Measuring Transparency of the Corporate Governance in Slovenia

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Abstract: Several corporate governance indices and ratings were developed in order to measure the level of corporate governance quality. One of indices recently developed is the SEECGAN index. SEECGAN Index of Corporate Governance (hereinafter SEECGAN Index) was created and presented in 2014 as a result of the joint efforts of the members of the South East Europe Corporate Governance Academic Network. Unlike other measures of corporate governance commonly used in different studies, this index captures all major aspects of corporate governance. The SEECGAN Index of Corporate Governance covers seven categories that are: 1) Structure and Governance of Boards; 2) Transparency and Disclosure of Information; 3) Shareholders’ Rights; 4) Corporate Social Responsibility; 5) Audit and Internal Control; 6) Corporate Risk Management; 7) Compensation / Remuneration. In the paper, we present the preliminary research on transparency and disclosure of information.

Keywords: corporate governance, corporate governance index, transparency

1 Introduction

A wave of corporate scandals at the beginning of the millennium has made corporate governance an important and often discussed topic in political, professional and academic spheres. Namely, common and central feature to these scandals is the assumption that somehow corporate governance is to blame (e.g., Larcker and Tayan 2011). Also for this reason, research in corporate governance field is concentrated around the main question of good governance, which is the one that considers interests of different groups of stakeholders as much as possible. Many research studies emphasized the role of transparency and disclosure in reducing information asymmetry between insiders (management or majority shareholders) and outsiders (minority shareholders, creditors, and other stakeholders) (e.g., Bauwhede and Willekens 2008; Healy and Palepu 2001). Greater transparency and better information provision on capital and control structures keep corporate stakeholders better informed about the way a company is being managed (Patel and Dallas 2002) and are important means to restore public trust in capital markets (Bauwhede and Willekens 2008). Studies also suggest that better disclosure has a positive impact on the efficient functioning of capital markets (e.g., Healy and Palepu 2001; Patel and Dallas 2002). Transparency and disclosure are therefore recognized as important components of the corporate governance quality.

It is therefore not surprisingly that a key aspect of governance debate at EU level is that it is supposed to stimulate corporate transparency in the integrated European market (Bauwhede and Willekens 2008). In most EU member states states the compliance with corporate governance codes and disclosure on corporate governance systems and practices is largely voluntary (i.e., “comply or explain” disclosure regime), although some countries, such as UK and Italy required companies to disclose whether they complied with a (national) corporate governance. In the contrast to “comply or explain” approach, the legislated mandatory governance model (i.e., the “one size fits all” corporate governance regulations) of which the most well-known is the SOX-based regime in the US, prescribes the same corporate
governance practices for all types of companies (Bauwhede and Willekens 2008; Luo and Salterio 2014; Renders and Gaeremynck 2012). However, many scholars questioned the “one size fits all” approach and its impact on improving corporate performance (e.g., Larcker and Tayan 2011).

Many research studies exist on corporate governance quality, and transparency and disclosure practices (e.g., Larcker and Tayan 2011; Patel and Dallas 2002; Sheridan et al. 2006) in different countries. However, we are lacking research on these topics in transition countries. Therefore, the main goal of our research is to broaden our understanding on transparency and disclosure practices by conducting research on the sample of public companies in Slovenia. The research on transparency and disclosure of information is a part of broader research on corporate governance quality, which is still going on. The research results presented in this paper are therefore of preliminary nature.

2 Corporate Governance

Corporate governance is recognized as being a key business discipline that can contribute to the financial stability and growth of any corporation, or, if ignored, can lead to the downfall of corporations - both large and small (Beckley and Parker 2005).

Corporate governance is needed because more detailed information about corporate projects allow investors to assess the corporate growth potential better and to invest their money into companies that can generate the highest returns. Therefore, if all companies were to conceal information about their activities, a more inefficient allocation of capital would arise, leading to lower economic growth. Hence, a re-distribution of wealth between competing companies caused by a higher level of disclosure seems less harmful for the economy than the misallocation of capital caused by the lack of transparency. As such, mandatory rules that impose more disclosure enable economies to achieve a more optimal outcome (Martynova and Renneboog 2010).

2.1 Good Corporate Governance and Transparency

Formal legislation, a series of formal regulations and informal guidelines, recommendations, codes and standards of corporate governance have been established that try to determine good governance and to prevent potentially self-interested managers from engaging in activities detrimental to the welfare of shareholders and stakeholders. (ECGI Research, 2015)

Adopting a specific corporate governance regulation is that it forces companies to commit credibly to a higher quality of governance (Becht et al. 2005). Even if companies initially design efficient governance rules, they may break or alter them at a later stage. Investors anticipate this and are willing to provide firms with funds at lower costs only when companies find ways to commit credibly to good governance.

However, credible pre-commitment mechanisms may be expensive or unavailable in countries lacking an effective institutional framework. For instance, a well-functioning infrastructure (in terms of internal control structures, audit mechanisms, voting procedures at the annual meetings etc.) is required to enable investors to verify the information that companies disclose (Doidge et al. 2007).

Investors believe that good corporate governance reduces risk and leads to improved shareholder value. Historically, it is difficult to quantify improvements in shareholder value that is attributable directly to corporate governance improvements and/or good behaviour (Beckley and Parker 2005).

Transparency principle in corporate governance is generally used by the public companies. Transparent annual reports bring positive results to the shareholders, as well as other stakeholders,
such as employees, suppliers, local community, etc., since it supports the level of the information to the interested public in general (Dewing and Russell 2004).

Business information, business and yearly reports about the results of the company performance and other company written statements, (such as Corporate Governance Statements) create an information, prepared by the company management and supervisory bodies, which show their attitude, regarding the communication with the interested investors, stakeholders and employees. If the obligatory and other company data’s are exchanged with the outside groups that are interested about the way that company performs its activities, than such an approach creates the basis for the transparent company. If the company responsible bodies creates the open and transparent inside and outside communication with the interested participants, than such a way of communication becomes a way and a part of general company corporate governance policy. Many European states have already recognized the importance of the transparency. Transparency is a method, used also on the field of long-term sustainability and company social responsibility (Djokic 2015).

2.2 Measuring the Corporate Governance Quality

Measuring the quality of corporate governance could be an important activity in the process of developing an effective corporate governance model. It is still a relatively new concept (Tipurić et al. 2014). Different governance ratings have been developed by consulting companies (e.g., Risk Metrics/ISS, Governance Metrics International (GMI), The Corporate Library (TCL)) that aim at ranking companies according to the set of criteria that they believe measure governance adequacy and effectiveness. Academic researchers have also put considerable efforts toward the development of models to measure governance quality. The typical model takes the form of a corporate governance index that aggregates several input variables into single metrics (e.g., Larcker and Tayan 2011).

Researches, which deal with the questions of good corporate governance, are concentrated around the main question of good governance, which is the one that considers interests of different groups of stakeholders as much as possible. Especially important issues refer to relationships between relevant stakeholders groups and top management. Owners (shareholders) are considered only one among different groups of stakeholders, even though they are in certain environments among the most influential ones. In the USA and United Kingdom the shareholder-centric view prevails, which holds that the primary responsibility of a company is to maximize shareholders wealth. Other countries tend toward a stakeholder value view, which holds that obligations toward stakeholders such as employees, suppliers, customers, and local communities should be held in equal importance to shareholder returns. It means that the governance system that maximizes shareholder value might not be the same as the one that maximizes stakeholder value (e.g., Larcker and Tayan 2011).

Several corporate governance indices and ratings were developed in order to measure the level of corporate governance quality. One of the recently created and applied is the SEECGAN Index.

2.2.1 SEECGAN Research – Slovenia 2014 and the SEECGAN Index

In order to measure a level of good governance practices implementation and to verify whether Slovenian companies perform better with regard to that, the SEECGAN Index of Corporate Governance was applied.

The SEECGAN Research – Slovenija 2014 (Djokic et al. 2014) has been realized in the Republic of Slovenia (RS), based on the SEECGAN index. Publicly accessed data's in the annual and business reports, as well as the articles of association and the other applicable internal acts of the Slovenian
public companies, listed on Ljubljana Stock Exchange, have been scrutinized by using the Index methodology.

The SEECGAN Index of Corporate Governance (hereinafter SEECGAN Index) was created and presented in 2014 as a result of the joint efforts of the members of the South East Europe Corporate Governance Academic Network - SEECGAN (Tipurić et al. 2014). The index has been introduced in several countries (i.e., Croatia, Bosnia and Herzegovina, Serbia, Montenegro, Slovenia and Macedonia). The research on the basis of the Index has been finalized in Croatia and it is approaching the final phases of the overall analyze on the whole scale in Slovenia. SEECGAN Index measures the following seven categories:

1) Structure and Governance of Boards;
2) Transparency and Disclosure of Information;
3) Shareholders' Rights;
4) Corporate Social Responsibility;
5) Audit and Internal Control;
6) Corporate Risk Management;
7) Compensation / Remuneration

These seven categories are represented by a total set of 98 corresponding questions.

We have been interested, if the Slovenian public companies recognized and shared the above understandings in the previous years of their operation. An analyse has been provided to find out what are the conditions for the realisation of the above goals through of the public company reporting in the Republic of Slovenia. (RS) Annual reports for the year 2013 and other public acts and information that have been communicated to the public have been analysed to evaluate the non-financial information from the particular public company, which shares are listed on the Ljubljana Stock Exchange (LJ SE List September 2014 – Februar 2015).

In the contribution, we present the results of preliminary research on transparency and disclosure in the Republic of Slovenia.

3 Measuring Transparency of the Corporate Governance in Slovenia

3.1 Some Previous Transparency Researches in Slovenia

The Republic of Slovenia (the RS) has achieved substantial legal progress in the field of disclosure and transparency of public companies in the last 10 years. Disclosure and transparency were in RS introduced by imperative rules of law and soft law (Djokic 2013). The combination of both techniques established a legal basis that helped to improve corporate governance of public corporations, not only in words but also in practice. The use of techniques of obligatory disclosure of non-compliance with the Code provisions seems to be more efficient than previous regulation techniques without such obligation. The progress has been evaluated, regarding the corporate information offered to the public and shareholders.

The frequency of disclosure and transparency of the data regarding the corporate governance issues and the potential conflicts of interest in this field from the years 2005 to 2010 have been scrutinized in the annual reports of Slovenian public joint-stock companies by the researches (SDA Research 2007, 2010). The researches illustrated that the practice in the RS is following the legislation demands and has been developing in harmony with the regulations of the ZGD-1-UPB3 2009 and the provisions of the Slovenian CG Codes. The historical overview and a comparative analysis have proved that the
disclosure and transparency of corporate information in public companies have been on the increase (Djokic 2012).

3.2 Some Transparency Results by the SEECGAN Research – Slovenia 2014

3.2.1 Sampling and Data Collection


The public information (general deeds, companies acts, web pages, etc.) have been scrutinized and the information gathered to be able to apply the methodology and collect the non-financial information about the following questions:

- Has the company developed and publicly disclosed its own Corporate Governance (CG) Code?
- Has the company adopted some official CG Code (CG Code of the Chamber of Commerce, CG Code of the Stock Exchange or similar)?
- Does the company disclose the Statute and/or Articles of Association (Incorporation) on its web page?
- Does the Company disclose the extent to which it is complying with its Corporate Governance Code (does it explain possible deviations from the Code)?
- Has the company adopted the Transparency Policy and the Information Disclosure Policy?
- Does the company disclose the Transparency Policy and the Information Disclosure Policy?
- Does the company disclose procedures for the disclosure of market sensitive information?
- Does the company website have all the information translated into English?
- Does the company disclose information on Related Party Transactions?
- Does the company disclose all periodic information (Annual, half-yearly and quarterly financial reports) in the legally binding period?
- Does the company disclose crucial strategy-related information relevant to its investors and stakeholders?
- Does the company publicly disclose information regarding the company's ownership structure on its website (top 10 shareholders, their names and percentage of shares as well as information on the number of other owners)?
- Does the company disclose information on other board memberships (when its board members sit on other corporate boards)?
- Does the company disclose a calendar of important events?
- Does the company disclose information on special relationships (if any) between shareholders?
- Does the company have a special section on its web page dedicated to Corporate Governance or Investors Relations (where all interested parties and stakeholders can find financial data,
ownership structure data, statute and articles of association, information on related party transactions, annual plans, CG Code etc.)?

3.2.2 Research Results

In this section we present the aggregated results of SEECGAN Index for all 22 companies included in the sample based on the data published in the year 2013 (Figure 1). The first category is divided in two sub-categories due to two-tier system applied in Slovenian public companies. The two-tier system is a corporate structure system that consists of two separate boards that work together in order to govern a business, the "Management Board", and the "Supervisory Board" each of these serves a particular purpose. The quality of transparency and disclosure of information is presented by the average value of this index category for all companies included in the sample (Figure 1) and by detailed illustration of transparency and disclosure practices quality of each company included in the sample (Figure 2).

Figure 1: SEECGAN Index for Slovenia

![SEECGAN Index for Slovenia](image)

The quality of corporate governance is evaluated as first-class, if the value of the SEECGAN index in particular segment or in total is higher than 7.5, good if the value is between 5.00 and 7.5, unsatisfactory if the value is between 2.5 and 5.00, and poor if the value is lower as 2.5. The data on the Figure 1 shows that the average value of the SEECGAN index (total) of the corporate governance quality of the listed companies in the Republic of Slovenia is good (5.49).
The transparency and disclosure of information of companies in the sample is evaluated as good with the average SEECGAN index of the companies' in this category being 6.62. The category of transparency and disclosure of information is ranked as the second best corporate governance category where the category of corporate risk management (with the average index 7.61) is ranked as the one where companies show the best results regarding the corporate governance practices.

Detailed analysis of transparency and disclosure of information of individual companies show that the transparency and disclosure of information is evaluated as first-class in eight companies where six companies are from prime quotation of Ljubljana stock exchange. Ten companies’ transparency and disclosure practices are evaluated as good and four companies display unsatisfactory transparency and disclosure practices. The Figure 1 shows that the most transparent company is Zavarovalnica Triglav PLC. The company reached the maximum SEECGAN index 10. The lowest score reached Kompas MTS PLC, which got the SEECGAN index in the category of transparency and disclosure 3.53. Companies have not published statutes, transparency policy, strategy and procedures of publication of commercially sensitive information. The graph shows that transparency gained a satisfactory level, in fact the average SEECGAN index of the companies’ is 6.62.

4 Conclusion

The research results on transparency and disclosure of information of Slovenian public companies show that corporate governance practices in the area of transparency and disclosure can be assessed on the average as good practices. However, detailed analysis of companies in the sample show that
differences in the quality of transparency and disclosure practices exist among examined companies. Future research should address these differences, their causes as well propose solutions for improving transparency and disclosure practices in Slovenian public companies.

The measuring of transparency and disclosure practices quality was a part of broader research on the corporate governance quality in Slovenian where the detailed analysis of research results is still going on (i.e., the SEECGAN Research – Slovenia 2014). We expect the final results for RS to be announced in September 2015. We believe that the SEECGAN Research – Slovenia 2014 will bring comprehensive, credible and quantified information and measurement, which will enable:

- Professional overview to the investors, shareholders, stakeholders and interested public;
- the comparison of the results in the region since the research on corporate governance quality applying the SEECGAN Index methodology is going in other SEE countries as well;
- improvements of the applied index based on the research results thus also enabling recommendations for improving corporate governance practices.

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