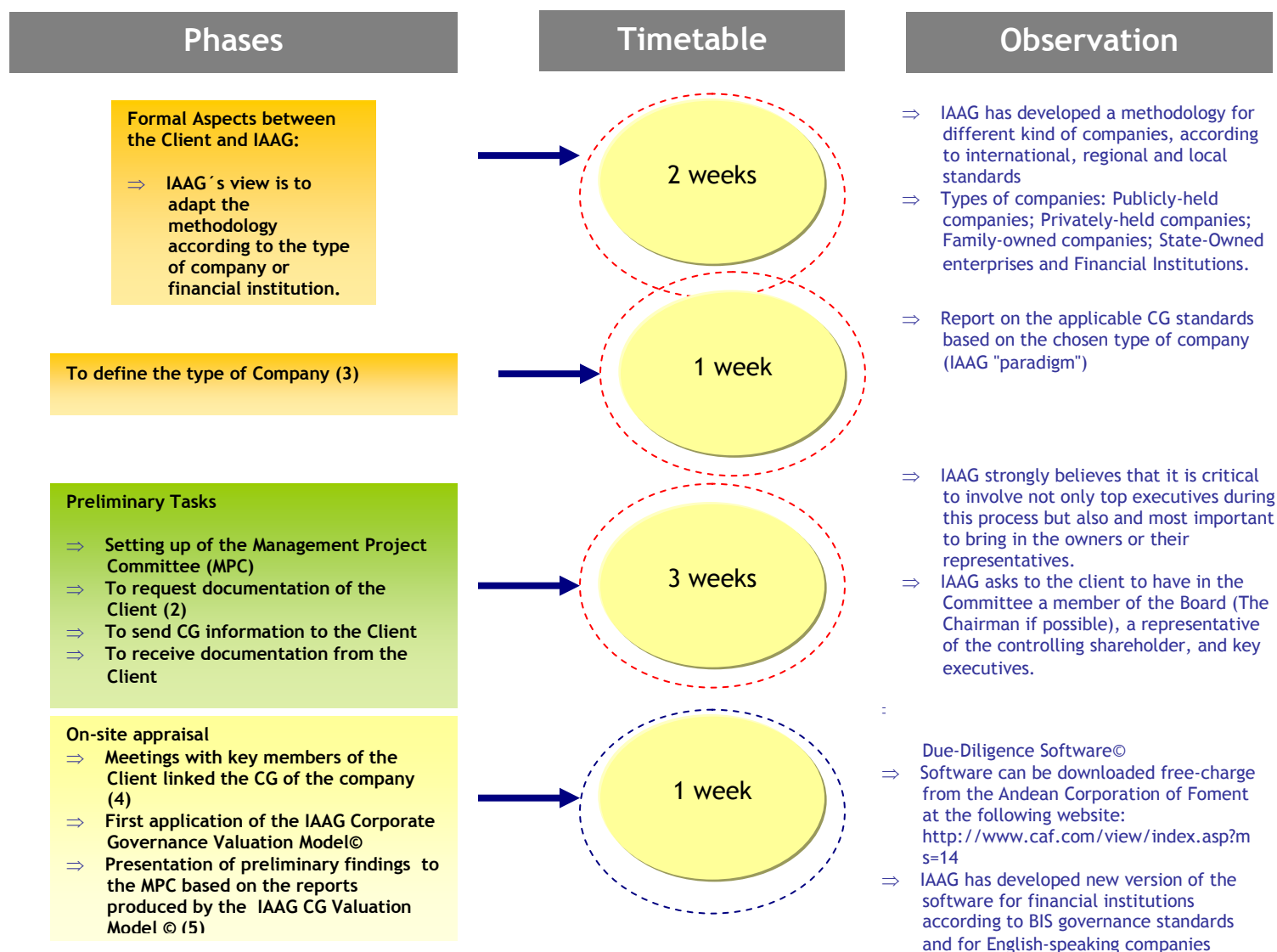
Nevertheless, we feel one of the major weaknesses for the effective implementation of corporate governance in the region is the absence, or at least serious limitations, of adequate enforcement vehicles, that is, the enforceability.

Therefore, the next steps should be oriented to reinforce the role that a set of bodies and institutions must play. In fact, if we want Corporate Governance to be widespread, there are some key players that must play their role:

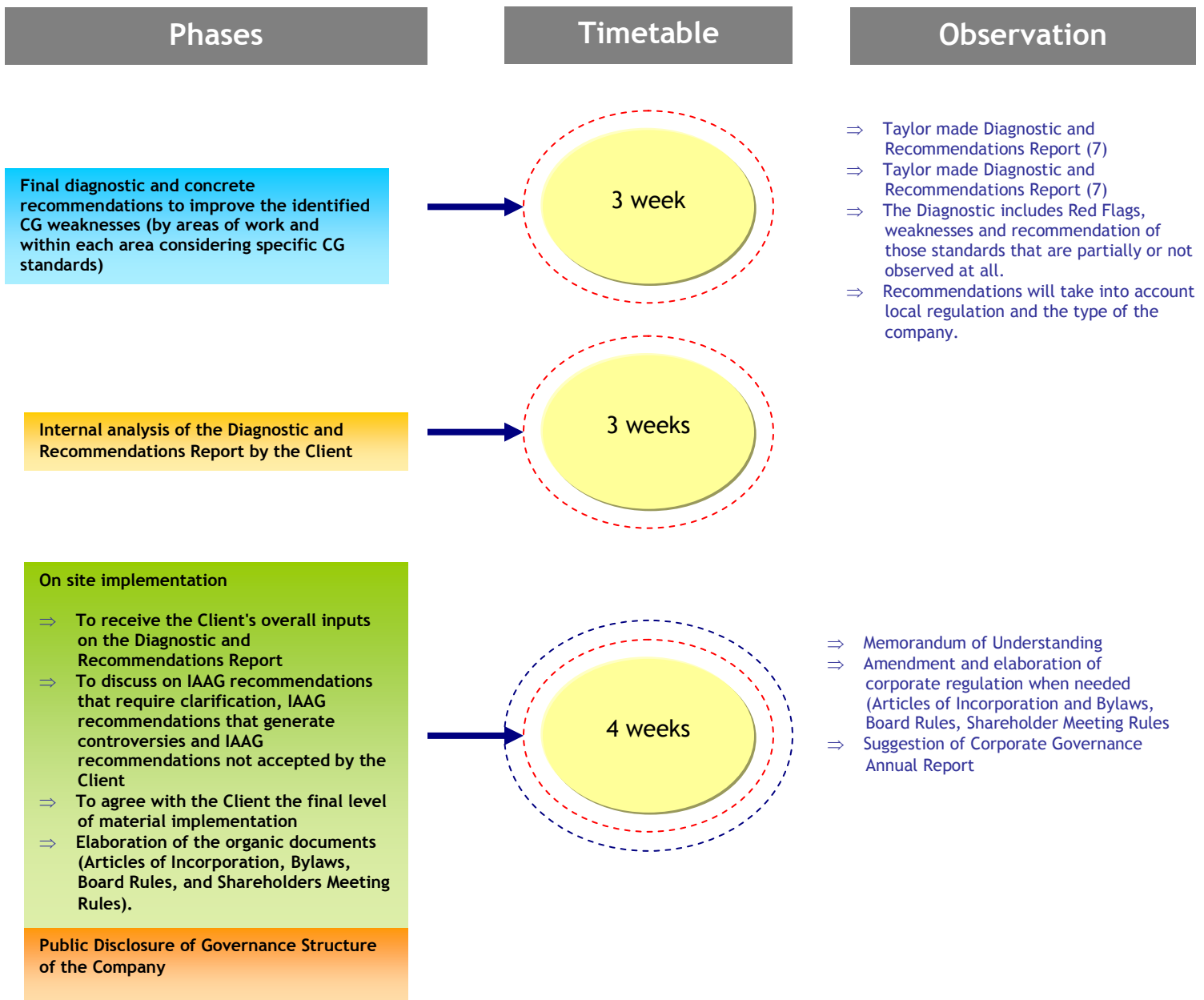
- **Banks and Financial Institutions:** Banks have a substantial importance in promoting Corporate Governance. They play a key role in the economy of any country. If banks adapt the lending policies they apply and consider the Corporate Governance practices of their clients, good Corporate Governance would be much more widespread.
- **Regulatory Bodies:** The Regulatory Bodies play a central role for the expansion of Corporate Governance. The definition of Corporate Governance rules for issuers (either stocks, fixed-income securities or both) should encourage the spread of Corporate Governance practices.
- **Private Equity Funds:** Private Equity transactions should be fostered if target companies have good corporate governance.
- **Other institutional investors:** Institutional investors, especially pension funds, should be involved not only in activity promoting improved governance of the companies they invest in, but in their own Corporate Governance.
- **Rating Agencies:** If rating agencies take into account corporate governance issues in their ratings, it helps them to get through the regional standard that should be observed not only by the companies but by the regulatory framework

\* \* \*



**ANNEX 1****Row Chart of IAAG s Methodology of Implementation plan for companies:****CORPORATE GOVERNANCE IMPLEMENTATION PLAN  
ROW-CHART**





### Annotations:

- ⇒ ..... On site visitation to the company
- ⇒ - - - - - Home office work (Consultant Headquarters)
- ⇒ A client may contract only the Due-Diligence phase.
- ⇒ IAAG is willing to develop and Assessment Plan, if the company wants to develop by it self the implementation phase.
- ⇒ For more information please feel to contact us at [gobiernocorporativo@iaag.com](mailto:gobiernocorporativo@iaag.com)
- ⇒ Contact persons: Alfredo Ibarguen - Partner ([aibarguen@iaag.com](mailto:aibarguen@iaag.com)); Paola Gutiérrez - Associate of the CG Unit ([pgutierrez@iaag.com](mailto:pgutierrez@iaag.com)); Jose Gomez-Zorrila - Associate of the CG Unit ([jgza@iaag.com](mailto:jgza@iaag.com)) ; Jorge Celio - Associate of the CG Unit ([jcelio@iaag.com](mailto:jcelio@iaag.com))

**ANNEX 2****INDEX OF THE CODE – SECTION 1.****EXPLANATORY REPORT ON THE CODE****I. INTRODUCTION**

- a. Background
- b. Scope
- c. Enforcement

**II. SCOPE OF APPLICATION**

- a. Scope
- b. Reach out and fundamentals
- c. Interpretation and applicability
- d. Interpretation and applicability of the By-Laws

**III. SHAREHOLDERS RIGHTS AND EQUITABLE TREATMENT**

- a. Equal treatment on voting rights
- b. Right of no dissolution of the companies capital
- c. Promoting participation and disclosure for shareholders
- d. Electronic mechanisms for disclosure and dissemination of information through corporate website
- e. Right of convey or transfer shares;
- f. Change of control

**IV. GENERAL ASSEMBLY OF SHAREHOLDERS**

- a. Function and competence
- b. Internal Rules for the General Assembly of Shareholders
- c. Different classes of meetings and notices
  - i. Compulsory obligation to notify
  - ii. Terms
  - iii. Mechanisms of dissemination of the notice
  - iv. Content of the notice
  - v. Shareholders rights to information with sufficient anticipation and during the meetings
  - vi. Institutional Investors and Significant Shareholders
  - vii. Establishment of Meeting rules
  - viii. Quorum and majorities required
  - ix. Shareholders interaction
  - x. Rules of representation and mechanisms for proxy voting
  - xi. Uninstructed proxy
  - xii. Directors voting procedures
  - xiii. Attendance of third parties

**V. THE BOARD OF DIRECTORS**

- a. The need of a Board
- b. Main functions of oversight and definition of strategy. Prohibition of delegation.
- c. Internal Rules and Chart of the well functioning of the Board
- d. Board dimension
- e. Different categories of Directors
- f. Nomination
  - i. Member appointment
  - ii. Representation of the shareholders
  - iii. Majority of non-executive directors
  - iv. Appointment of independent directors
  - v. Declaration of independence
- g. Cease of Directors
- h. Rules on director's duties
- i. Director's compensation
  - i. Proposals and approval procedures
  - ii. Disclosure of compensation schemes
  - iii. Compensation items
- j. Board Structure
  - i. Chairman
  - ii. Vice-Chairman
  - iii. Board Secretary
- k. Top executive
  - i. CEO and Senior Management
- l. Internal rules on board functioning, notice, and organization
- m. Special Committees
  - i. Audit Committee
  - ii. Nomination and Compensation Committee
- n. Oversight and control on related party transactions

**VI. DISCLOSURE OF FINANCIAL INFORMATION AND INTERNAL CONTROL**

- a. Disclosure to financial markets
- b. Shareholders agreement Disclosure

**VII. CORPORATE GOVERNANCE ANNUAL REPORT**

- a. Evaluation and overview of the observance of the internal rules on corporate governance
- b. Information included in the Corporate Governance Report

**VIII. ARBITRATION AND ALTERNATIVE DISPUTE RESOLUTION MECHANISMS IN THE BY-LAWS**

### ANNEX 3

#### CASE – STUDY ON IMPLEMENTATION PLAN OF CORPORATE GOVERNANCE GRAÑA y MONTERO LARGE LISTED COMPANY

Graña y Montero, S.A.A., in Peru, because of its dimensions and characteristics relies on a strong internal organization with top quality staff and directors with a widespread knowledge on the topic of Corporate Governance.

Graña y Montero S.A.A stated from the very beginning of the process its ability in the decision-making process in regard to the different topics covered by the Consultancy, both when it was on-going and the processes that had to be undertaken after. It was clear that the main drivers for the process were: i) competitive advantages, ii) leadership and market transparency, iii) to become more attractive for investors, shareholders, rating agencies and financial institutions.

The starting point of the process was characterized by the existence *de-facto* of a central company working as a holding; a significant free float as a listed company in the Stock Exchange of Lima; five non-listed subsidiaries and interlocking boards.

Consequently, it was decided that as a conglomerate, major changes needed to be done in the “Mother” company, so Corporate Governance measures and recommendations would have to break down to subsidiaries.

The process started with a Due-Diligence based on the software developed by IAAG, and in general, results can be summarized as follows:

- ⇒ **Shareholders Rights and Equitable treatment:** All standards on average level, special emphasis was given to all aspects related to information given to shareholders.
- ⇒ **General Shareholders Meeting:** The consultant identified that measures should be undertaken especially with regard to the Rule of meetings; shareholders aggregation and proxy voting.
- ⇒ **Board of Directors:** The importance of the existence of an Internal Charter for the Board, the need of recruitment of different categories of directors, conflict of interest and related party transaction management procedures were underlined.
- ⇒ **Transparency and disclosure:** Special attention was given to aspects related to external auditor and related party transactions given the presence of a conglomerate.

Once the report on recommendations was discussed, with the company the changes describe above were incorporated in the following internal corporate documents:

- ⇒ Amendments of the By-Laws
- ⇒ Rules for Shareholders Meetings
- ⇒ Rules for the Board of Directors
- ⇒ Annual Report on Corporate Governance

***Summary of the most outstanding improvements contained in the documents stated before:***

⇒ **Shareholders Rights and Equitable treatment:**

- Creation of special division for investors relationship
- Proxy voting clear measures

⇒ **General Shareholders Meeting:**

- Widespread diffusion of the meeting notice
- Approval of the Rules for Shareholders Meetings

⇒ **Board of Directors:**

- Different categories of Directors were recognized: Non-executives and independent directors among others.
- Special Committees were created (Audit and Compensation)
- New dimension of the board was approved. The number of member was elevated to nine (9)
- Appointment of directors procedures were clarified and approved
- The position of Secretary of the Board was created
- Self evaluation was incorporated.

⇒ **Transparency and disclosure:**

- The Audit committee is now in charge of the evaluation of significant related party transactions
- A Corporate Governance Report on an annual basis was established.
- Disclosure of other services given by the firm in charge of conducting the external auditing.

**Evolution of the stock price of Graña y Montero, S.A.A.,  
VS Corporate Governance implementation plan timetable**

