

Legal aspects of corporate governance in Croatia: Issue of state owned companies

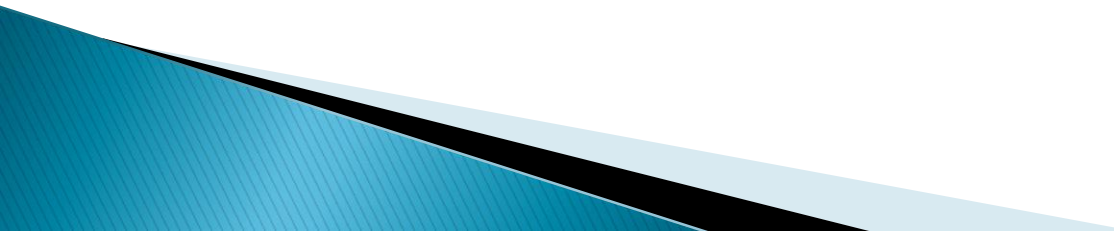
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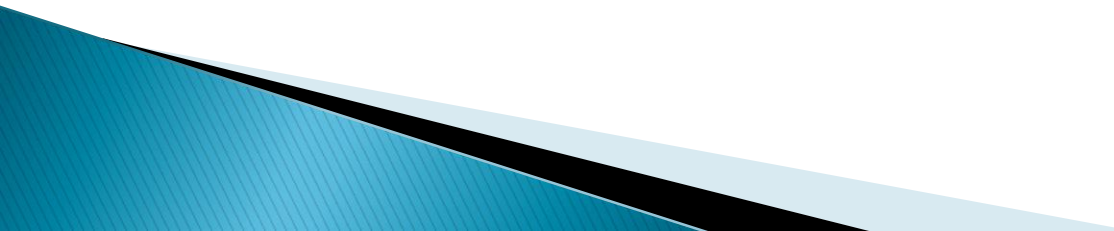
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1st International conference "Corporate governance – new experiences: Implementation in South Eastern Europe"

- ▶ “It is a paramount importance that European business demonstrate the outmost responsibility not only towards their employees and shareholders but also towards society at large” (Communication from the Commission to the EP *Towards a Single Market Act – for a highly competitive social market economy*, COM (2010) 608 final/2)

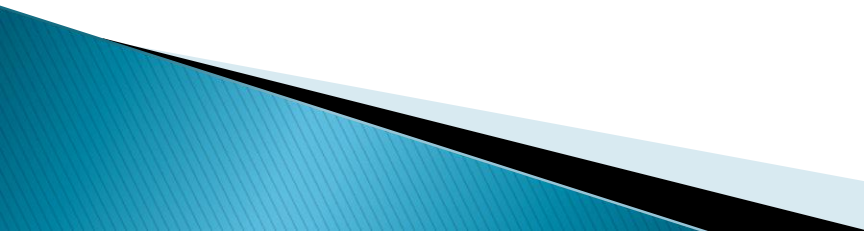
IN CROATIA:

- ▶ CG need support of public policy
 - ▶ Corporate strategy formation is made within a framework provided by a set of rules
 - ▶ These rules may include private self-regulation, but consist mainly of public laws and regulations such as company law, securities regulation, listing requirements and insolvency legislation
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- ▶ Good CG practices cannot develop without appropriate public policy, without an adequate legal and regulatory framework
 - ▶ This is mainly why governments all around the world pay due attention to CG
 - ▶ Does the government in Croatia?
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CG in the context of transition

- ▶ In transitional economies the development for good CG practice is more about creating the key institution that will drive successful economy transformation to market based economy

- Such a cultural shift takes time and slowly becomes evident in most transition economies (OECD)
 - the most significant improvements in SEE could come from effective enforcement of existing laws and regulations
 - Major obstacles: lack of sanctioning powers and independence of regulators, limited co-operation and trust between authorities and private sector, etc.
 - Beside the existing legal and regulatory framework it should be upgraded in terms of coherence and force ability
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- ▶ Company law – core of the corporate framework /in many cases the law doesn't provide sufficiently clear and efficient set of rules, not well implemented – lack of proper enforcement mechanism

Achievements in Croatia


- numerous changes in Croatian company law and corporate governance have been done in past decade mainly as a result of compliance with *acquis communautaire* of the EU
- In that process the importance of CG and the idea of implementation of good corporate governance standards have become more and more important
- The provisions of the Companies Act in Croatia provide comprehensive legal regulation of the scope of the activities of the joint stock companies' body
- Above mentioned harmonisation process with EU legislative and regulatory practice has revealed a need to adopt a CG Code, to regulate where the act stops

Regulatory and legal framework

- Companies Act (Official Gazette N.N. 137/09)
- Court Register Act (N.N. 91/10)
- Accounting Act (N.N. 109/07)
- Auditing Act (N.N. 139/08)
- Implementing regulations
- Capital Market Act(N.N. 74/09)
 - ▶ for capital market participants in Croatia, for issuers whose securities are admitted to a regulated market (Zagreb stock exchange 2009)
- ZSE rules (2011)
- HANFA s ordinances and instructions

- Companies Act contains in Art. 272p “comply or explain” principle /as introduced in the Directive 2006/46/EC/ –
requirement for listed companies to include CG statement in their annual report containing description of the main features of the companies internal control and risk management systems in relation to the financial reporting process.
- It mandates the application of CG codes either by way of “comply or explain” or alternatively it allows the application of companies specifics extra legal principles

- The provisions of the Companies Act in the Republic of Croatia provides comprehensive legal regulation of the scope of activities of the joint stock company's bodies
- Nonetheless, harmonisation process with the EU legislative and regulatory practice has revealed a need to adopt a Corporate Governance Code, to regulate where the act stops
- The Corporate Governance Code was first created in 2007 by the Croatian Financial Services Supervisory Agency /HANFA/ and Zagreb Stock Exchange (amended in 2010)

- Some authors believe that the German code should be used as a model, given the fact that the Croatian Companies Act is closest to the German Akt-G.
 - Although this idea is in principle correct, Croatian particularities, especially those of the Croatian financial market as well as the maturity of corporate governance tradition in the Republic of Croatia should not be overlooked.
 - numerous companies in the Republic of Croatia have their own corporate governance codes that can also be included in the annual report within the meaning of Article 272p
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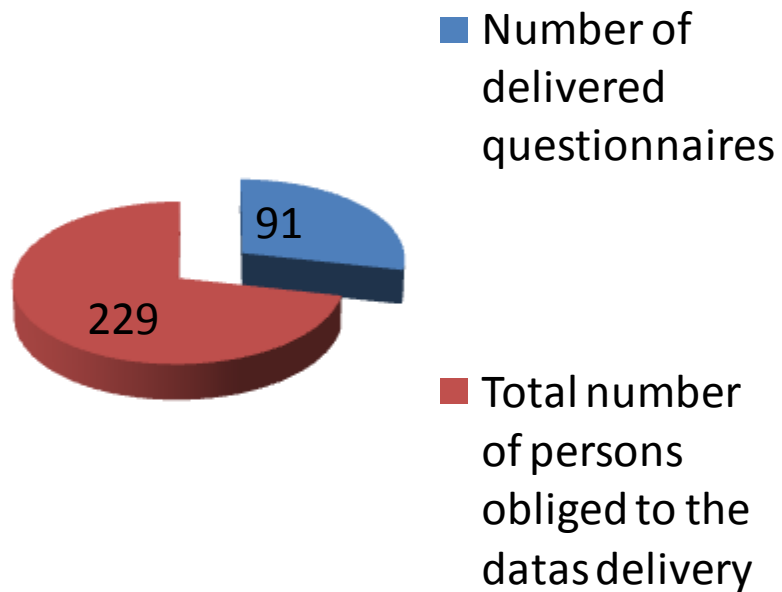
- ▶ Croatian financial services supervisory agency (HANFA) in 2011 have started with issuing Annual report on CG in Croatia for 2010 in comparison with the data from 2009
[/www.hanfa.hr/](http://www.hanfa.hr/)
- ▶ this comprehensive report is of utmost importance and shows the achievements and development of CG culture in Croatia.

Application of CG Code in Croatia*

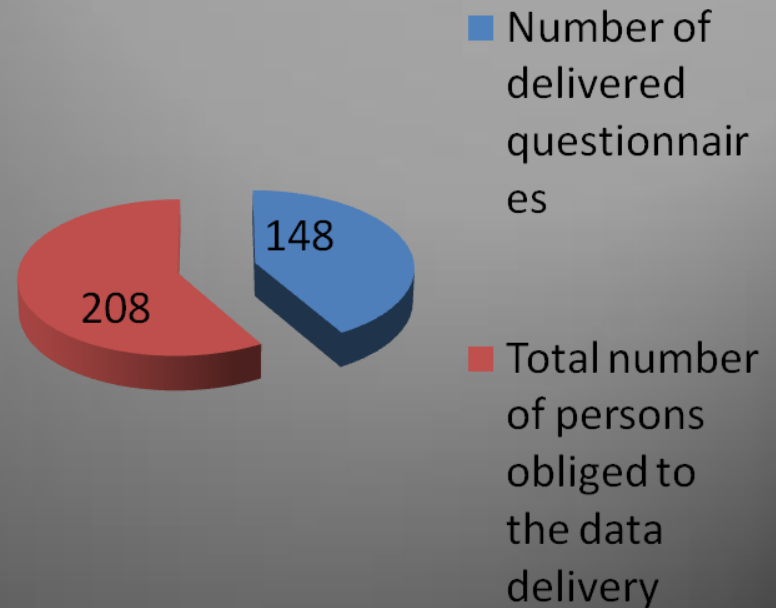
- According to the data of Zagreb Stock exchange in 2009 91 issuers delivered fulfilled questionnaire on Code of CG – 39, 74% of the total number of the persons obliged for the data delivery
- In 2010 the same questionnaire was delivered from 148 issuers (31.7.2011) – 71,15% of the total number of the persons obliged for the data delivery
- the number has increased for 31,41%

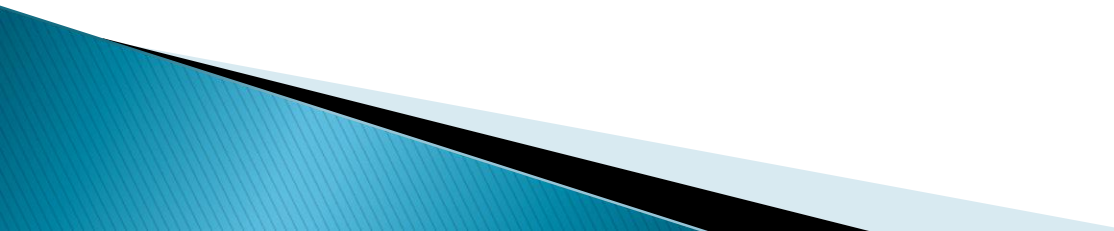
*data from HANFA Report, p. 60 (see next slide)

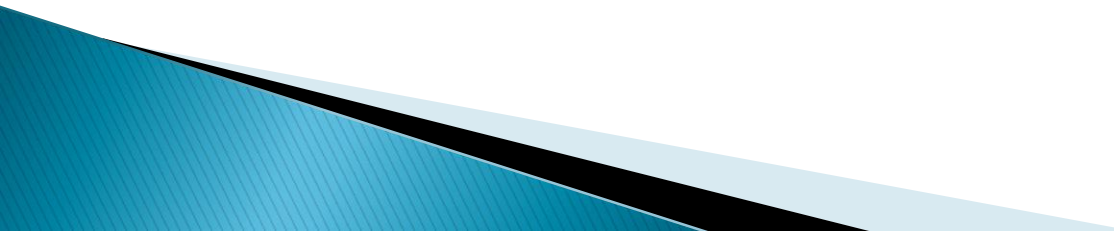
Number of delivered questionnaires in 2009




Number of the delivered questionnaires in 2010

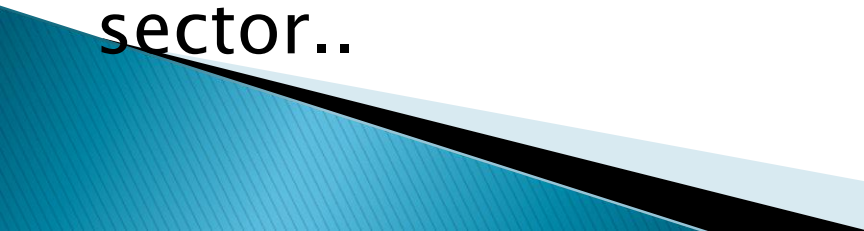


- According to the questionnaire 28 issuers additionally applies some other CG code and 9 of them use their companies specific code
 - 95 issuers publish data on their web site, 90 don't publish, and others didn't answered the question
 - only 125 issuers who are applying the CG codes answered that 66% of them fully comply with the CG code *
 - Source HANFA , p.61
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- ▶ According to the shown data it seems that the level of CG culture is currently raising
 - ▶ It is obvious that this achievement is outcome of high level of Croatian legislative and regulatory framework alignment with the EU legal framework
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- However recent business practice shows that CG experiences have not been really implemented
 - this gap between legal and business practice has only recently resulted in numerous corporate abuses, presently awaiting resolution in court proceedings.
 - only time will tell whether the court epilogue could influence the development of the CG culture or raise the awareness of CG and management to the benefit of the company itself and thus its shareholders as well.
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Special question – state owned companies!


- ▶ 69 companies of special state interest , in 21 100% owner
 - ▶ Revenue cca 10 billion. eur, expenditure cca . 10bill. net. loss 500.000.000 mil. eur. after taxation
 - ▶ Energy, agriculture, tourism, shipbuilding, financial sector..
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Regulatory framework

- ▶ Definition of companies of special state interest (2006, 2009 and 2010) –
Decision on the list of legal entities of special state interest (N.N. 144/2010)
- ▶ Law on the management of state assets (N.N. 145/10)
- ▶ Founding the Agency for the Management of State Assets (2010)
- ▶ Ordinance on the sale of shares and equity in companies owned by the Republic of Croatia, institutes and other legal entities owned by the Republic of Croatia (N.N. 64/11)
- ▶ Ordinance on the terms for tendering the members of supervisory and management boards of companies in which Republic of Croatia has shares (N.N. 95/10)
- ▶ Corporate Governance code for state owned companies (N.N. 112/10)

- ▶ What remains is obligation to draw up proposals for:
 - Strategy for the Privatisation of Companies Owned by the State
 - Plan of privatisation of Companies owned by the state

Deadlines, publically available information, value of assets–liabilities of SO, strategic plans of companies, structural problems...

- ▶ Greater public attention must be devoted to the management of government financial and non financial assets because of poor financial effect on the budget and poor cg
 - ▶ By joining the EU Croatia – part of larger market and management of SO assets crucial for the stabilisation and long term financial sustainability of public sector
 - ▶ Greater transparency , independence and accountability should be achieved through the implementation of the CG instruments
 - ▶ All stakeholders should be involved in this process
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- ▶ CG should have important spill over effect on society as a whole
 - ▶ Unaccountable and opaque corporations are more than likely to undermine the rule of law and the effectiveness of government, creating and sustaining a vicious circle of corruption, bribery and mismanagement not only in the private sector but also in the public sector
 - ▶ The development of good CG can be seen as key public institution–building ingredient for a transparent and accountable society
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