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## **2010 Review of the Implementation Status of Corporate Governance Disclosures: An Inventory of Disclosure Requirements in 21 Frontier Markets**

**Report by the UNCTAD secretariat**

### **Executive summary**

During the twenty-first session of the Intergovernmental Working Group of Experts on International Standards of Accounting and Reporting (ISAR), it was agreed that an annual survey to assess the state of reporting on corporate governance (CG) would be useful. This study continues to provide a picture of the current status of disclosure requirements by focusing on enterprises listed on stock exchanges in 21 ‘frontier markets’, i.e. developing countries with relatively small equity markets. The study was conducted by examining the corporate governance disclosure requirements of relevant laws and stock exchange listing rules, and comparing these with the ISAR benchmark of good practices identified in the 2006 UNCTAD publication *Guidance on Good Practices in Corporate Governance Disclosure*.

This study indicates that the frontier markets require significantly less information from listed companies than would be required in larger emerging markets or developed countries. It also identifies a number of common issues with regard to existing regulations on disclosure requirements. Addressing these issues could assist decision makers in these countries in strengthening their requirements in this area where appropriate in order to meet the expectations of capital providers based on good international practices with a view to facilitate investment to these countries.

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## Introduction

1. Corporate governance has been a key area of work of the Intergovernmental Working Group of Experts on International Standards of Accounting and Reporting (ISAR) since 1989 (E/C.10/AC.3/1989/6). At its twenty-first session, ISAR has requested UNCTAD to conduct an annual review of the implementation status of corporate governance (CG) disclosure. These studies have included examinations of the regulatory requirements of different markets, the actual disclosure practices of enterprises in selected markets, as well as more detailed individual country case studies. All these studies are conducted based on UNCTAD *Guidance on Good Practices in Corporate Governance Disclosure as a benchmark*. The objective of these studies has been to raise the awareness of regulators and other relevant stakeholders about the current disclosure practices on corporate governance issues. These studies intend to assist decision makers to examine a need and assess challenges for further improvements in this area in their countries in accordance with good practices in order to strengthen the ability of their capital markets to attract foreign investment, mobilize domestic resources and guard against financial instability.

2. The 2010 study examines corporate governance disclosure requirements<sup>1</sup> in a sample of developing countries referred to in the investment community as ‘frontier markets’. These countries typically have relatively small and or new equity markets.

3. Section I of the paper provides an overview of background and methodology; section II contains comparative data on disclosure requirements, along with detailed analysis by market and subject area; and section III provides analysis of main issues of existing regulatory requirements on corporate governance disclosures in the 21 selected countries.

4. The findings of this study show that most of the markets examined do not have mandatory disclosure rules in place for most of the items identified as good practices in the ISAR benchmark on CG disclosure. The findings suggest that many of the small markets in the study are still developing their regulatory infrastructure in the area of corporate governance. The analysis also highlights a number of areas where regulators can strengthen or clarify rules on CG disclosure. In particular, this paper maps out different existing models of disclosure requirements to assist countries in producing clear disclosure regulations of their own.

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<sup>1</sup> The examination of disclosure requirements in this review uses the same methodology applied in two earlier reviews, the “2007 Review of the Implementation Status of Corporate Governance Disclosure: An Inventory of Disclosure Requirements in 25 Emerging Markets” (TD/B/COM.2/ISAR/CRP.6, hereinafter the “2007 CG Inventory”); and the “2009 Review of the Implementation Status of Corporate Governance Disclosures: An Inventory of Disclosure Requirements in 24 Emerging Markets” (TD/B/C.II/ISAR/CRP.8, hereinafter the “2009 CG Inventory”).

## I. Background and methodology

### A. ISAR benchmark

5. The 2006 UNCTAD publication *Guidance on Good Practices in Corporate Governance Disclosure* forms a benchmark (hereinafter the “ISAR benchmark”) of over fifty disclosure items on corporate governance. The ISAR benchmark is the subject of occasional revisions and further refinement. For this study, revisions include the removal of two disclosure items, both of which were considered to substantially overlap with other disclosure items in the benchmark, and thus were seen as redundant. The first item removed was “*disclosure practices on related party transactions where control exits*” which was considered to substantially overlap with the disclosure item “*nature, type and elements of related-party transactions*”. The second item removed was “*number of outside board and management position directorships held by the directors*” which substantially overlapped with the disclosure item “*types and duties of outside board and management positions*”; these two disclosure items were therefore merged into a single revised disclosure item “*types and number of outside board and management positions*”.

6. As a result of these revisions, the ISAR benchmark used in this study contains 51 items in total. This set of 51 disclosure items are grouped into five broad categories, or subject areas, of corporate governance disclosure, and are presented and analyzed by category in section III below. These categories are:

- (a) Financial transparency;
- (b) Ownership structure and exercise of control rights;
- (c) Board and management structure and process;
- (d) Auditing;
- (e) Corporate responsibility and compliance.

### B. Selected markets

7. The sample of 21 markets examined in this study was drawn from the Frontier Markets Index produced by Morgan Stanley Capital International (hereinafter the “MSCI FM Index”).<sup>2</sup> MSCI is a leading commercial provider of financial information, including equity indices tracking publicly listed enterprises around the world. The MSCI Frontier Markets Index is designed to track the performance of a range of equity markets that have recently become more accessible to international investors. Table 1 below provides a list of economies included in the MSCI FM Index. Some of the countries in the MSCI FM Index were excluded from the present study because they have been covered in previous ISAR studies on the same subject.<sup>3</sup>

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<sup>2</sup> All MSCI FM Index data used in this study is based on the FM Index as of 18 January 2010. For up to date information on the MSCI FM Index please see: [http://www.msicbarra.com/products/indices/international\\_equity\\_indices/fm/](http://www.msicbarra.com/products/indices/international_equity_indices/fm/)

<sup>3</sup> Argentina and Jordan were covered in a 2009 study (TD/B/C.II/ISAR/CRP.8) available at: [http://www.unctad.org/en/docs/ciisarcpr8\\_en.pdf](http://www.unctad.org/en/docs/ciisarcpr8_en.pdf). Pakistan was also the subject of a detailed country study in 2009 (TD/B/C.II/ISAR/CRP.5) available at: [http://www.unctad.org/en/docs/ciisarcpr5\\_en.pdf](http://www.unctad.org/en/docs/ciisarcpr5_en.pdf)

**Table 1. The sample of 21 economies from the MSCI FM Index**

1. Bahrain	12. Oman
2. Bulgaria	13. Qatar
3. Croatia	14. Romania
4. Estonia	15. Serbia
5. Kazakhstan	16. Slovenia
6. Kenya	17. Sri Lanka
7. Kuwait	18. Trinidad & Tobago
8. Lebanon	19. Ukraine
9. Lithuania	20. United Arab Emirates
10. Mauritius	21. Vietnam
11. Nigeria	

### C. Research question and methodology

8. The research question applied to this sample was: which of the ISAR benchmark disclosure items are required to be reported to the public by enterprises listed on the major stock exchanges of each of the 21 markets studied? The study examined government laws and regulatory instruments as well as the listing requirements of major stock exchanges of these countries. The main elements of the methodology are:

- (a) Using the ISAR benchmark as a measure of disclosure requirements.
- (b) Disclosure should be mandatory, required by law or regulations or listing requirements. This study examines the existence of mandatory requirements in order to assess the role of regulators and stock exchanges in shaping CG disclosure practices.
- (c) Disclosure should be regular and periodic in nature and remain a company's continuing obligation after listing. Regular periodic disclosure after listing is necessary to provide investors and other stakeholders access to up-to-date information on corporate governance issues. This report included in its inventory of disclosure requirements only those requirements that related to regular periodic reporting, and excluded disclosure requirements that were one time in nature, such as disclosure in the course of incorporation or IPO proceedings.
- (d) Disclosure should be publicly available. For information to be useful, it must be available to current and potential investors, regulators, and other stakeholders. In effect, it must be available to the entire public. This report included in its inventory of disclosure requirements only those requirements that related to public disclosure, and excluded disclosure requirements that provided information only to regulators, stock exchanges or an explicitly limited scope of stakeholders.
- (e) This report does not measure the quality of disclosure within individual markets; rather it is a measure of the existence of regulations requiring the selected disclosure items.

### D. Sources of information

9. The research was performed primarily by using publicly available legal documents from the Internet, but in some cases relied on direct communication with regulators and or stock exchange officials. The legal sources generally included company law, financial market law, corporate governance codes and listing rules of stock exchanges. In regard to stock exchange listing rules, in countries with more than one stock exchange, the listing rules considered were the rules of the largest stock exchange in the country (by market capitalization).

10. A preliminary copy of the findings for each market was submitted to regulators or stock exchange authorities in that market for comment. A number of replies were received and incorporated

into the findings below. While every effort was made to be thorough in this research, this report cannot claim to have covered all applicable laws and regulations. The complete list of sources used, by market, is contained in annex I.

## II. Status of implementation of good practices in corporate governance disclosure at the regulatory level

### A. Disclosure requirements of 21 frontier markets

11. Table 2 below displays the results of the study within each of the five broad categories discussed in section I above. This grouping of the disclosure items allows readers to draw their own conclusions based on the importance they assign to a particular category or subject area and, within that category, a particular disclosure item. It also facilitates the analysis of the relative level of disclosure within each category.

**Table 2. Main findings of the inventory of disclosure requirements in 21 frontier markets**  
(Number of markets requiring this item)

Disclosure item	No. of markets (max.=21)
<b>Financial Transparency</b>	
Financial and operating results	21
Nature, type and elements of related-party transactions	15
Company objectives	10
Rules and procedures governing extraordinary transactions	9
Decision making process for approving related-party transactions	8
Impact of alternative accounting decisions	5
Critical accounting estimates	2
Board's responsibilities regarding financial communications	1
<b>Ownership Structure and Exercise of Control Rights</b>	
Availability and accessibility of meeting agenda	20
Changes in shareholdings	14
Control structure	13
Control rights	7
Ownership structure	6
Rules and procedures governing the acquisition of corporate control in capital markets	4
Process for holding annual general meetings	3
Control and corresponding equity stake	2
Anti-Takeover measures	1

<b>Disclosure item</b>	<b>No. of markets (max.=21)</b>
<b>Board and Management Structure and Process</b>	
Composition of the board of directors	15
Determination and composition of directors' remuneration	15
Role and functions of the board of directors	14
Material interests of senior executives and board members	14
Governance structures, such as committees and other mechanisms to prevent conflicts of interest	13
Composition and function of governance structures	12
Qualifications and biographical information on board members	10
Independence of the board of directors	10
Existence of procedures for addressing conflicts of interest among board members	9
Checks and balances mechanisms	8
Risk management objectives, system and activities	8
Professional development and training activities for board members	7
Performance evaluation process for board members	6
Availability of advisorship facility for board members or board committees	5
Compensation policy for senior executives departing the firm as a result of a merger or acquisition	5
Types and number of outside board and management positions	4
Duration of directors' contracts	3
Existence of succession plan for senior executives and board members	2
<b>Auditing</b>	
Internal control systems	9
Process for appointment of external auditors	5
Scope of work and responsibilities for internal auditors	4
Rotation of external auditors	4
Process for interaction with internal auditors	3
Process for interaction with external auditors	3
External auditors' involvement in non-audit work and fees paid to auditors	3
Duration of current external auditors	1
Board confidence in the independence and integrity of external auditors	1

Disclosure item	No. of markets (max.=21)
<b>Corporate Responsibility and Compliance</b>	
Mechanisms protecting the rights of other stakeholders	6
Policy and performance in connection with environmental and social responsibility	5
Policy on "whistle blower" protection	3
A Code of Ethics for the board and waivers to the ethics code	2
A Code of Ethics for company employees	2
Existence of employee elected director(s) on the board	1
Impact of environmental and social responsibility policies on sustainable development	0

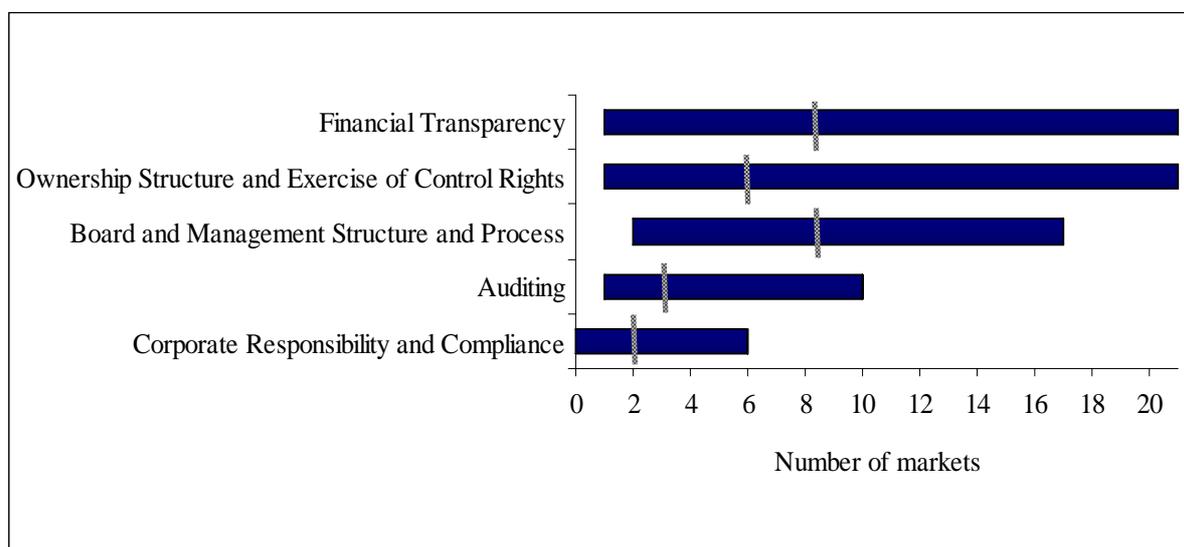
### General Overview

12. As shown in table 2, most of the items of the ISAR benchmark are not the subject of mandatory disclosure in most of the markets in this study. This stands in contrast to earlier studies by UNCTAD of larger emerging markets where most of the ISAR benchmark items were the subject of mandatory disclosure rules. For the 21 markets in this study, one-third of the ISAR benchmark indicators are the subject of disclosure requirements in slightly more than half of the markets studied. Only four markets in the study require half or more of the items in the ISAR benchmark. Despite the generally low number of required disclosure items in these markets, two individual items are nevertheless the subject of disclosure requirements in most or all of the countries studied: *financial and operating results* and *availability and accessibility of meeting agenda*.

13. Consistent with UNCTAD's earlier studies on this subject, the first three categories of disclosure items ('Financial transparency', 'Ownership structure and exercise of control rights', and 'Board and management structure and process') are more likely to be the subject of mandatory disclosure requirements than the last two categories ('Auditing' and 'Corporate responsibility and compliance').

14. Disclosure requirements existed in 10 or more markets for 4 out of 8 disclosure items in the category 'Financial transparency', 3 out of 9 items in 'Ownership structure and exercise of control rights' and 8 out of 18 items in 'Board and management structure and process'. In contrast, all of the disclosure items in the last two categories ('Auditing' and 'Corporate responsibility and compliance') were the subject of mandatory reporting rules in less than 10 of the markets in this study. The disclosure items in the category of 'Corporate responsibility and compliance' were required by the lowest number of markets, with one item (*impact of environment and social responsibility policies on sustainable development*) not required in any of the markets examined. Figure 1 below provides an overview of the maximum and minimum number of markets requiring individual disclosure items in each category.

**Figure 1. Overview of disclosure requirements by category**  
 (Maximum and minimum number of markets requiring disclosure items in this category – vertical line indicates the median number)



15. Figure 1 provides an illustration of the extent of mandatory disclosure requirements in each of the five categories. This analysis remains largely consistent with the findings of UNCTAD's 2009 inventory of CG disclosure requirements in emerging markets in so far as the relative order of the categories. One significant difference, however, is the overall lower level of disclosure requirements in frontier markets when compared with emerging markets. This lower level is indicated in both the very wide spread between the most often required items and the least often required items within each category, but also by the relatively low median number. In the 2009 inventory, for example, the least required items in three categories was still required by more than half of the markets in that study.<sup>4</sup>

16. Also consistent with the 2009 inventory, the categories of 'Auditing' and 'Corporate responsibility and compliance' are subject to the least number of disclosure requirements. As seen in table 2 below, disclosure items from these two categories make up the majority of the bottom 10 least prevalent disclosure requirements.

<sup>4</sup> The three categories are: 'Financial transparency' and 'Ownership structure and exercise of control rights' and 'Auditing'. See page 8 of the *2009 Review of the implementation status of corporate governance disclosures: an inventory of disclosure requirements in 24 emerging markets* (TD/B/C.II/ISAR/CRP.8).

**Table 3. Most prevalent and least prevalent disclosure items**  
(Number of markets requiring this item)

Top 10 most prevalent disclosure items required among 21 frontier markets	No. of Markets	Bottom 10 least prevalent disclosure items required among 21 frontier markets	No. of Markets
Financial and operating results	21	Control and corresponding equity stake	2
Availability and accessibility of meeting agenda	20	Existence of succession plan for senior executives and board members	2
Composition of the board of directors	15	A Code of Ethics for the board and waivers to the ethics code	2
Nature, type and elements of related-party transactions	15	A Code of Ethics for company employees	2
Determination and composition of directors' remuneration	15	Board's responsibilities regarding financial communications	1
Changes in shareholdings	14	Anti-Takeover measures	1
Role and functions of the board of directors	14	Duration of current external auditors	1
Material interests of senior executives and board members	14	Board confidence in the independence and integrity of external auditors	1
Control structure	13	Existence of employee elected director(s) on the board	1
Governance structures, such as committees and other mechanisms to prevent conflicts of interest	13	Impact of environmental and social responsibility policies on sustainable development	0

17. Of the ten most prevalent disclosure items, five of them are from the category “board and management structure and process”, which differs with the findings of the 2009 inventory of emerging markets in which the highest category of disclosure requirements was that of “ownership structure and exercise of control rights”. Moreover, while seven of top ten most prevalent disclosure items are required in all 25 of the emerging markets in the 2009 inventory, the present study finds that only one of the top ten items is required by all 21 of the frontier markets examined.

18. As far as the bottom ten least prevalent disclosure items are concerned, the number of frontier markets requiring disclosure is significantly lower than the bottom ten least required items among the 25 emerging markets in the 2009 inventory. The number of frontier markets requiring individual items in the bottom ten range from 2 to 0, which is much lower than the same data for emerging markets where the number of markets for the least required items ranged from 13 to 2.

## **B. Gap analysis of disclosure requirements**

19. Table 4 below provides another view of the main findings of the study, illustrating where gaps exist in corporate governance disclosure requirements. The top line of the table lists the numbers of the 51 disclosure items of the ISAR benchmark, grouped according to general category; these numbers correspond to the complete list of disclosure items found in annex II. The blank or white spaces in the table indicate an absence of a mandatory requirement for disclosure of that item. The markets in the table are listed from top to bottom in order of the total number of disclosure items required.

20. This presentation of the data provides an overview of what disclosure items are required in each market. As noted above, the disclosure items in the categories “financial transparency”, “board and management structure” and “ownership structure” are the subject of more disclosure

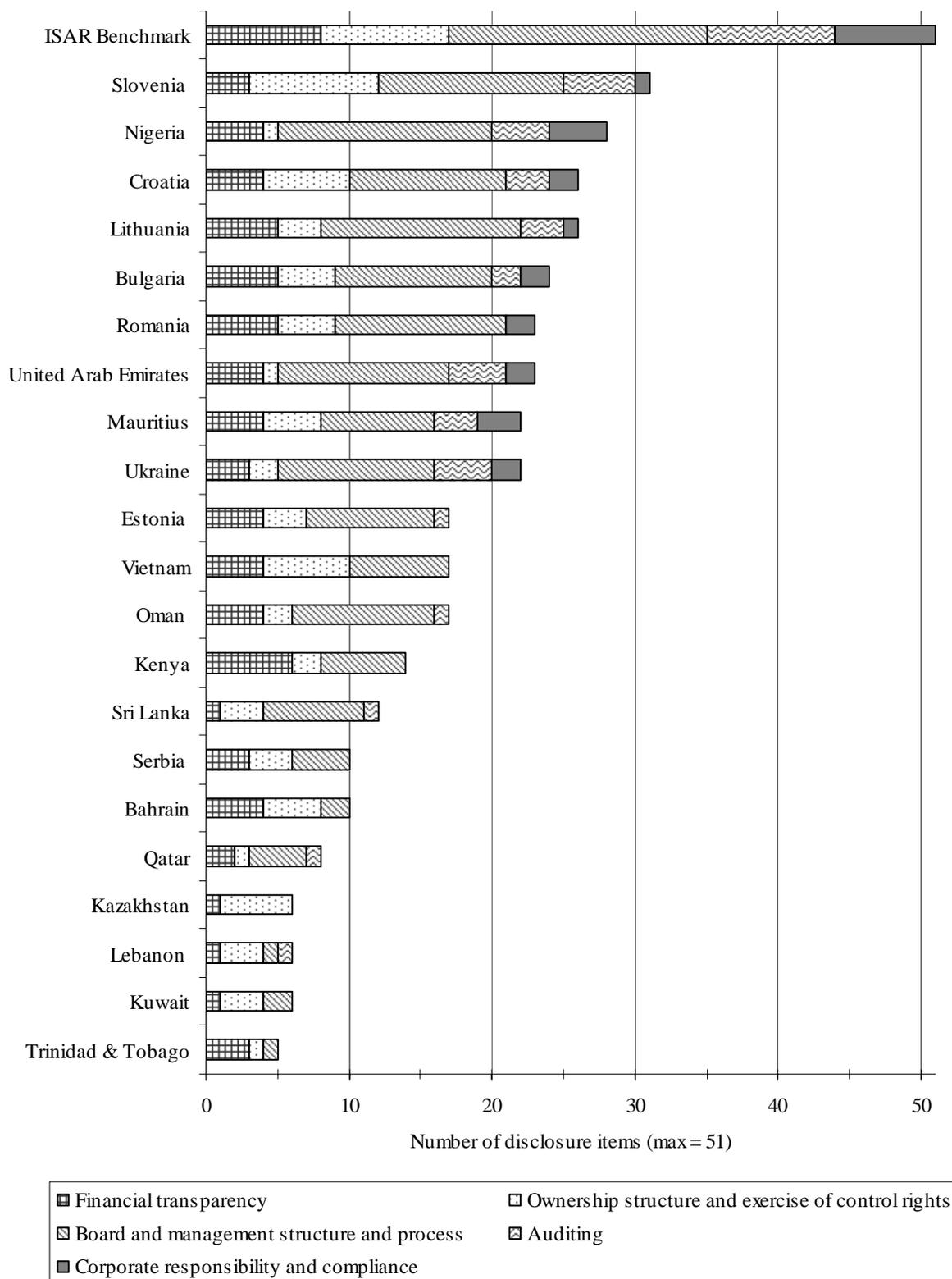
requirements in the countries examined. In contrast, some markets have few or no disclosure requirements in the categories of “auditing” and “corporate responsibility and compliance”.



**C. Comparison of disclosure requirements between markets**

21. Figure 2 presents an overview of the number of disclosure items required for each category of disclosure in each of the 21 frontier markets reviewed. For comparison purposes, the figure also includes the number of disclosure items for each category of the ISAR benchmark.

Figure 2. Disclosure requirements by market and category



22. The figure indicates that the majority of frontier markets required less than half of disclosure items of the ISAR benchmark. Only one market stipulates more than 30 items. The numbers of items required in eight markets fall between 20 and 30 items. There are seven markets which have between 10 and 20 required items. Five countries require disclosure of less than 10 of the

ISAR benchmark items. In comparison with emerging markets, figure 2 suggests that many frontier markets have levels of mandatory corporate governance disclosure that are significantly lower, not only in terms of the number of disclosure items covered but also the range of topics (or categories) addressed.

### III. Main challenges of existing disclosure requirements

23. This study helped to identify the following main challenges with regard to existing disclosure requirements on corporate governance.

#### A. Vague or generalized disclosure rules

24. An issue found among many countries' CG disclosure rules is lack of specificity about the information that is to be disclosed. Some rules require overly generalized statements on corporate governance that lack the kind of specific information that might be useful to investors and other stakeholders. There are two common types of overly generalized disclosure regulations found in this research:

- (a) *The regulation requires vague or undefined information.* For example, some regulations require that listed companies publish a "corporate governance report" or disclose "material information" of corporate governance without setting forth the content of such reports in any detail, or providing any criteria as to the materiality of information. As a result, disclosure regulations that contain a high-level of generality, or non-precise language, without specific reference to other relevant authoritative sources of reference, in most cases do not, in practice, require any specific information to be disclosed.
- (b) *The regulation requires a general statement of compliance with the CG code.* Some challenges of application of this requirement are discussed in more detail below (see section III.D under '*general disclosure statements versus specific itemized disclosure*').

25. To improve the usefulness of CG disclosures, regulators could avoid requiring vague or overly-generalized information, and work towards clarifying what type of disclosures are required. For example, one country in this study integrated within its CG code an annual questionnaire specifying the disclosure of compliance. Similarly, another country issued a *Disclosure form concerning the compliance with the Corporate Governance Code for the Companies Listed on [the national stock exchange]*. Both methods provide enterprises with detailed guidance on specific corporate governance disclosure requirements.

#### B. "Comply or explain" principle: challenges in application

26. Many countries based their CG disclosure requirements on "comply or explain" principle which is a central element of many national corporate governance codes. It provides useful flexibility in code implementation, however its practical application can lead to complexities and confusion when combined with other factors discussed in this section, such as voluntary codes and overly generalized requirements.

27. The "comply or explain" principle was first put forward in the Cadbury Code in the United Kingdom as a practical means of establishing a single code of corporate governance whilst avoiding an inflexible 'one size fits all' approach. *Cadbury 1992* required that "[L]isted companies... should state in the report and accounts whether they comply with the Code and identify and give reasons for any areas of non-compliance."<sup>5</sup> Since the advent of the Cadbury Code, many countries around the world (including many of the frontier markets in this study) have adopted the "comply or

<sup>5</sup> David Seidl and Paul Sanderson (2009) "Applying 'comply-or-explain': Conformance with codes of corporate governance in the UK and Germany". Centre for Business Research, University of Cambridge Working Paper No.289

explain” principle and implemented it as per the original core elements. There are two core elements of the “comply or explain” principle:

- (a) The code applying the “comply or explain” principle is ‘soft law’, which means it is non-binding and voluntarily implemented. Listed companies are entitled to decide on their own adoption and degree of compliance with the code. Deviation from the code does not breach it; and
- (b) No matter how listed companies implement the code, disclosure concerning the compliance or non-compliance is *obligatory*, with an additional explanation in the case of non-compliance.

28. These two core elements can be summed up in the simple equation: *voluntary implementation of the code + mandatory disclosure*. Companies can choose what elements of the code they comply with, but they must explain what they do. This is the essence of the “comply or explain” principles based approach to corporate governance disclosure.

*‘comply or explain’ + unclear regulations*

29. A challenge arises from the combination of the “comply or explain” principle with unclear regulations. Such situations can create the appearance of contradictions and generate confusion about whether a code requires mandatory implementation or not. In one country, for example, the rules state that “*The Code should be implemented by all public companies*” which suggests that implementing the code and all its provisions is a mandatory requirement. Yet the same rules go on to say that “*The Code is to be adopted and implemented according to the ‘comply or explain’ principle*”. This second statement generates confusion by creating an apparent contradiction with the first: the “comply or explain” principle is normally associated with voluntary codes and explicitly entails the option of not complying. This leaves the question: since the option of not complying exists, is implementation of the code mandatory?

*transparency section within a ‘comply or explain’ code*

30. Another challenge arises when regulators combine explicit transparency and disclosure rules within a “comply or explain” model. Counterintuitively, the addition of explicit disclosure guidance within a “comply or explain” code can create confusion. In a “comply or explain” based code, every provision of the code dealing with corporate governance *mechanisms* is also potentially a provision dealing with *disclosure*, since companies would typically (under best practice) be required to explain their compliance with each provision in the code (what can be called an ‘itemized statement of compliance’). If, however, a chapter on transparency and disclosure also addresses issues of mechanisms covered elsewhere in the code, this can lead to confusion: two parts of the rules covering similar subjects with different implications for disclosure.

31. In the end a number of questions remain: in a comply or explain based code, is it optional to comply with the transparency section of the code? This would seem to be the case, but it is not clear. Drafters of codes could usefully clarify this point by, for example, indicating in the transparency section a clear list of mandatory disclosure items, and explaining that the disclosure section itself is not optional.

### **C. Models of mandatory and voluntary disclosure regulation**

32. This section looks at the different models of disclosure regulations that have been identified in UNCTAD’s research on CG regulations. The issues discussed in this section are illustrated in Figure 3 below. Discussion is based on a distinction between a) *mechanisms* of corporate governance, i.e. what governance structures companies should have, what rules and procedures they should follow and b) *disclosure* of corporate governance practices, i.e. what companies should report about what they are doing.

**Model 1: Mandatory mechanisms + mandatory disclosure**

33. The first model represents conventional command and control rules with obligatory requirements. Regulations other than corporate governance codes typically adopt this approach in stipulating disclosure obligations. However some corporate governance codes also adopt this approach. In this model, a country's corporate governance code is not 'soft law' rather it is 'hard law': a mandatory regulation like any other government regulation.

34. Mandatory rules on mechanisms in this case are typically accompanied by mandatory disclosure requirements. Such regulations normally include text such as "The listed companies shall publish/report to the public/disclose... (corporate governance disclosure items)". For example, an article of one country's law states:

*(Publishing information on the change in major holdings)*

*(1) A public company shall be obliged to publish the information contained in the notice on the change in major holdings ...*

35. This is an example of an explicit conventional mandatory disclosure requirement. In this type of regulation, the disclosure is a legal obligation.

**Model 2: Voluntary mechanisms + mandatory disclosure ("mandatory comply or explain")**

36. The second model follows the core elements of the "comply or explain" principle explained above: voluntary rules on mechanisms combined with mandatory disclosure. In this situation, all companies, whether they fully comply with the code or not, are obliged to disclose information about their compliance.

**Model 3: Voluntary mechanisms + voluntary disclosure ("voluntary comply or explain")**

37. The third model highlighted here involves the voluntary rules on mechanisms combined with voluntary disclosure. Some markets use a "comply or explain" rule that is not applied to every company automatically, rather companies must voluntarily adopt this rule, thus a disclosure obligation is triggered only if and when a listed company decides to adopt the code or some part of the code. The selective nature of this opt-in process makes this type of regulatory regime a voluntary one. The combination of this type of voluntary opt-in process with the "comply or explain" leads to a situation of "voluntary comply or explain". Within this model not all companies are subject to the same disclosure obligations, and what disclosure obligations do exist for companies are a product of a voluntary choice by those companies. An example of this model can be found in the following excerpt from one country's corporate governance code::

*Article 1...*

*For companies whose securities are admitted to some of the markets of the Stock Exchange, the obligation of the Code implementation is generated in the case they voluntarily in written (sic) inform the Stock Exchange that they accept its application.*

*Article 2. The implementation of the Code implies the following obligations for the companies:*

- *[...]*
- *To report at least once a year on the corporate governance including information on implementation of the Code recommendations or provide explanations for noncompliance(the rule "comply or explain")*

38. In this example, Article 1 indicates that the obligation of implementation is generated only by voluntary adoption. Article 2 provides for disclosure using the "comply or explain" principle. Thus

Article 2 would only apply to companies that voluntarily adopt the code and decide to assume these disclosure requirements.

## D. Explicit and implicit disclosure

39. Another issue related to corporate governance disclosure rules is the existence of explicit and implicit disclosure obligations. Explicit disclosure rules are typically simple, clear and direct. While implicit disclosure rules often require the combination of one or more provisions within a code, or the combination of a code with a separate company law that applies mandatory disclosure rules to the code. This issue has been discussed briefly in UNCTAD's previous reports on corporate governance.<sup>6</sup> The section below seeks to add further explanation.

### 1) Explicit disclosure

40. During the review of regulations and listing requirements of stock exchanges, it was observed that in some instances, for some disclosure items, there was an obvious and explicit requirement to disclose or report a particular item. An example of an explicit disclosure rule is provided above (section D.1 *mandatory* implementation).

### 2) Implicit disclosure

41. In contrast, a disclosure requirement can be regarded as *implicit* when it needs to be considered together with other regulation or general principles to determine whether or not a particular issue is subject to mandatory disclosure. There are two main types of implicit disclosure found among the regulations of the 21 countries in this study:

- (a) **Implicit Disclosure I:** *the disclosure requirement could be determined from the consideration of two separate articles within the same regulation or from different regulations*. For example, one article states that the annual report shall be published, but without specifying the specific corporate governance subjects to be included in the report. Meanwhile, another provision lists the detailed items that shall be embodied in the annual report. Thus, the disclosure requirements regarding detailed subjects can be identified by considering these two articles together. Another common example of this kind of implicit disclosure is when a provision sets forth "*Information regarding ... [preceding or following provisions] shall be reported to the public*". In this case, the disclosure obligation becomes applicable to all the subjects covered in those provisions.
- (b) **Implicit Disclosure II:** *the disclosure requirement could be determined from the consideration of an article and a general principle*. Because of the disclosure obligation incurred from the "mandatory comply or explain" principle, the ordinary CG regulation in the code implies that listed companies shall disclose the actual CG practice in the same regard. For example, a provision from a code adopting the "mandatory comply or explain" principle states "*The company should set up an internal control system that guarantees effective reporting and disclosure of information*". Then the disclosure obligation of this provision is that listed companies must disclose whether they have set up internal control systems, how their systems are and whether the systems fulfill the requirement, etc.

42. Explicit disclosure and implicit disclosure type I are typically found in mandatory implemented corporate governance codes and other regulations, whilst implicit disclosure type II typically exists only in the circumstance of the mandatory comply or explain model.

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<sup>6</sup> See the studies noted in footnote 1.

*general disclosure statements versus specific itemized disclosure*

43. An issue identified in UNCTAD's previous studies on corporate governance disclosure is the use of 'general disclosure statements' or general statements of compliance with a code.<sup>7</sup> The problem with such statements is that they do not contain any detailed, useable information about exact company specific practices. As such they are not considered a form of implicit disclosure.

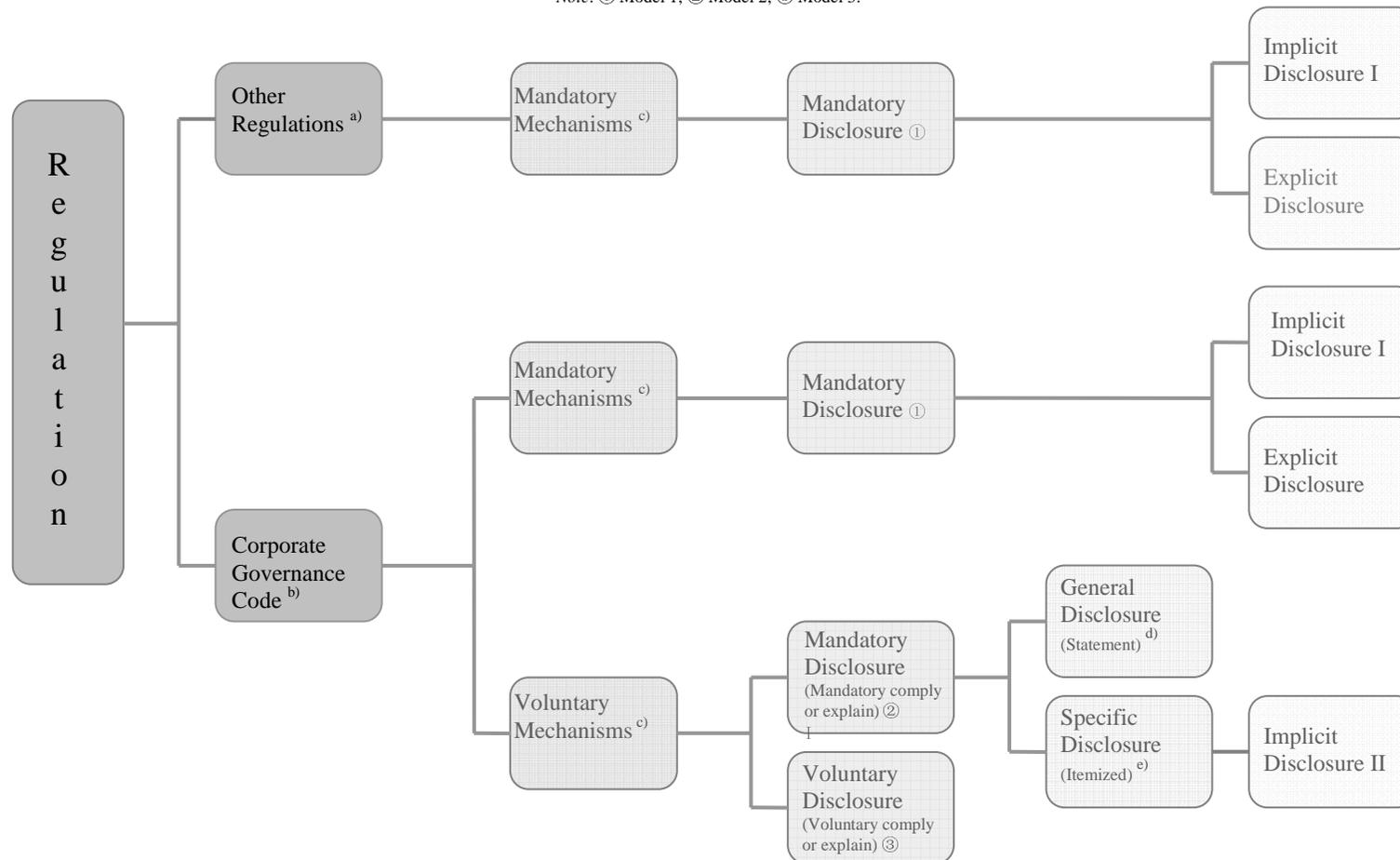
44. In contrast to general disclosure statements, some codes require specific itemized disclosure of individual corporate governance subjects (this can be thought of as 'itemized comply or explain'). This type of disclosure rules can be considered a form of implicit disclosure II.

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<sup>7</sup> See in particular paragraph 58 of "2009 Review of the implementation status of corporate governance disclosures: case study Pakistan" (TD/B/C.II/ISAR/CRP.5).

**Figure 3. Models of voluntary and mandatory disclosure regulation**

Note: ① Model 1; ② Model 2; ③ Model 3.



a) Relevant regulations other than CG codes, for example: company law, listing rules, etc.

b) Includes explicit CG codes, resolutions or legal-decisions specific to CG mechanisms and disclosure.

c) Refers to the enforcement (binding or non-binding) of the CG mechanisms regulations.

d) Company discloses compliance with CG code by a general statement, e.g. "I have complied with the code" or "I have not complied with the code" along with relevant reasons.

e) Company discloses compliance with CG code by providing details of CG mechanisms item by item corresponding with each provision of the code.

## E. Disclosure chain: does the information get to the public?

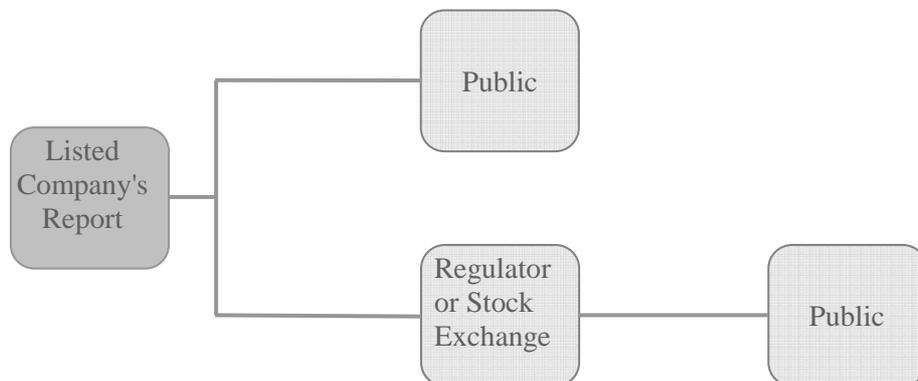
45. In addition to the issues outlined above, one additional aspect should come to the attention of regulators working in this area is the question of whether or not corporate governance disclosure information reaches the public. UNCTAD's studies<sup>8</sup> focus on disclosure that is public and available to all current and potential future shareholders, as well as other stakeholders. Some forms of regulation complicate or obstruct the transmission of information to the public. This section highlights four issues to consider in promoting improved access to information.

### 1) Path: direct vs. indirect

46. Among the regulations reviewed in this study, the path of disclosing CG information to the public is either direct or indirect. The direct path is that the information reported by listed companies is communicated directly to the public (e.g. via a company website or other documents widely accessible to the public). Regulations typically contain text such as "The listed companies shall publish ... (CG information) on their website". This type of rule is common among the countries in this study.

47. The indirect path is less common but has the same effect of reaching the public. Some countries' regulations stipulate the listed company shall report the CG information to the regulator or stock exchange and subsequently the regulator or stock exchange is obliged to disclose to the public (e.g. via the website of the regulator or stock exchange). These two distinctive paths are shown in Figure 4 below.

**Figure 4. Path of disclosure to the public**



48. A problem can arise, however, in the regulations of some countries wherein companies are only required to report CG information to the regulator or stock exchange, and the regulator or stock exchange does not subsequently pass on this information to the public. This situation, while keeping regulators duly informed, does not allow for informing current and potential investors and other stakeholders. Regulators can remedy this situation by making all company reports available on a website.

<sup>8</sup> See for example the studies list under footnote 1 above.

## **2) Recipient**

49. As noted above, this study is based on the disclosure to the general public and all current and potential future investors. However, it is not common for regulations among the countries in this study to clearly state the goal of “publish” or “disclose to the public”. Many regulations state instead that companies should “report to shareholders”. Of the 21 countries in this study, for example, 17 have regulations providing disclosure of some items only to shareholders. For the purpose of this study, regulations that require disclosure to “shareholders” generally were interpreted as being current as well as potential future shareholders, in essence the general public. However some rules were even more specific using text such as “current shareholders” which would preclude all potential future shareholders and other stakeholders. Regulators therefore might consider clarifying their rules by using language such as “disclosure to public” rather than “disclosure to shareholder”.

## **3) Accessibility of information: passive versus active disclosure**

50. Disclosure requirements can specify the way in which companies disclose information, with implications for the accessibility of that information to the general public and international investors. Regulations can require a more active approach to disclosure meaning that the company takes steps to make the information easily accessible by the public, e.g. via a company website.

51. Regulations can also permit a more passive approach, allowing the company to make CG information available via less accessible means. For example, the company may be permitted (or required) to keep CG information in its office, at the office of the regulator or another registered office; the information is then made available upon request to visitors of the office where it is stored. In some cases, people seeking access to this information are required to pay a fee. This situation limits the accessibility of information to stakeholders in general and can significantly limit the accessibility of such information to international investors. Regulators can improve the accessibility of information by requiring it to be published on company websites, or on the regulator’s website.

## **4) Intermediary**

52. Regulations can contain a variety of intermediaries for corporate governance disclosure, including: mass media; local newspapers in wide circulation; a regulator’s official bulletin; public gazette; websites; etc. Each of these intermediaries has implications for accessibility. While specific issues may require specific mediums of communication, in general, regulators could consider the prioritization of the use of websites as the most cost effective means of making information accessible to a wide range of stakeholders, including international investors.

## IV. Conclusions

53. This report is a regular annual review of corporate governance disclosure prepared by the UNCTAD secretariat. This study follows the same approach of earlier studies in 2007 and 2009 but while those earlier studies examined a range of emerging markets, this study has looked at group of countries with smaller, typically less developed securities markets, commonly referred to by investors as ‘frontier markets’; specifically at a sample of 21 economies drawn from the MSCI Frontier Markets Index.

54. The main findings of this study show that most of the economies in the MSCI FM index do not have mandatory disclosure rules for most of the items in the ISAR benchmark of good practices. This is in contrast to earlier UNCTAD studies of larger emerging markets that require disclosure of a majority of the items of the ISAR benchmark. These findings suggest that the frontier markets have a less developed regulatory environment related to corporate governance disclosure and require significantly less information from listed companies than would be required in larger emerging markets or developed countries. This suggests that officials interested in promoting investment in these frontier markets might usefully consider a re-examination of the disclosure requirements of listed companies, with a view to strengthening such requirements where appropriate in order to meet the information expectations of international investors.

## **Annex I**

### **List of sources by market**

#### **Bahrain**

- Central Bank of Bahrain and Financial Institutions Law 2006
- Bahrain Stock Exchange Law
- Bahrain Stock Exchange Internal Regulation
- Commercial Companies Law 2001
- BMA Disclosures Standards Book

#### **Bulgaria**

- Law on Public Offering of Securities
- Commerce Act
- Measures Against Market Abuse with Financial Instruments Act
- Ordinance No. 2 of September 17, 2003
- Bulgarian National Code for Corporate Governance
- Listing Rules (Bulgarian Stock Exchange-SOFIA)

#### **Croatia**

- The Securities Market Law
- Code of Corporate Governance+ Annual Questionnaire
- Rules (The Zagreb Stock Exchange)
- The Capital Market Act
- Directive 2001/34/EC of the European Parliament and of the Council
- Regulation (EC) No 1606/2002 of the European Parliament And of the Council
- The Act on the Takeover of Joint Stock Companies
- Ordinance on the Contents and Form of Financial and Business Reports of Public Joint Stock Companies

#### **Estonia**

- Securities Market Act
- Commercial Code
- Requirements for Issuers
- Corporate Governance Recommendations

#### **Kazakhstan**

- Law Concerning Joint-stock Companies
- Law Concerning the Securities Market
- Listing Rules of Kazakhstan Stock Exchange
- Rules on Exchange Information Dissemination

#### **Kenya**

- The Capital markets (Securities) (Public Offers, Listing and Disclosures) Regulations,2002
- Guidelines on Corporate Governance Practices by Public Listed Companies in Kenya
- NSE Listing Manual
- Companies Act
- Capital Markets Act

#### **Kuwait**

- Capital Markets Bill 2010
- Law of Commercial Companies
- KSE Committee Decision No.(2) for the Year 2008 Concerning the Rules and Conditions for Listing Shareholding Companies in the Official Market
- Ministerial Resolution No. 35 of 1983 Promulgating the Kuwait Stock Exchange by-law

**Lebanon**

- The BSE Law
- Bylaws of the Beirut Stock Exchange
- The Regulation of Holding Companies
- The Offshore Companies Statute
- Code of Commerce (legislative decree No.304)

**Lithuania**

- Law on Companies
- Law on Securities
- Law on Markets in Financial Instruments
- The Listing Rules of AB NASDAQ OMX Vilnius
- The Corporate Governance Code for the Companies Listed on NASDAQ OMX Vilnius
- Concerning Disclosure of Compliance with the Corporate Governance Code

**Mauritius**

- Code of Corporate Governance (inside the Report on Corporate Governance for Mauritius)
- The Securities Act 2005
- The Companies Act 2001
- Securities (Disclosure Obligations of Reporting Issuers) Rule 2007
- The Listing Rules (official market)

**Nigeria**

- Code of Corporate Governance 2008
- The Investments and Securities Act 2007
- Securities and Exchange Commission Rules and Regulations
- Companies and Allied Matters Act 1990

**Oman**

- The Capital Market Law
- Executive Regulation of The Capital Market Law 2009
- Listing Rules at Muscat Securities Market
- Code of Corporate Governance for MSM Listed Companies
- Requirements and Terms for Issuing Shares in the Sultanate of Oman 2005
- The Commercial Companies Law

**Qatar**

- Law No.33 of 2005
- Doha Securities Market Bylaws
- Law No.5 of 2002 the Commercial Companies Law

**Romania**

- The Capital Market Law No.297/2004
- CNVM Regulation No.1/2006 on Issuers and Operations with Securities
- Regulation No.31/2006 Amending CNVM Regulations by Implementing Certain Provisions of European Directives
- Rulebook of the Bucharest Stock Exchange
- Company Law
- Bucharest Stock Exchange Corporate Governance Code

**Serbia**

- Law on Business Companies
- Law on the Market of Securities and Other Financial Instruments
- Rulebook on the Contents and Manner of Public Companies' Reporting and Notification on Possession of Voting Shares

- Rules on Listing and Quotation

**Slovenia**

- Companies Act
- Market in Financial Instruments Act (ZTFI)
- Corporate Governance Code 2009
- Ljubljana Stock Exchange Rules
- Guidelines on Disclosure for Listed Companies
- Takeover Act

**Sri Lanka**

- Colombo Stock Exchange Listing Rules 2010
- Companies Act No. 07 of 2007
- Securities and Exchange Commission of Sri Lanka Act

**Trinidad and Tobago**

- The Companies Act 1995
- Securities Bill 2010
- Disclosure, Registration and Corporate Finance The Annual Report (TTSEC)
- Trinidad and Tobago Stock Exchange Rules

**Ukraine**

- Law of Ukraine on Securities and the Stock Market
- Law on Joint Stock Companies, 2008
- Ukrainian Corporate Governance Principles

**United Arab Emirates**

- Resolution No.(518) 2009 Concerning Governance Rules and Corporate Discipline Standards
- Decision No.(3/R) of 2000 Concerning the Regulations as to Disclosure and Transparency
- Decision No.(12)of 2000 Concerning the Regulations as to the Listing of Securities and Commodities
- Federal Law No.(4) of 2000 Concerning the Emirates Securities Commodities Authority and Market
- Federal Law No.8 of 1984 Concerning Commercial Companies
- Listing Requirements of Dubai Financial Market (foreign company, local company, bonds)

**Viet Nam**

- Vietnam Listing Rules
- Circular on Disclosure of Information on the Securities Market 2007
- The Government's decree on Securities and Securities Market
- Law on Enterprises
- Circular Providing Guidance on Information Disclosure on the Securities 2004
- Decision Promulgating Regulations on Corporate Governance 2007

## Annex II

### List of disclosure items in the ISAR benchmark<sup>9</sup>

<b>Disclosure</b>	
<b>Financial Transparency and Information Disclosure</b>	
1	Financial and operating results
2	Critical accounting estimates
3	Impact of alternative accounting decisions
4	Company objectives
5	Nature, type and elements of related-party transactions
6	Decision making process for approving related-party transactions
7	Rules and procedures governing extraordinary transactions
8	Board's responsibilities regarding financial communications
<b>Ownership Structure and Exercise of Control Rights</b>	
9	Ownership structure
10	Changes in shareholdings
11	Control structure
12	Control rights
13	Control and corresponding equity stake
14	Rules and procedures governing the acquisition of corporate control in capital markets
15	Anti-Takeover measures
16	Process for holding annual general meetings
17	Availability and accessibility of meeting agenda
<b>Board and Management Structure and Process</b>	
18	Checks and balances mechanisms
19	Governance structures, such as committees and other mechanisms to prevent conflicts of interest
20	Composition and function of governance structures
21	Composition of the board of directors

<sup>9</sup> ISAR benchmark as of 2010 revision. See section I.A. above for details.

22	Role and functions of the board of directors
23	Qualifications and biographical information on board members
24	Types and number of outside board and management positions
25	Duration of directors' contracts
26	Risk management objectives, system and activities
27	Existence of succession plan for senior executives and board members
28	Independence of the board of directors
29	Material interests of senior executives and board members
30	Existence of procedures for addressing conflicts of interest among board members
31	Professional development and training activities for board members
32	Availability of advisorship facility for board members or board committees
33	Determination and composition of directors' remuneration
34	Performance evaluation process for board members
35	Compensation policy for senior executives departing the firm as a result of a merger or acquisition
<b>Auditing</b>	
36	Internal control systems
37	Process for interaction with internal auditors
38	Scope of work and responsibilities for internal auditors
39	Process for interaction with external auditors
40	Process for appointment of external auditors
41	Duration of current external auditors
42	Rotation of external auditors
43	External auditors' involvement in non-audit work and fees paid to auditors
44	Board confidence in the independence and integrity of external auditors
<b>Corporate Responsibility and Compliance</b>	
45	Policy and performance in connection with environmental and social responsibility
46	Impact of environmental and social responsibility policies on sustainable development
47	A Code of Ethics for the board and waivers to the ethics code
48	A Code of Ethics for company employees
49	Policy on "whistle blower" protection

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50	Mechanisms protecting the rights of other stakeholders
51	Existence of employee elected director(s) on the board