CORPORATE GOVERNANCE IN ROMANIA (II – CONSIDERATIONS ON ROMANIA'S COMPLIANCE ON OECD PRINCIPLES ON CORPORATE GOVERNANCE)

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Abstract: Result of the theoretical researches on the issues related to possible different interests of shareholders and executive managers, OECD issued in 1999 The Principles of Corporate. In Romania, there were identified some problems, related to: weak institutional framework, necessity of urgent implementation and enforcement of the already existing laws, the lead that private sector should take in developing implementation tools and promoting public debate on corporate governance issues, protection of minority shareholders rights. In the late years, Romanian authorities achieved a process of revising legislation related to companies' governance. This new regulation will benefit to all parts involved, such as major investors, minority shareholders and companiest; finally, the whole society will benefit from a cleaner and more performing economic environment.

Key words: corporate governance, Romania, legislation

As practical results on theoretical researches on the issues related to possible different interests of shareholders and executive managers, the most important one is The Principles of Corporate Governance, achieved by OECD in 1999 and revised in 2004. According to OECD, the main principles needed to be observed by companies refer to:

1. 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.
2. The Rights of Shareholders and Key Ownership Functions. The corporate governance framework should protect and facilitate the exercise of shareholders' rights.
3. 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.
4. 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.
5. 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.
6. 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 main issues about Corporate Governance in Romania, as identified in the White paper on corporate governance in South East Europe Corporate Governance Roundtable (OECD) are:

- Weak institutional framework, among other things, is one of the significant impediments to the establishment of a sound investment climate

- Implementation and enforcement of the already existing laws should be a priority
- The private sector should take the lead in developing implementation tools and promoting public debate on corporate governance issues
- Address the most severe weakness – minority shareholders rights violations.

In the wake of the international financial crisis of the 1990s, the international community started to enforce initiatives to strengthen the international financial architecture, with the objective of crisis prevention, mitigation and resolution. The Financial Stability Forum, the G7, the G20 and the G223 have emphasized the role of minimum standards and codes in strengthening the international financial architecture. At the international level, standards enhance transparency, identify weaknesses and foster market efficiency and discipline. At the national level, standards provide a benchmark to identify vulnerabilities and guide policy reform. To best serve these two objectives, the scope and application of such standards need to be assessed in the context of a country's overall development strategy and tailored to individual country circumstances. The IMF, the World Bank and other international financial institutions are undertaking the assessment of systemically important countries of the observance of 11 core standards relevant to private and financial sector development and macroeconomic stability. In this context, the Bretton Woods institutions have initiated the joint initiative on "*Reports on the Observance of Standards and Codes*" ("ROSCs"), covering 11 core standards relevant to economic stability and private and financial sector development. The individual standard assessments are collected as "modules" in country binders constituting the aforementioned "ROSCs". Under this modular approach, the IMF takes the lead in preparing assessments in the areas of data dissemination and fiscal transparency. (Fremond and Capaul, 2002).

About Romania, the Report on the Observance of Standards and Codes (Rosc) Corporate Governance Country Assessment ROMANIA April 2004 stated the following levels of observance:

1. The rights of shareholders: 4 criteria considered largely observed (basic shareholder rights, shareholder AGM rights, Disproportionate control disclosure, Control arrangements should be allowed to function), 1 partially observed (Basic shareholder rights) and 1 (Cost/benefit to voting) materially not observed
2. Equitable treatment of shareholders: 2 criteria (All shareholders should be treated equally, Board/Mgrs. disclose interests) partially observed, 1 criterion (Prohibit insider trading) largely observed
3. Role of stakeholders in Corporate Governance: 3 criteria (stakeholder rights respected, redress for violation of rights, access to information) largely observed, 1 criterion (performance enhancement) materially not observed
4. Disclosure and transparency: 3 criteria (disclosure standards, standards of accounting and audit, fair and timely dissemination) partially observed, 1 criterion (independent audit annually) materially not observed
5. Responsibilities of the Board: 1 criterion (ensuring compliance with law) largely observed, 1 (acts with due diligence, care) partially observed, 4 criteria (treat all shareholders fairly, the Board should fulfill certain key functions, the Board should be able to exercise objective judgments, access to information) materially not observed.

One year later, The 2005 Legal Indicator Survey confirms that related-party transactions remain an issue for concern in all transition countries. The degree to which minority shareholders can obtain effective disclosure or redress is limited, and well below what could be expected when looking at the laws. Disclosure and redress are inextricably linked. This is because an action for redress can only be initiated when evidence is secured. The assessment reveals that requesting a general shareholders' meeting is the most common action provided by law to minority shareholders, but it is unlikely to produce any disclosure when the company is controlled by a powerful shareholder. In cases of obvious misconduct, criminal proceedings are available by law in all countries in the region, but the vast majority of contributing practitioners expressed serious doubts as to the experience and competence of prosecutors in corporate cases.

Three main conclusions can be drawn. First, countries that have developed a solid institutional environment can generally offer an effective legal framework. Nevertheless, as demonstrated by the issue of disclosure in Estonia, this alone is not enough to give minority shareholders adequate protection against abusive behaviour by controlling shareholders. The sound environment needs to be coupled with a

corporate governance framework in line with international standards and with an effective civil procedural framework. Second, consistent with previous studies on shareholder and creditor rights in transition countries, the survey shows that new EU member states and candidate countries,29 while displaying a better institutional environment, do not systematically outperform other transition countries with regard to the effectiveness of disclosure or redress mechanisms. Finally, even excellent laws can suffer from poor implementation. This undermines the usefulness of legal provisions and diminishes the confidence of foreign investors in the legal system as a whole – in particular, in its ability to uphold contractual rights. Most transition countries need to upgrade their commercial laws to standards that are generally acceptable at an international level. Even more importantly, they must make those laws fully effective, particularly through strengthening their court systems, tackling corruption and adopting appropriate measures to strengthen the rule of law (*EBRD Legal Indicator Survey 2005*).

According to *Doing Business 2008* report, covering the period April 2006 to June 2007, Romania has the 48 rank, in progress compared to 55 rank in 2007.

Ease of…	Doing Business 2008 rank	Doing Business 2008 rank	Change in rank
Doing Business	48	55	+7
Starting a Business	26	14	-12
Dealing with Licenses	90	87	-3
Employing Workers	145	133	-12
Registering Property	123	112	-11
Getting Credit	13	32	+19
Protecting Investors	33	32	-1
Paying Taxes	134	135	+1
Trading Across Borders	38	39	+1
Enforcing Contracts	37	37	0
Closing a Business	81	109	+28

Source: http://www.doingbusiness.org

About the Protecting Investors criterion, the indicators below describe three dimensions of investor protection: transparency of transactions (Extent of Disclosure Index), liability for self-dealing (Extent of Director Liability Index), shareholders' ability to sue officers and directors for misconduct (Ease of Shareholder Suits Index) and Strength of Investor Protection Index. The indexes vary between 0 and 10, with higher values indicating greater disclosure, greater liability of directors, greater powers of shareholders to challenge the transaction, and better investor protection.

Indicator	Romania	Region	OECD
Disclosure Index	9	4.9	6.4
Director Liability Index	5	3.8	5.1
Shareholder Suits Index	4	6.3	6.5
Investor Protection Index	6.0	5.0	6.0

According to Industrial Bulletin of GEA (Group for Applied Economy), three quarters of the companies do not know and apply the OECD Corporate Governance Principles. More specific, 77.8% of the companies declare they do not know the principles of corporate governance (15.7% do not know them and 6.5% do not know/do not respond), while 79.7% of the companies declare they are not applying these principles.

According to GEA experts, it is however possible that some companies apply these principles without knowing it, in the context that:

- only 34.7% of the companies do not have a written conduct code, formally establishing the rights and responsibilities of AGA's members and of the management, the communication and reporting way between managers and shareholders;

- in 31.3% of the companies shareholders do not receive in advance the documents to be discussed in shareholders general assemblies;
- in 26.2% of the companies the minority shareholders do not have access to the book sheets of the company;
- 30.8% of the companies had not published, till May 2007, a report on company's activity in 2006
- 79.7% of the companies haven't change the company's auditor in the last 3 years.

What are the recent developments in the institutional framework of CG?

Following the conclusions of several official document regarding the Romania's progresses (such as: European Commission's Report on Romania's progress in 2004 regarding the EU accesing process, The Monitoring Report of preparation stage for EU accession – October 2005, the conclusions of World Bank in evaluating the compliance of Romania's legislation with OECD Corporate Governance Principles ROSC-2004), Romanian authorities achieved a process of revising legislation related to companies. The main EU regulations relevant for this matter are:

- First Directive of EU Council no. 68/151/EEC;
- Second Directive of EU Council no. 77/91/EEC;
- Third Directive of EU Council no. 78/855/EEC;
- 6th Directive of EU Council no. 82/891/EEC;
- 11th Directive of EU Council no 89/666/EEC;
- 12th Directive of EU Council no. 89/667/EEC.

The legislation reform intended to adjust both to the standards imposed by the EU acquis regarding the companies and to OECD standards on Corporate Governance. Consequently, the new legislation (Law no.441/2006 to modify Law no. 31/1990 regarding the companies and Law no. 26/1990 on trade register, published in Monitorul Oficial, Part I no. 955 on November 28, 2006). Regarding the compliance to OECD Corporate Governance principles, we can mention some aspects of the new legislation, such as:

- reconfiguring the structure of the Board (Consiliul de administratie), choosing the "one-tier" model, making distinction between the executive and non-executive positions;
- defining the executive and non-executive positions and the liability of executive and non/executive administrators;
- criteria to ensure the independence of non-executive administrators;
- revising the regulation of administrators' statute, by enforcing the due diligence obligation, the loyalty to company obligation, the "business judgement rule";
- clarifying the issue of position cumulating;
- improving the minority shareholders' protection by new regulations on general assemblies meetings, quorum and majority requirements, enforcing the right to vote, to information and disclosure, dividend payments, etc.;
- regulating the financial auditors appointment, etc.

Very important in our opinion are:

- the possibility to create consultative committees in order to make investigations and elaborate recommendations for the Board, concerning: audit, remuneration of the administrators, managers, personnel, nominating candidates for management positions;
- the regulation on independent non-executive administrators: at least one member of each committee must be an independent non-executive administrator. The audit Committee and the Remuneration Committee must be composed only by non-executive administrators. The presence of independent non-executives directors will enforce a independent control over the actions of executive directors, enhancing the responsibility of executive directors.

This new regulation will benefit to all parts involved, such as investors, especially minority shareholders and companies, benefiting from a better management; finally, the whole society will benefit from a cleaner and more performing economic environment.

We must add that, right at the moment we finished that paper, Romanian Stock Exchange launched the April version of it's project on Corporate Governance Code. Conceived to be a non compulsory code, based on the principle "comply or explain" it will enhance the companies' compliance to the corporate governance principles, in order to make a more open and favorable economic environment in Romania, to the benefit of all investors, major and minor shareholders.

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