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Efficient Business Governance – a Solution for a Sustainable Development

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Abstract

Considering the special interest shown towards the concept of corporate governance, in this paper. we want to reflect the degree of compliance of the banking companies listed on the Bucharest Stock Exchange (BSE) with the principles and provisions of the Corporate Governance Code, considering the importance of the banking sector in the financial system, the one that basically manages the liquidities in an economy. In order to achieve the purpose of this research, we analysed both annual and sustainability reports issued in the period 2017-2018 by the listed entities in the banking field in Romania included in the study by using a scoring system to rank the compliance with the principles and provisions of CGC regarding the responsibilities of the board, risk management and internal control system, fair rewards and motivation and building value through investors relations. Our analysis reflects that, although the provisions and principles issued by the Corporate Governance Code are not mandatory for the listed companies, they are largely implemented in the activity of banking companies in order to increase the level of transparency and trust, essential elements for a sustainable development.

Keywords: corporate governance, principles, BSE.

JEL Classification: M42, G34

1. Introduction

Corporate governance, or the way entities are controlled and managed, represents a concept that requires continuous improvement given the globalization of the economic environment, the major risk for a new financial crisis that may affect the world economies and also the resounding financial scandals that have imprinted on the credibility of the information published by companies.

According to the US Government Environmental Protection Agency, EPA, between 2009-2015, car manufacturer Volkswagen sold worldwide about 11 million cars equipped with illegal software meant to report lower fuel consumption

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and lower emissions than in reality. Following this scandal, Volkswagen became the target of multiple investigations and the share price fell sharply. As a result, the Chairman of the Board of Directors resigned and other board members were suspended.

Considered a symbol of the failure of control measures and of corporate fraud, the famous Enron case cannot go unmentioned. The company overestimated its profit and underestimated its debt, thus affecting the lives of many people involved in the activity of the energy company and of those who invested in its shares, given that the company's share price dropped from 90 dollars to only 50 cents over a very short period of time. In this situation as well, among those involved in the scandal we can mention the founder of the company, the CEO, the CFO and the audit and consulting company Arthur Andersen, which provided consulting and performed both internal and external audit, thus compromising the auditor's independence.

The Parmalat scandal broke when the Italian authorities discovered that billions of euro from the company funds were hidden, (one of the entities in which the funds had been diverted being called suggestively ”Bucanero” − "Black hole" − so, in this case, the management that committed the fraud showed cynicism) the debts were undervalued and the accounts recorded forged documents. Following the controls put in place, both the company president and the executive directors were arrested.

Financial scandals are also encountered in South Africa, an example being the companies run by the Gupta family, who, under the inefficient supervision of the auditor, used public funds for personal purposes.

As it can be noticed from the examples above, in America, Europe and also Africa resounding financial scandals with significant impact for society, generated by the participants involved in the management of companies took place, thus reflecting the need of an efficient business governance.

2. Problem Statement

A first definition of corporate governance dates back to 1992. In the view of the specialist A. Cadbury who elaborated the Cadbury report in the UK, corporate governance reflects “the set of rules by which a company is directed and controlled”, and the conclusions of the report reflect that corporate failures were due to the inefficiency of the internal control system.

According to the OECD “A good corporate governance is not an end in itself, but a means to support economic efficiency, sustainable growth and financial stability. It facilitates companies' access to capital for long-term investment and helps ensure that shareholders and other stakeholders who contribute to the success of the corporation are treated fairly.” The corporate governance is defined as “a set of relationships between a company's management, its board of directors, its shareholders and other stakeholders”, also providing “the structure through which the objectives of the company, as well as the means of attaining those objectives and monitoring performance are determined”.

According to Professor Feleagă, corporate governance represents a set of "rules of the game" by which companies are managed and supervised by the board of directors, in order to protect the interest of all stakeholders (Feleagă et. al., 2011).

Professor Bunget O., quoted by Apostol C. (Apostol C., 2015: 21) states that corporate governance is primarily concerned with the management of the company and its structures, but it also includes issues regarding social responsibility and the ethics of business practices. (Bunget et al. 2009: 18).

The financial crisis between 2008-2012 has engulfed the global economy and has caused many bankruptcies in recent years, which should give greater importance to the way entities are managed and controlled. The most important sector and the first one affected was the credit institutions - the ones that basically manage the liquidities in an economy. Moreover, the financial-accounting frauds that can occur in the absence of an efficient business governance can have a major impact on the achievement of the economic-financial performances of companies, see the case of BRD from 2007 when the bank was very close to collapse due to a trader's transactions with derivatives that have bypassed internal control systems.

In this context, corporate governance should be seen as an essential element for the development and improvement of economic efficiency and efficacy, as an efficient system by which companies are directed, managed and controlled provided the principles issued by the OECD are respected.

3. Research Questions/Aims of the research

In this paper, we aim to reflect the degree of compliance of the banking entities listed on BSE with the principles and provisions of the Corporate Governance Code, by using the data issued in 2017 and 2018 by the companies included in the study, BRD, Transilvania Bank and Patria Bank.

4. Research Methods

We used a scoring system that reflects the extent to which the entities included in our study comply with the provisions and principles of the CGC.

Taking into account the fact that in the Comply or explain statement the companies have three options through a self-assessment that reflects the full compliance, partial compliance or non-compliance, the following table reflects the scoring system used according to the response published by the studied companies:

Table 1. Conformity marks

Conformity mark	Significance
3	Full compliance with the principles and provisions
1	Partial compliance
0	Non-compliance

Source: author's own projection

5. Findings

There isn't a certain model for an efficient corporate governance, but complying with the OECD principles can be a competitive advantage and attract new investors into the company, given that they decide to place their capital within entities that apply high standards of governance in order to ensure the profitability of their investments.

The Bucharest Stock Exchange re-established in 1995, after a period of suspension during the communist regime, represents the main stock exchange in Romania that drafted in 2001 the first Corporate governance code. A new code was developed in 2008, based on the OECD principles, which came into force in 2009 and was voluntarily implemented by the listed companies. Based on the "Apply or Explain" statement, listed companies declare their compliance or non-compliance with the principles of the Corporate Governance Code. The last code issued by BSE dates back since 2015 and replaces the original code issued in 2001 and the one revised in 2008.

The recommended principles, which mainly concern the access of investors to information and the protection of the shareholders' rights, encouraging entities to build a strong relationship with their shareholders and other stakeholders, are structured in four sections as follows:

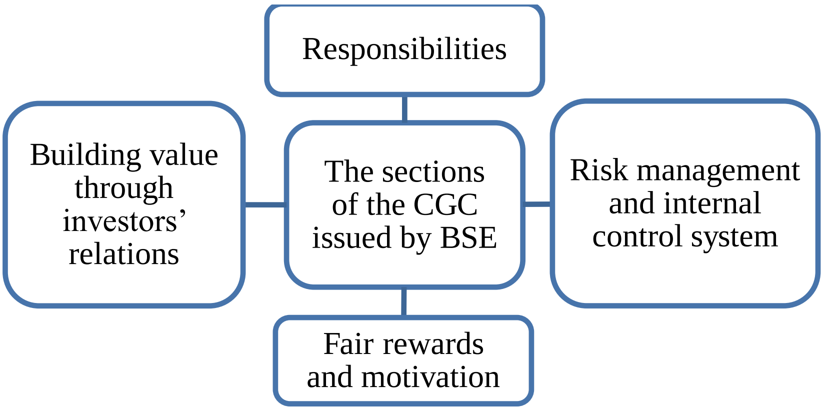

Figure 1. The sections of the CGC issued by BSE
Source: authors own elaboration

The provisions of the CGC and the way in which they are respected by the banking entities listed on the BSE are reflected below:

SECTION A – RESPONSIBILITIES – 11 Pillars

Figure 2. Section A of the CGC issued by BSE
Source: authors own elaboration after BSE CGC

The way in which the provisions of section A of the Code are respected by the listed entities can be graphically reflected as follows:

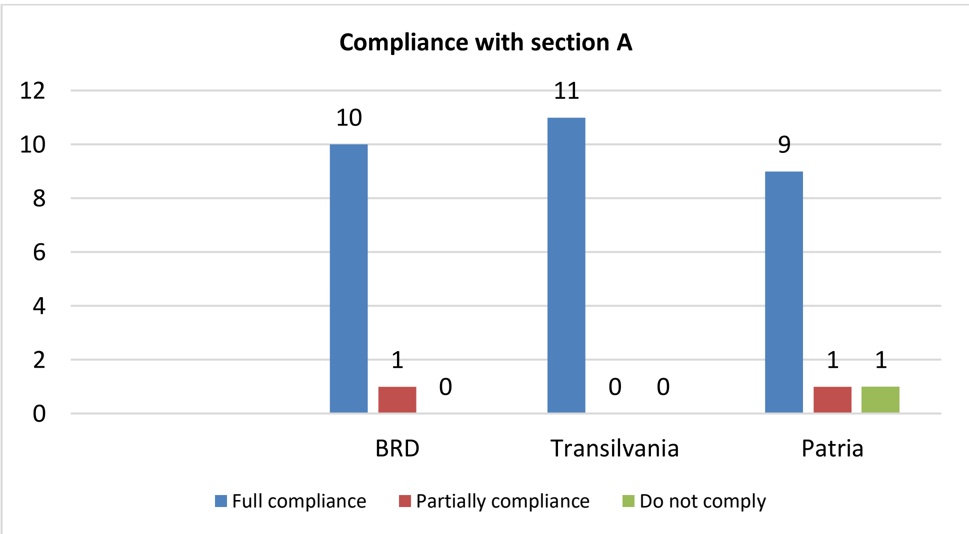

Figure 3. Entities compliance with section A
Source: authors own elaboration

SECTION B - RISK MANAGEMENT AND INTERNAL CONTROL SYSTEM – 12 Pillars

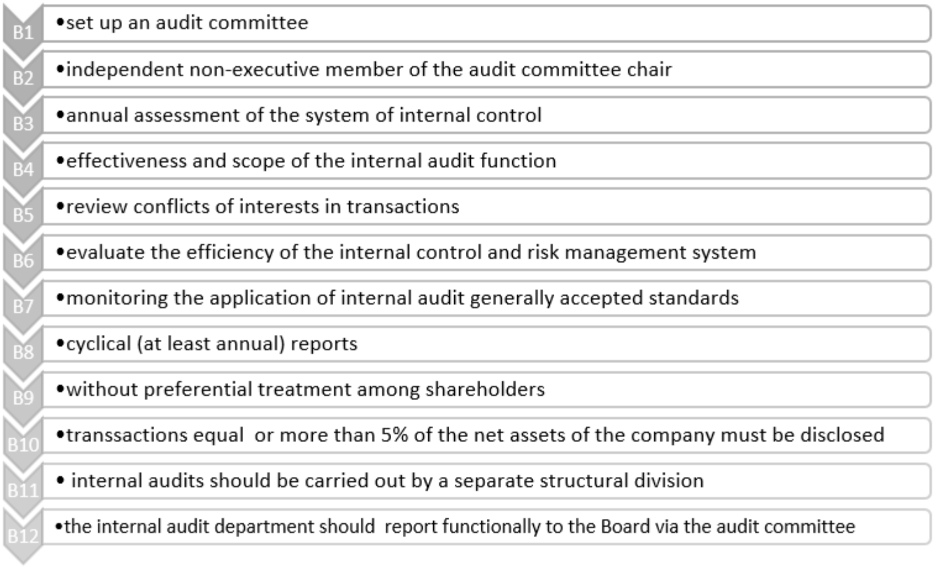

Figure 4. Section B of the CGC issued by BSE
Source: authors own elaboration after BSE CGC

The way in which the provisions of section B of the Code are respected by the listed entities can be graphically reflected as follows:

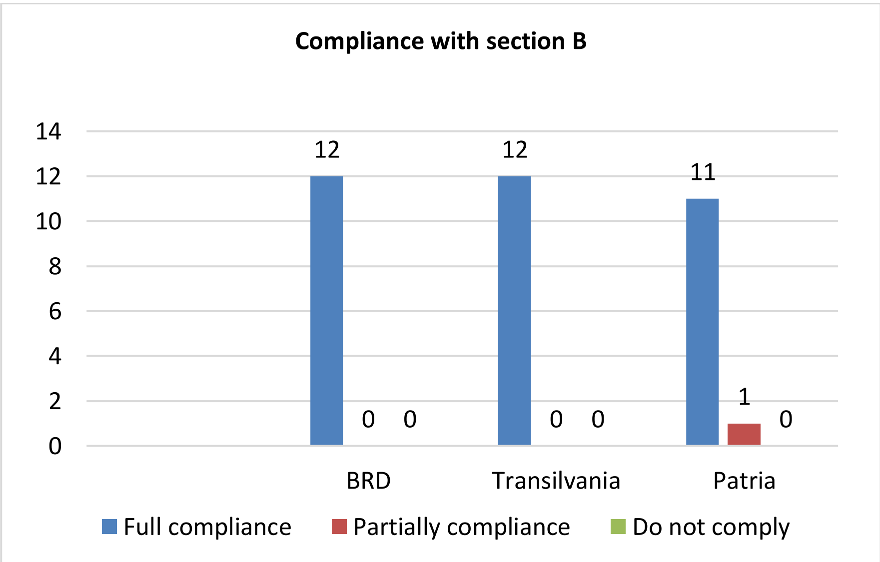

Figure 5. Entities compliance with section B
Source: authors own elaboration

SECTION C - FAIR REWARDS AND MOTIVATION – 1 PILLAR

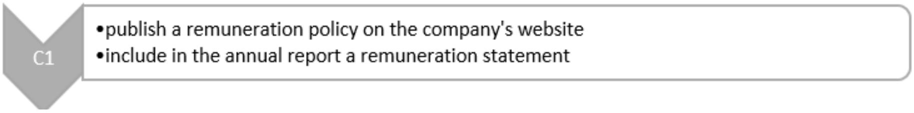

Figure 6. Section C of the CGC issued by BSE
Source: authors own elaboration after BSE CGC

The way in which the provisions of section C of the Code are respected by the listed entities can be graphically reflected as follows:

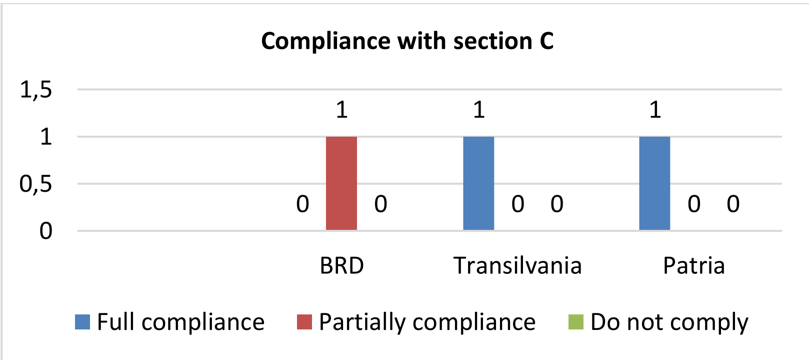

Figure 7. Entities compliance with section C
Source: authors own elaboration after BSE CGC

SECTION D - BUILDING VALUE THROUGH INVESTORS' RELATIONS – 10 PILLARS

Figure 8. Section D of the CGC issued by BSE
Source: authors own elaboration after BSE CGC

The way in which the provisions of section D of the Code are respected by the listed entities can be graphically reflected as follows:

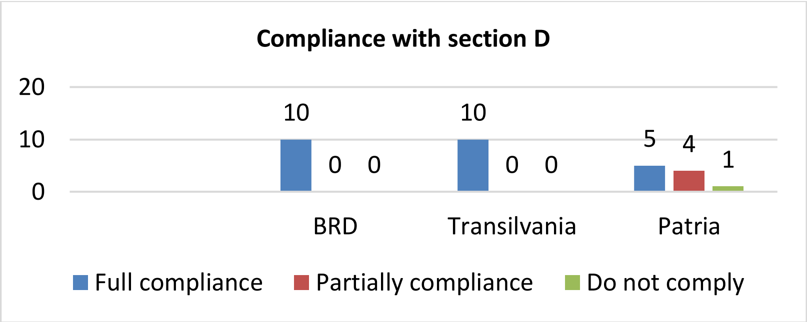

Figure 9. Entities compliance with section D
Source: authors own elaboration

Using the conformity marks, the overall perspective of the compliance of the entities in the banking field listed on the BSE with the provisions of the Corporate Governance Code, highlights the following level of conformity:

Table 2. Level of conformity with the Code s provisions

Category	Total CGC score	BRD	Transilvania	Patria
Section A score	33	32	33	28
Section B score	36	36	36	34
Section C score	3	1	3	3
Section D score	30	30	30	19
TOTAL Score	**102**	**98**	**102**	**84**
Conformity level	**100%**	**96.08%**	**100%**	**82.35%**

Source: authors own elaboration

As can be seen from the figure presented above, Transilvania Bank fully (100%) complies with the provisions of the Corporate Governance Code. Of the 34 provisions, BRD fully complies with 32, which means a 94% compliance, and 2 (6%) provisions of the Code are only partially respected. In the case of Patria Bank, (the most recently founded bank) the provisions of the Code are fully respected in a proportion of 76%, 6 (18%) provisions are partially complied and 2 (6%) provisions are not respected at all.

Analysing the Corporate governance statements and our results, we can conclude that although they are not mandatory, the provisions of the Code are largely respected and implemented within the three entities included in our study, an outcome that can represent a competitive advantage in this field. From our results, we can state, in line with Dumitrașcu et al. (2019), that in order to achieve a sustainable development, any company needs to find the balance between financial and non-financial performance.

6. Conclusions

The economic and social transformations, the registered bankruptcies, the financial crisis that affected all the economies, as well as the resounding frauds that took place have raised the interest for the significance of the corporate governance concept. It is becoming increasingly obvious that both investors and their interests are protected by an effective governance system that aligns with the practices and principles recommended by means of regulations.

The main aim of this paper was to study the compliance of banking companies listed on the Bucharest Stock Exchange with the principles and provisions of the Corporate Governance Codes issued by the main stock exchange in Romania. We believe that the ease of access to additional funds, the increase of transparency in reporting, the sustainable development in the context of globalisation and the increase of the market value of the company are the benefits of an efficient corporate governance system that can represent a competitive advantage to any economic entity. The study undertaken showed that the analysed companies comply largely with the provisions and principles of the codes, which reflect the importance given to this concept by which companies are controlled and managed. This, basically, contributed to overcoming the impasse of the Romanian banks, for example, during the economic crisis from 2008-2012 and beyond.

We are aware that this compliance with the principles of corporate governance also entails significant costs. We can include here the costs of hiring independent non-executive directors or of reporting relevant information to stakeholders, but the economic entity must adopt a system of corporate governance that allows obtaining benefits that exceed costs.

Also, the formalism of these statements of the entities must be considered, while we are aware of the limits of our study regarding the content and the way in which the analysed entities have a pro-active attitude regarding governance. A sustainable developing economy must be based on entities in which decisions and the governance system works effectively. Often, behind a formal conformity we do not find a well-balanced style of governance based on trust and transparency and balance between stakeholders - as a sine qva non condition for a successful corporate governance - as we have tried to outline the acceptance of the corporate governance term.

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