Corporate Governance Instruction Sheet*

1. What is Corporate Governance?

Corporate governance refers to the structures and processes for the direction and control of companies and concerns the relationships among the management, Board of Directors or Supervisory Board, controlling shareholders, minority shareholders and other stakeholders. Good corporate governance contributes to sustainable economic development by enhancing the performance of companies and increasing their access to outside capital. [1]

2. Why Corporate Governance Matters for our Investee Companies

- **Access to Capital**. An increasing amount of empirical evidence indicates that well-governed companies receive higher market valuations. Improving corporate governance will also increase other capital flows to companies in developing countries: from domestic and global capital; equity and debt; and from public securities markets and private capital sources.

- **Improving Performance**. Good corporate governance leads to better performance for our investee companies. Improved governance structures and processes help ensure high quality decision making, encourage effective succession planning for senior management and enhance the long-term prosperity of companies, irrespective of the type of company and its sources of finance.

3. Why Corporate Governance Matters for Development Finance Institutions (DFIs)

- **Adding Value**. Corporate governance is a priority for DFIs because it presents opportunities to manage risks and add value to investee companies through increased performance and access to capital.
- **Reducing Investment Risk**. It is in the interest of DFIs to reduce the risk of our investments by improving the governance of investee companies.
- **Avoiding Reputational Risk**. DFIs assume a reputational risk if involved with companies with poor governance, and may become tainted by corporate scandals at investee companies.
- **Developing Capital Markets**. Improving corporate governance contributes to the development of the public and private capital markets.

4. Key Corporate Governance Tools

The DFIs Corporate Governance Toolkit includes 3 key corporate governance tools for analyzing the governance of DFIs' investee companies.

a) **Instruction Sheet.** The purpose of this Instruction Sheet is to introduce the concept of corporate governance; the value of good corporate governance for investee companies and DFIs; and to describe each of the key corporate governance tools, how they should be used, and who should be interviewed in the course of a corporate governance review.

b) **Corporate Governance Progression Matrix.** The progression matrix relates the five areas of governance (Commitment to Corporate Governance, Structure and Functioning of the Board of Directors, Control Environment and Processes, Transparency and Disclosure and Rights of Minority Shareholders) to four levels of achievement. The use of a matrix framework emphasizes the importance of ongoing improvements in the governance practices of investee companies, rather than trying to apply rigid and static minimum standards. The first level of the matrix represents the basic governance practices that investee companies might have in place. The next three levels describe more advanced practices towards which investee companies should gradually progress. In addition, the progression matrix allows investee

[1] This DFIs Corporate Governance Toolkit builds on the DFIs Corporate Governance Statement from 2007. Good corporate governance for some DFIs also includes business integrity issues which are not addressed in these materials.

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companies to self-assess their governance. *The progression matrix should be distributed to the investee company at the earliest opportunity.*

c) **Corporate Governance Questionnaire.** This list of questions establishes the basis for the corporate governance review of an investee company. This questionnaire is organized to correspond to the five areas of governance in the progression matrix. DFI investment staff should answer this questionnaire by collecting the relevant information from the investee company and from interviews during the appraisal of the investment opportunity.

In addition to these 3 key tools, the following sample and supportive documents can be used by DFI investment staff as needed:

d) Sample Corporate Governance Improvement Program. After completing the corporate governance review, DFI investment staff should summarize their key findings in the form of a Corporate Governance Improvement Program. This document will describe the main governance risks and opportunities of the investee company and suggest recommendations for improvement.

e) Sample Corporate Governance Section in the Internal Investment Approval Documents. This sample power-point slide can be used by DFI investment staff as a platform for addressing the key corporate governance risks and opportunities when deciding on a specific investment opportunity. The level of risk (low/moderate/high) is decided by DFI investment staff based on the findings of the corporate governance review.

f) List of Key Corporate Governance Terms. The purpose of this document is to provide definitions of key corporate governance terms from the progression matrix and the questionnaire.

5. Who to Interview?

A list of individuals who would normally be interviewed during a corporate governance review is provided below. It is important that DFI investment staff meet with those people who, as a practical matter, are responsible for establishing and maintaining the principal corporate governance framework, irrespective of their job titles. The corporate governance questionnaire matches the individuals to interview with each of the five areas of corporate governance.

- Representatives of controlling shareholders
- Representatives of other holders of significant blocks of shares
- Chairperson and members of the Board of Directors, including any independent Board members and the chairs of the audit and other special committees of the Board
- Chief Executive Officer
- Chief Financial Officer (or senior accounting officer)
- General Counsel (or senior lawyer)
- Corporate Secretary
- Chief of the Internal Audit function and, if relevant, chief of Internal Controls
- Chief of Investor Relations
- Independent External Auditors
- External Corporate Governance Advisors
- Minority Shareholders (especially those with past or current disputes with the Company)

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