CORPORATE GOVERNANCE DEVELOPMENTS IN SPAIN

Silvia Gómez-Ansón
University of Oviedo
Recent “legal” developments in Spain

Codes of Best Practice:

* Olivencia Report (1998):
  • 23 recommendations:
    – Structure of the Board:
      » majority of non-executive directors
      » setting up of specialized committees made up exclusively of non-executive directors (i.e. auditing, remuneration or appointment committees
      » need to disclose directors’ pay details
      » Board size
      » retirement age for directors
    – Corporate Governance Report: voluntary (comply or explain)
  • Limited success:
    – Questionnaire by the Spanish Supervisory Agency in 2000: mean compliance with the Code recommendations 81% among the 61 firms that answered the questionnaire. Only two firms complied with all recommendations.
    – Questionnaire in 2001: mean compliance was 77% for the 67 firms that answered the questionnaire, with only five firms implementing all 23 recommendations.
    – Low degree of compliance with the “comply or explain” rule, a large part of the companies did not publish a Corporate Governance Report.
Recent legal developments in Spain

- Codes of Best Practice
    - Similar recommendations to Olivencia Report
    - Differential characteristics: transparency of information:
      - Corporate Governance Report
      - Web page
Recent legal developments in Spain

- Legislation:
  * Law of Reform of the Financial System, Law 44/2002:
    • Compulsory Audit Committee with a majority of non-executive directors
  * Transparency Law (Law 26/2003)
    • Reform of Company Law
    • Established the obligation to:
      – Publishing and filling an Internal Code of Conduct, Rule of the Board of Directors, Rule of the General Shareholders’ Meeting
      – Publish an annual Corporate Governance Report
      – Disclose information on the web page
  * Developments of the Transparency Law:
    • Orden ECO/3722/2003
    • Directive of the Spanish Supervisory Agency (March, 2004):
      – Disclosure of information
- The Foundation of Financial Studies (Spanish Institute of Financial Analysts) in cooperation with researchers of the University of Oviedo promoted in 2003 the creation of an *Annual Observatory of Good Practices for Spanish quoted companies*.

- The study will be presented every year to the Chairmen, CEOs and Secretaries of the Boards of the companies quoted on the Spanish Stock Exchange:
  
  * **Promote discussion** of the state of Corporate Governance in Spain by incumbent managers
  
  * **Award** (in cooperation with the press group Recoletos) to the Company presenting the Best Corporate Governance Practices.
    
    • Ranking to the Jury based on the Observatory
Structure of the Observatory in 2003

- **201 variables:**
  * Ownership structure
  * Board of Directors’ characteristics and structure
  * Shareholders’ rights
  * Transparency of Information

- **Definition of the variables:**
  * Recommendations of Codes of Best Practices
    * Olivencia Code (1998)
    * Legislation

- **Sample:**
  * 35 firms in the Ibex-35 Index, firms with the largest market capitalisation
Methodology: Categories

Observatory of Corporate Governance
201

Ownership structure
28

Board of Directors
72

Shareholders’ rights
32

Transparency of Information
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Board’s Structure
57

Remuneration
15

Shareholders rights
10

Rule of the General Shareholders Meeting
10

Anti-takeover devices
12

Accounting Transparency
13

Corporate Governance Transparency
33

Transparency On the Web
page 23
Results: ownership structure – ownership concentration

- All Largest Shareholders Ownership: 43.41%
- Five Largest Shareholders Ownership: 42.40%
- Three Largest Shareholders Ownership: 39.02%
- Largest Shareholder ownership: 26.29%
Results: ownership structure – large shareholders-

- Free float; 56.49%
- Non-financial companies; 17.39%
- Individuals and Families; 10.83%
- State; 1.47%
- Others; 0.43%
- Mutual and pension funds; 4.95%
- Banks and financial companies; 8.45%
Results: Board of Directors’ structure

- Relevant aspects:
  * Mean Size: 15
  * Number of annual meetings: 10
  * Composition of the Board: reflects the high ownership concentration of Spanish firms
  * Separation of the posts of CEO and Chairman: No, 77%
  * Secretary a director? 31%
  * Limitations in the number of mandates of independent directors: Yes 9%
Results: Board of Directors – composition:

- Independent directors; 36.76%
- Executive Directors; 17.89%
- Directors representing large shareholders (not linked to executives); 39.64%
- Directors representing large shareholders (linked); 1.98%
- Independent directors (grey); 3.73%
Results: Board of Directors’ structure

- Relevant aspects:
  * Board Committees: 3
  * Executive Committee: 65.71%
  * Audit committee: All (by law)
    • Chairman independent director: 71%
    • Chairman external director: 100%
  * Remuneration and Nominees Committee: Almost all companies
    • Chairman external director: 100%
Results: Board of Directors’, remuneration

- Relevant aspects:
  * Almost all companies remunerate their external directors
  * 68.58% use fixed payments
  * Small percentage use option plans or variable remuneration schemes
  * Mean remuneration to external directors: 56.537 euros
Results: Shareholders’ rights – Grades –

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<th>Shareholders' rights</th>
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### Results: Transparency of Information – Grades –

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Conclusions of the Observatory, 2003

- Positive aspects of Spanish Corporate Governance Practices:
  * Low percentage of shares held by the State
  * Size of the Boards of Directors
  * Number of annual meetings of the Boards
  * Composition of the Board
  * Existence of audit and nominees and remuneration committees
  * Office of the Shareholder
  * Low degree of usage of anti-takeover devices
  * High degree of Accountings’ transparency of information
  * High degree of transparency of information on the web page
Conclusions

- Aspects of Spanish Corporate Governance Practices that should be revised:
  * Existence of pyramidal structures
  * Low ownership held by directors
  * Existence of grey directors
  * No separation of CEO and Chairman
  * The Secretary of the Board is not a Director
  * 30% of the firms lack an executive committee
  * Directors remuneration is usually not linked to the firm value
  * Low degree of Corporate Governance’s Transparency of Information