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Lessons Learned Series

corporate governance

better companies, better societies

Panama's Experience Shows Importance In Defining Objectives, Attracting Committed Supporters, Exerting Leadership

When the head of Panama's securities regulatory commission (Comisión Nacional de Valores) met prominent business leaders in October 2006 and encouraged them to advance corporate governance within their business community, he offered advice: Motivation and commitment will ultimately determine success.

"Like any business venture, corporate governance has inherent vested interests," Carlos Barsallo said. "You should expect conflict. That's why you must be committed to thwart dissension, but you must be committed for the right reasons. Clear goals and objectives—supported by all parties—are a must. In Panama, we initially thought that we all had the same vision, but it wasn't the case. It took time to resolve our differences and define shared goals."

Few Understood the Business Necessity for Corporate Governance

"Commission President Barsallo's message was a catalyst in galvanizing our attention to do something," said Joseph Fidanque, Jr., a director of Mobil Phone and the founding president of the Institute of Corporate Governance—Panama (Instituto de Gobierno Corporativo Panamá). Fidanque's extensive experience includes his tenure in 1998 as the first chairman of an oversight board of Panamanian banks (La Superintendencia de Bancos).

"We knew that we needed to take action, but we had to understand more about corporate governance and its implications, particularly for family-owned businesses. There was little awareness. The practices and experiences of large global companies were not relevant. We needed to explain how companies like ours were making progress. Through their success stories, we could broaden awareness of corporate governance among business leaders and help them implement reforms."

The Institute's board. Seated (from left to right): Julieta Rodríguez, Joseph Fidanque, Jr., Jorge Martins. Standing (from left to right): Milton Chambonett, José Chen Barría,Temístocles Rosas, Ricardo Bell.

The Forum's counsel and support was critical in the Institute's early days.

For many of Panama's privately owned companies, corporate governance was seen as a necessity only if the company wanted to list on foreign stock exchanges. Some owners misunderstood their obligations should they adopt corporate governance best practices. Others rejected some requirements as being competitive disadvantages or a low priority given Panama's size and its companies' ownership patterns.

One stumbling block in advancing corporate governance awareness and action in the country is the concept "independent

Global Corporate Governance Forum

The Global Corporate Governance Forum is an International Finance Corporation (IFC) multi-donor trust fund facility located in the IFC/World Bank Corporate Governance and Capital Markets Department. The Forum was co-founded by the World Bank and the Organisation for Economic Co-operation and Development (OECD) in 1999.

Through its activities, the Forum aims to promote the private sector as an engine of growth, reduce the vulnerability of developing and transition economies to financial crisis, and provide incentives for corporations to invest and perform efficiently in a socially responsible manner. The Forum sponsors regional and local initiatives that address the corporate governance weaknesses of middle- and low-income countries in the context of broader national or regional economic reform programs.

Donors to the Forum include the IFC and the Governments of Canada, France, Luxembourg, the Netherlands, Norway, Sweden, and Switzerland.

IFC International Finance Corporation World Bank Group

directors" and the stress on board composition and decision making.

"When we discussed the business case for corporate governance, owners questioned how they could have 'independent' directors," said Fidanque. "Companies in Panama are owned by the same families. Those who you would like to have on your board most likely have ties to your business and family. It's inevitable, given how small our country is. There was nervousness about sharing business secrets with someone who isn't closely involved with the company and its family. It is these kinds of questions that family-owned companies and their boards need to work through before fully embracing corporate governance."

"Corporate governance is a journey. We have many steps ahead, but we've laid a strong foundation for an Institute with regional influence."
Joseph Fidanque, Jr.

Institute Launches, Defines Mission

In April 2007, 15 business leaders formed the Institute of Corporate Governance–Panama and chose Fidanque as president. "Having a well-known, highly respected person as our president gave the Institute tremendous authority in approaching board chairmen," said Temístocles Rosas, the Institute's first comptroller and managing director of Consulting Plus, a private consulting firm. "Through Mr. Fidanque's participation, we attracted other important business leaders."

FORUM OBSERVATION

"Carlos Barsallo and Alberto Diamond did a highly unusual thing—they stepped back after sparking interest in and debate over the need for an Institute. They continued to be supportive, but they did so at arm's length. They permitted the Institute's founders to have the healthy distance needed to develop their own definition of who the Institute is and what it will do."

Nancy J. Metzger
Senior Project Officer
Global Corporate Governance Forum

Bengt Hallqvist, founder of the Brazilian Institute of Corporate Governance and a member of the Private Sector Advisory Group, visits Panama.

After many deliberations, the Institute defined its mission and objectives:

- Build a resource that helps company owners, board directors, investors, and other stakeholders learn about corporate governance
- Improve governance practices in business entities (including listed companies, banks and financial institutions, family-owned and state-owned enterprises, and small and medium enterprises)
- Train and develop directors, managers, investors, and others
- Help develop business practice standards through codes or policy recommendations, guided by the OECD's *Principles of Corporate Governance*

"In defining our purpose, we spent a great deal of time discussing what we should try to achieve, knowing that we couldn't move too far ahead of the business leaders that we needed to persuade to support corporate governance reform," said Milton Chambonett, an Institute founding director and founder of Chambonett & Asociados, an accounting firm. "This process helped us to formalize how the Institute's leadership would work together and make decisions. Having beneficial goals we all understood was an important foundation in establishing a process through which we could work together to reach a consensus and resolve conflicts."

Six months after their founding, Fidanque noted that, "We still have work to do in defining our mission and the actions that will support that mission, but we are much clearer today of our purpose and direction."

FACTORS FOR SUCCESS

- Highly respected business leaders attract peer interest
- Business-led initiative seen as more persuasive than government demands
- Public sector representatives help broaden awareness
- Clearly defined objectives focus efforts
- Patience – it's a long-term process that builds over time
- Leverage international organization's support to focus Institute's efforts
- Ownership of issue deepens supporters' commitment, enhances vision
- Relevant success stories build awareness, convince skeptics
- Institute's need for expertise, other roadblocks addressed through Forum's knowledge-sharing, networking support, toolkits
- Inevitable obstacles overcome by following other institutes' solutions
- Take a step-by-step approach, building upon initial, narrowly-focused efforts to generate sustainable momentum for more comprehensive efforts

The Institute's vision is to become a resource for the region, according to Ricardo Bell, an Institute founder and an internal auditor at Asseguradora Mundial, member of Grupo Mundial. "Sharing the experiences of companies in Panama, Costa Rica, and El Salvador will give our Institute members more value."

"We are an international center, a commercially vibrant, open economy; we want to continue to be attractive for all multinational corporations. We want to be a hub for Latin America," said José Chen Barría, the Institute's first vice president, founder of the consulting firm, Interhouse, Seguros y Valores, S.A., and a board director of Grupo Rodelag.

Forum Shares Expertise, Provides Counsel

The counsel and support provided by the Global Corporate Governance Forum was critical in the Institute's early days. At a Forum-sponsored seminar held in January 2007, founders and leaders from other corporate governance institutes shared their experiences in Brazil, Colombia, and Mexico on launching, growing, and managing an institute.

"We had many basic questions," said Bell. Through the Forum, he said, the Institute's founders learned how "other institutes survived the initial phase" and obtained guidance and access to experts. Having their insights meant that we didn't have to reinvent the wheel; we could profit from what others learned and move forward more confidently."

"It's not possible to fail in corporate governance if you act responsibly in every decision you are called to make. Better companies make better societies."

Temístocles Rosas

The founders have been using the Forum's toolkit to help shape the process of making key decisions in the Institute's first year. "As we go through the steps, we find the toolkit's 'tips' to be invaluable," said Julieta Rodríguez Molina, the Institute's founding secretary and an associate attorney at Galindo, Arias, and Lopez.

Institute meets with regulatory officials in March 2007.

RESULTS

- Institute formed in June 2007
- Extensive media coverage on corporate governance
- Plans underway for building awareness, training
- Negotiating agreements with stock exchanges in El Salvador and Costa Rica

"Everything the toolkit said that would happen in the process, including the pitfalls, did happen, but we were able to resolve those based upon the toolkit's practical advice."

'Ownership' – A Powerful Driver

In the process of defining the mission, "the Institute's founders have gained a sense of ownership of the issue of corporate governance, and that's a powerful driver," said Jorge Martins, the Institute's first executive director and who has served on many companies' boards.

"What helps us in explaining corporate governance is the prestige of the Institute's supporters," said Molina. "They are peers with the business leaders who we want to attract and persuade. Their experience and success are very persuasive tools. They have also fueled some competition among their peers to become involved; some CEOs don't want to feel left out of what their competitors may be doing."

Institute meeting with CNV officials.

Institute Directors Should Represent Diverse Interests

Diversity was one key principle in choosing the Institute's directors. "Different generations and both the public and private sectors should be represented. Building a bridge to the public sector, in particular, helps in formulating public opinion," said Barría.

PANAMA'S CORPORATE GOVERNANCE CHALLENGES

Panama has experienced strong growth since 2006. The country's banking system is the largest in the Central America region, with consolidated assets representing more than three times Panama's GDP. A revised banking law and the creation of the Superintendency of Banks (SdB) in 1998 helped to modernize the regulatory and supervisory framework for banking.

"Now is a good time for an institute," said Barría. "We have the momentum, a booming economic life. But fast-paced growth causes all the problems of putting yourself before the good of others."

"Some owners realize that they must make more progress to safeguard the reputation of our country's fast-growing capital market, attract more investors, and expand into global markets," said Fidanque. "But for others, their success has hidden many deficiencies, so they don't see the need or urgency."

Family-owned companies prevail in Panama, one of the oldest and largest offshore financial centers serving Latin America and beyond. These businesses are in the early stages of adopting corporate governance best practices, according to the 2004 assessment by the World Bank. (http://www.worldbank.org/ifa/rosc_cg_pan.pdf).

In its February 2007 country report, the International Monetary Fund also noted the need for corporate governance reforms. "A regulatory framework for corporate governance structure and internal controls should be developed. The law should incorporate corporate governance rules and minimum internal controls that should be in place and reviewed. Board members responsibilities should be clearly stated. Consideration should be given to the specifying the composition of the board such as requiring the inclusion of independent members, appointing a compliance officer, or creation of committees." (For more information: http://www.imf.org/external/pubs/ft/scr/2007/cr0766.pdf)

The corporate governance challenges Panama confronts are common to emerging market countries. These include: a high concentration of ownership; weak recruitment processes; a limited number of experienced directors; poor awareness about corporate governance; and, underdeveloped legal regimes. (For more information on emerging markets' corporate governance challenges, see 'Improving Board Performance in Emerging Markets" in the McKinsely Quarterly. Available at: http://www.mckinseyquarterly.com/Governance/Improving_board_performance_in_emerging_markets_1711_abstract)

FOUNDERS' REFLECTIONS

Involvement of credible, prominent business leaders who act as ambassadors of corporate governance and build support among skeptical peers

"The individual connections of the founders are absolutely key as the starting point. Their seal of approval is a positive sign that others in the business community should take note, that the effort will not be a waste of their time."

Temístocles Rosas, the Institute's first comproller and managing director of Consulting Plus.

Attracting and retaining a diverse group of individuals to reflect the business community's views and to provide a "reality check" for vetting the institute's plans

Carlos Barsallo, president, National Securities Commission

"Don't make it a club of friends. You need a diverse range of views in your discussions. This way you can anticipate potential sources of opposition and be prepared to address those challenges. Bringing together a group of individuals with strong and very different points of view may slow down the process but it reflects the larger world in which business operates. You also learn how to balance competing interests and personalities."

Carlos Barsallo, president, Panama's National Securities Commission (Comisión Nacional de Valores).

Agreement on clear, well-understood objectives that communicate the value of corporate governance and the institute's vision

"Clear goals and objectives that are supported by all parties is a must. In Panama, we thought initially that we all shared the same objectives but it wasn't the case. It takes time to sort out those differences. A year should not be considered unusual just to define shared goals."

Carlos Barsallo

Allocating sufficient time to iron out the inevitable problems that arise with any start-up, including defining the mission, attracting supporters, developing a plan, resolving conflicts, assessing progress, and obtaining financial support

"One solution is having regular meetings with an agenda so people feel the time is spent wisely. A clear decision making process that values Institute directors' input is also important."

Julieta Rodríguez Molina, the Institute's founding secretary and an associate attorney at Galindo, Arias and Lopez

Using success stories that are relevant to family-owned enterprises to demonstrate the business case for corporate governance

"Demonstrate the business case with examples that will show companies how their peers are adopting best practices and the results achieved. That will also stir competitiveness to match or beat what others are doing."

Joseph Fidanque, Jr., the Institute's founding president and director of Mobil Phone

Involving international organizations like the Forum to focus efforts

"You need external forces to help an institute develop support and move forward. The Forum, for example, helped to shape the dialogue during the institute's early stages so that discussions were more objective, more focused on the key issues rather than getting bogged down in local disputes. International organizations help you to keep your eyes on the prize. When you lose focus, they can help redirect interests."

Julieta Rodríguez Molina

"Unless our thinking and actions truly reflect those of the business community in Panama, and more broadly, Latin America, we will quickly be seen as irrelevant or misguided."

Alberto Diamond, president of KPMG Central America and director at KPMG Panamá, counseled that supporters of the Institute would come and go. "You shouldn't see this as an initial sign of failure. It inevitably happens with a start-up. As new members join and others quit, you eventually arrive at a core dedicated group."

Two activities, according to Martins, are Institute priorities: increasing membership and arranging events to build relationships and inform Panama's business leaders about corporate governance. "The enthusiasm and commitment of the core group is driving the Institute now," said Bell, "but we realize our success will be tied to our ability to involve more people in our efforts."

One of those issues was financing. But Diamond advised the group that they should not "get deterred from action due to money constraints at the start. Sure, money is important because initiatives cost money. But a lot of things can be done at low cost because there already exists a high level of knowledge and experience within the group. With growth and acceptance, the money will come."

The Institute was able to secure initial funds from its business community and international organizations. ■

EMBRACING CORPORATE GOVERNANCE: STEPS FOR FAMILY-OWNED COMPANIES

Throughout emerging market countries, second and third generation owners—schooled in global business best practices—are assuming management responsibilities from their elders and want to open their boards to professional directors and adopt other necessary elements of sound corporate governance.

As the transition occurs, here are some steps toward reforms:

- **Establish a "family constitution"**
- **Establish a family employment policy–and separate family members' rights and responsibilities as shareholders and as employees**
- **If the firm will not pay dividends, set up a fund or other mechanism to buy out family shareholders who prefer, for example, annuity income over owning a growth stock**
- **Create a succession plan for owner/founder/CEO/chairman**
- **Develop transparent systems for financial accounting, management accounting, human resources, and strategy development**
- **Create a board which can seriously add value to the business itself**

Source: IFC
www.ifc.org

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Next issue:

Bulgaria Launches Corporate Governance Code — On the brink of Bulgaria's accession to the European Union, the country adopted a Corporate Governance Code in October 2007. The task force drafting the Code looked to the Global Corporate Governance Forum for technical and practical advice on how to develop, implement, and monitor a Code.