



THE WORLD BANK

ROSC

Report on the Observance of Standards and Codes (ROSC)

CORPORATE GOVERNANCE
COUNTRY ASSESSMENT

El Salvador

June 2012

About the ROSC

What is corporate governance?

Corporate governance refers to the structures and processes for the direction and control of companies. Corporate governance concerns the relationships among the management, board of directors, controlling shareholders, minority shareholders and other stakeholders. Good corporate governance contributes to sustainable economic development by enhancing the performance of companies and increasing their access to cost-effective capital.

The OECD Principles of Corporate Governance provide the framework for the work of the World Bank Group in this area, identifying the key practical issues: the rights and equitable treatment of shareholders and other financial stakeholders, the role of non-financial stakeholders, disclosure and transparency, and the responsibilities of the board.

Why is corporate governance important?

For emerging market countries, improving corporate governance can serve a number of important public policy objectives. Good corporate governance reduces emerging market vulnerability to financial crises, reinforces property rights, reduces transaction costs and the cost of capital, and contributes to capital market development. Weak corporate governance frameworks reduce investor confidence, and can discourage outside investment. Also, as pension funds continue to invest more in equity markets, good corporate governance is crucial for preserving retirement savings. Over the past several years, the benefits and importance of corporate governance have been highlighted by an increasing body of academic research. Studies have shown that good corporate governance practices have led to significant increases in economic value added (EVA) of firms, higher productivity, and lower risk of systemic financial failures for countries.

The Corporate Governance ROSC

Corporate governance has been adopted as one of twelve core best-practice standards by the international financial community. The World Bank is the assessor for the application of the OECD Principles of Corporate Governance. Its assessments are part of the World Bank and International Monetary Fund (IMF) program on Reports on the Observance of Standards and Codes (ROSC).

The goal of the ROSC initiative is to identify weaknesses that may contribute to a country's economic and financial vulnerability. Each Corporate Governance ROSC assessment benchmarks a country's legal and regulatory framework, practices and compliance of listed firms, and enforcement capacity vis-à-vis the OECD Principles.

- The assessments are standardized and systematic, and include policy recommendations and a model country action plan. In response, many countries have initiated legal, regulatory, and institutional corporate governance reforms.
- The assessments focus on the corporate governance of companies listed on stock exchanges. At the request of policymakers, the World Bank can also carry-out special policy reviews that focus on specific sectors, in particular for banks and state-owned enterprises.
- Assessments can be updated to measure progress over time.
- Country participation in the assessment process, and the publication of the final report, are voluntary.

By the end of June 2012, 83 assessments had been completed in 58 countries around the world.

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Acknowledgements

This assessment of corporate governance in El Salvador was conducted in May 2010 by Pasquale Di Benedetto and Alexander Berg of the World Bank Global Capital Markets and Corporate Governance Practice, as part of the Reports on Observance of Standards and Codes Program.

The report reflects technical discussions with a number of private and public sector institutions, as well as other relevant stakeholders, whom the World Bank would like to thank for their time and insight into corporate governance practices in El Salvador. The World Bank would like to expressly thank Superintendencia Financiera SSF, the Superintendencia de Sociedades, the Bolsa de Valores de El Salvador, Cedeval, and representatives of companies, banks, and market participants in addition to a number of companies, banks, and financial institutions, as well as law and audit firms.

Much of the legal and regulatory analysis of this Corporate Governance ROSC is based on an in-depth review of the legal and regulatory framework conducted by the legal firm Consortium.

Acronyms

BVES: Bolsa de Valores de El Salvador (El Salvador Stock Exchange)
CEO: Chief Executive Officer
CFO: Chief Financial Officer
Commercial Code: Code of Commerce, 1970
CVCA: Consejo de Vigilancia de la Profesión de Contaduría Pública y de Auditoría (Accounting and Auditing Monitoring Board)
DCA: Detailed Country Assessment
EGM: Extraordinary General Meeting
GDP: Gross Domestic Product
AGM: Annual General Meeting of Shareholders
IFRS: International Financial Reporting Standards
IOSCO: International Organization of Securities Commissions
ISA: International Standards on Auditing
Ley de Mercado: Securities Law, Decreto 809, 1994
ROSC: (Corporate Governance) Report on Standards and Codes
RPT: Related Party Transaction.
SSF: Superintendencia Financiera de El Salvador
SSFL: Financial System Supervision and Regulation Law
SOM: Superintendencia de Obligaciones Mercantiles (Superintendency of Companies)
SRO: Self regulatory organization

Definitions

Cumulative voting: Cumulative voting allows minority shareholders to cast all their votes for one candidate. Suppose that a publicly traded company has two shareholders, one holding 80 percent of the votes and another with 20 percent. Five directors need to be elected. Without a cumulative voting rule, each shareholder must vote separately for each director. The majority shareholder will get all five seats, as s/he will always outvote the minority shareholder by 80:20. Cumulative voting would allow the minority shareholder to cast all his/her votes (five times 20 percent) for one board member, thereby allowing his/her chosen candidate to win that seat.
Pre-emptive rights: Pre-emptive rights give existing shareholders a chance to purchase shares of a new issue before it is offered to others. These rights protect shareholders from dilution of value and control when new shares are issued.
Proportional representation: Proportional representation gives shareholders with a certain fixed percentage of shares the right to appoint a board member.
Pyramid Structures: Pyramid structures are structures of holdings and sub holdings by which ownership and control are built up in layers. They enable certain shareholders to maintain control through multiple layers of ownership, while at the same time they share the investment and the risk with other shareholders at each intermediate ownership tier.
Shareholder agreement: An agreement between shareholders on the administration of the company. Shareholder agreements typically cover rights of first refusal and other restrictions on share transfers, approval of related-party transactions, and director nominations.
Squeeze-out right: The squeeze-out right (sometimes called a “freeze-out”) is the right of a majority shareholder in a company to compel the minority shareholders to sell their shares to him. The sell-out right is the mirror image of the squeeze-out right: a minority shareholder may compel the majority shareholder to purchase his shares.
Withdrawal rights: Withdrawal rights (referred to in some jurisdictions as the “oppressed minority,” “appraisal” or “buy-out” remedy) give shareholders the right to have the company buy their shares upon the occurrence of certain fundamental changes in the company.

Executive Summary

This report assesses El Salvador's corporate governance policy framework. It highlights recent improvements in corporate governance regulation, makes policy recommendations, and provides investors with a benchmark against which to measure corporate governance in El Salvador. The OECD Principles focus on private-sector publicly traded companies, both financial and non-financial, but are also applicable to other public interest entities, including banks, insurance companies, and state-owned enterprises

The equity market in El Salvador is small and has not showed much growth in the past five years. Most observers blame unwieldy approval processes for new share offerings, and the predominance in the economy of small- and medium-sized family-owned companies which do not have an interest in becoming public. Given the limited depth of the market, both regulator (SSF) and stock exchange (BVES) have taken measures towards regional integration. El Salvador today is participating in a regional initiative to develop an integrated Central American capital market with Panama and Costa Rica.

Good corporate governance enhances investor trust, helps to protect minority shareholders, and can encourage better decision making and improved relations with employees, creditors, and other stakeholders. It is an important prerequisite for attracting the patient capital needed for sustained long-term economic growth.

Achievements: The regulatory framework in El Salvador has been revamped in August 2011 and the Superintendencies that regulate the capital market, the financial sector, and the pension fund are now integrated into one Supervisor, the Superintendencia del Sistema Financiero (SSF). As most of the issuers are financial institutions, the integration will enhance supervisory processes and consolidate monitoring. The authorities are working hard to ensure that integration process is fast and effective and it does not distract the legal reform agenda. They are also using the merger as an opportunity to increase El Salvador's compliance with international financial standards, including corporate governance.

The Law that constitutes the new integrated SSF highlights the need to focus legal and supervisory processes on corporate governance, and this paves the way for reforms in this area. In February 2012 the SSF issued a set of voluntary governance norms for financial institutions. The norms encourage constitution of risk committees, presence of independent members on the board, enhancements on the disclosure of board practices, and spells out the responsibilities of the audit committee, which is required by law.

The current standards for governance of issuers are significantly lower than the ones for financial institutions. Rules and recommendations on board composition, fiduciary duties, the review and approval of related party transactions, and non-financial disclosure are nascent. As their governance norms evolve, issuers could learn from the experience of financial institutions. The authorities have begun to take action in this direction and an Instructorio (Guideline) issued in 2011 by the BVES begins to shed some light on 'relevant facts' that the issuers need to share with

the regulatory authorities on a continuous basis. It has clear rules on timing of disclosure, but it still misses to regulate some key areas such as related party transactions and large transactions.

In this evolving legal and regulatory environment, awareness of corporate governance as a policy issue is still in its early stages. However, a number of companies have noted the importance of international corporate governance standards and are moving towards improved board practices.

Key Obstacles: The regulatory framework for corporate governance is incomplete:

- **Board practices in most companies are still fairly basic.** This is partially due to an outdated legal framework, a business community that is mainly family owned, and the lack of a market for capital that can push for enhancement of the practices.
- **Shortcomings of the Commercial Code and the Securities Law.** The Commercial Code and the Securities Law have not been updated in a while and many observers believe that a significant revision of the key provisions related to the corporate governance framework is long needed.
- Indeed, a number of provisions of the Commercial Code do not provide strong protection to minority investors and shareholder protections on related party transactions, large transactions, and dividends are still minimal.
- **Slow adoption of international accounting and auditing standards.** The process for adopting IFRS has been much slower than anticipated, due in part to a lack of preparedness by interested parties, including both the Accounting Board (CVCA) and the audit profession. The constraints on CVCA included limited financial resources and staffing. In addition, requirements to become an accountant and auditor are minimal. Neither a professional examination nor practical experience is required. This environment does not ensure that licensed practitioners have adequate technical knowledge and professional competence to perform quality audits and get up to speed with international standards.

Next Steps: The challenge for the authorities is to build awareness of good corporate governance and to develop an appropriate legal and regulatory framework for corporate governance that encourages the growth and development of the capital market. The authorities should focus on three areas that need urgent attention and relate to the enhancement of board practices, implementing stronger shareholder protections, completing the adoption of IFRS and ISA, and increasing more complete non financial disclosures. In this vein, three key steps should be undertaken:

- **Draft a corporate governance code** including strengthening the role of the board;
- **Update the Commercial Code**, including amending shareholders protections;
- **Recommendations for financial reporting and disclosure**, aimed at addressing accounting, auditing and disclosure weaknesses.

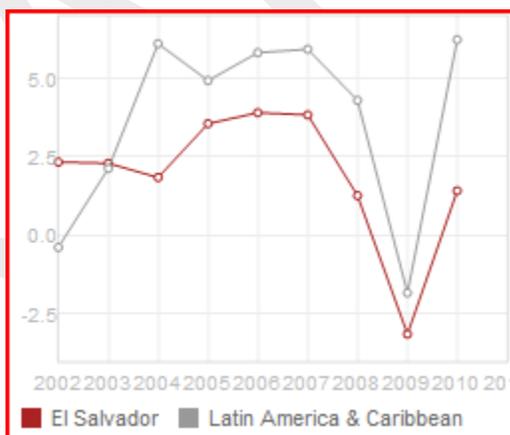
Landscape

The international economic crisis brought an end to a period of growth

As in many other economies, El Salvador felt the effects of the global financial crisis. The economy experienced a GDP contraction of 3.5% in 2009, and then managed growth of 1.3% in 2010. The contraction was a result of a drop in exports and remittances, higher levels of unemployment and rising food and energy prices. In response to the effects of the economic downturn, the Government formulated the Anti-Crisis Plan for 2009-11, with a stimulus package of nearly US\$600 million that included measures to create temporary jobs and increase the coverage of social security system.

The recovery is in progress but the economic structure of El Salvador still remains vulnerable to adverse natural events, high levels of violence and rising food prices, which may threaten the country's sustainable development and long-term economic growth.

El Salvador GDP Growth



The capital markets in Salvador have played a very limited role in the economy.

Capital Markets

The size of capital markets in El Salvador is in line with that of neighboring markets (e.g. in Costa Rica, Guatemala and Panama), but are still small, underdeveloped, and have so far played a limited role in the national economy compared with the role of relatively more advanced markets in their respective economies in the region (e.g. in Colombia, Peru and Chile). As of the end of May 2012, there were 38 listed stocks and a limited number of private corporate bond issues. Stock market capitalization was about US\$11 billion, equivalent to 48.9 percent of GDP.

Market capitalization is driven by financial institutions

Several causes discourage new equity issuance.

Pension funds are the largest domestic institutional investors, but their investment policies are severely constrained.

In 2012, there were four new share issuances.

The listed sector includes 38 financial institutions, for which listing is mandatory, but which are largely controlled by foreign institutions. The shares of the financial institutions are not generally traded, and have a minimal float in the market. The other listed companies are the four electricity generating companies, which were privatized (with strategic investor control) in the 1990s. Without the financial institutions, market capitalization drops to less than 6 percent of GDP.

There have been few initial public offerings (IPOs) in recent years. This is partly due to (-) unwieldy approval processes and (-) dominance of small- and medium-sized family-owned companies which do not have an interest in becoming public. Issuers have to list with the BVES before registering with the SV. Although both entities essentially have the same requirements; they conduct their own reviews of the information submitted. The dual approval process is often perceived as inconsistent, not cost-effective, and slow at times. In some instances, the prolonged approval process has pushed some large domestic companies to seek listing abroad and registering as foreign securities in the local market.

Issuers	2008	2009	2010	May-12
Number of Listed Companies	37	38	38	38
Number of New Issuers	6	2	2	4
Market Capitalization (US\$ m)	6,773	5,139	4,584	11,278
of which financial institutions (US\$ M)	5,631	4,185	3,831	10,637
Market Capitalization (% of GDP)	31.61	24.88	21.4	48.92%

Since the social security system privatization in the 90s, pension funds have increased their relevance in the financial system. At the end of 2009, pension funds assets were around US\$ 5 billion, about 23% of GDP. As of the end-2011, pension fund assets raised to US\$ 6.5 billion, about 29 percent of GDP. There are two pension fund administrators (AFPs) operating in the country and they dominate the institutional investors segment of the financial sector. About 84 percent of pension fund assets are invested in public debt securities. This is mainly due to: (i) a requirement to invest a minimum of 45 percent of assets in paper issued by the government via the Fideicomiso de Obligaciones Provisionales (Certificados de Inversion Provisional - CIPs), which in turn fund the pensions of retiring workers (ii) a lack of investable domestic securities and (iii) additional layers of fees as pension funds have to complete all

El Salvador is participating in a regional initiative to develop an integrated Central American market

their transactions on the BVES and through brokerage firms.

Given the limited number and size of issuers and investors, both regulators and stock exchanges have taken measures towards regional integration of securities markets. The regulators and Stock Exchanges of El Salvador, Costa Rica and Panama, have been active in this effort. After signing a series of Memorandum of Understanding (MoU), the regulators have so far agreed to create a council of Central American superintendents to explore lessons from global experiences with capital markets integration while the exchanges of El Salvador, Costa Rica and Panama have initiated the AMERCA project to allow brokers from the two of the countries remote access to the third country's jurisdiction.¹

El Salvador has made progress to spur the integration effort

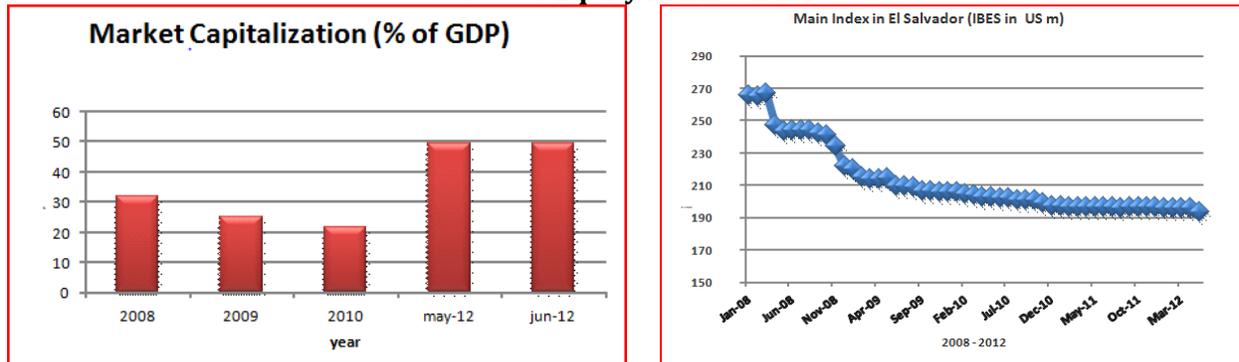
El Salvador has taken important steps to facilitate integration. Of note, the Ley de Mercado (art. 10) has been updated and it now allows foreign issuances, and the recently enacted SSFL attributes now to the SSF the power (art. 4N, and art.19X) to share non public information with countries with which MoUs have been signed.

El Salvador contains a critical mass of companies in which corporate governance can be relevant

Joint stock-companies (with variable or fixed capital) represent the overwhelming majority of Salvadoran enterprises, most of which are family-owned businesses. Joint-stock companies require a minimum capital of 2,000 USD and have to register to the Superintencia de Obligaciones Mercantiles (SOM) to operate. The number of entities SOM is supposed to monitor is estimated at between 30,000 to 50,000. Corporate governance improvements on disclosure, shareholder protection rights, and board practices can play a role to facilitate companies' competitiveness and ability to mobilize and allocate capital, and support the development of a capital market that is sustainable.

¹ In 2003, El Salvador and Panama signed a memorandum of understanding (MoU) that was expected to facilitate "fast track" registration and Panama also granted El Salvador the status of recognized jurisdiction. In 2003, El Salvador and Costa Rica signed another MoU designed to facilitate streamlining of the registration process but did not proceed further than a diagnostic of the issues.

Selected Equity Market Data



Source: SSF

Source: SSF

Figure 4: Equity Market: El Salvador vs. Regional and Global Emerging Markets 2010

	Listed Co's	Market Cap percent GDP	Market Cap (Billions \$US)	Turnover Ratio (%)	Market Cap percent of OECD Avg.	Market Cap (\$) % of OECD Avg.	Turnover ratio % of OECD Avg.	Portfolio Equity Inflows (Billions \$US)
El Salvador	38	21.4	4.5					
Costa Rica	9	4.2	1.4	2.8	6.1	0.1	4.0	.0
Panama	34	40.8	10.9	2.0	59.2	0.9	2.9	.0
South America								
Chile	227	167.9	341.6	19.7	243.5	29.0	28.1	.3
Colombia	84	72.3	208.5	13.4	104.8	17.7	19.1	.1
Argentina	101	17.3	63.9	4.6	25.1	5.4	6.6	-.2
Peru	199	64.9	99.8	4.7	94.1	8.5	6.7	.0
Bolivia	38	17.1	3.4	0.4	24.8	0.3		.0
Brazil	373	74	1,545.6	66.4	107.3	131.0	94.9	37.1
Ecuador	40	8.9	5.3	3.8	12.9	0.4	5.4	.0
Mexico	130	43.7	454.3	27.3	63.4	38.5	39.0	4.2
Lat America Avg	124	51	273.5	14.5	74.1	23.2	20.7	4.1
China	2063	81	4,762.8	164.4	117.5	403.7	234.9	28.2
India	4987	93.5	1,615.9	75.6	135.6	137.0	108.0	21.1
Russia	1383	20	32.4	5.4	29.0	2.7	7.7	.0
OECD Avg	786	69	1,179.9	70.0	100.0	100.0	100.0	19.0

Source: World Bank, World Development Indicators

Key Findings

The following sections highlight the principle-by-principle assessment of El Salvador's compliance with the OECD Principles of Corporate Governance.

COMMITMENT AND ENFORCEMENT

Legal Framework

El Salvador's legal and regulatory framework is based on civil law and the key laws governing corporate governance include: Commercial Code (1970), Capital Market Law (legislative decree no. 809) issued December 6, 2001, the Banking law (legislative decree no. 697, 1999) issued September 2, 1999; norms for external auditors of listed companies (RCTG 8/2010) and norms for auditors of financial institutions (NBP2-07).

The new SSFL paves the way for governance oriented reforms...

The regulatory framework in El Salvador has changed and the Superintendencies that regulate the financial sector are now integrated into one Supervisor, the Superintendencia del Sistema Financiero (SSF). The Financial System Supervision and Regulation Law (SSFL) issued in August 2011 highlights the need to focus legal reforms and supervisory processes on corporate governance (Art. 35 k). This has already generated effects as a set of norms for the corporate governance of financial institutions were enacted in February of 2012 (NPB4-48).

..yet the overall legal framework remains skeletal and outdated

The Commercial Code and the Securities Law have not been updated in many years and many observers believe that a significant revision of the key provisions of the Commercial Code and Securities Law related to the corporate governance framework is overdue.

Institutional Framework and Enforcement

The joint stock company (sociedad anonima, or SA) is the incorporation form required to become an issuer. The Code contemplates various forms of corporate entities (sociedad en nombre colectivo, anonima a capital fixo and variable), the most commonly used by far being the joint-stock company with variable capital (sociedad anónima de capital variable or SA de CV). The institution in charge of oversight of the SA is the Superintendencia of Corporate Obligations (SMO). If SAs become issuers,

SOM plays a monitoring function...

then the newly integrated Superintendence of the Financial System (SSF), and the stock exchange (Bolsa De Valores, or BVES) come into play.

Joint stock companies (sociedades anonimas) register with the Superintendence of Corporate Obligations (SOM) and file a variety of financial and non-financial documentation.

...but it faces operational challenges

SOM faces severe capacity constraints (ten staff) which hamper its effectiveness. With a staff of 10 inspectors, the number of entities SOM is supposed to monitor is estimated at 30,000 to 50,000. SOM is not equipped, whether in terms of IT system or human resources, to adequately oversee such a large population of corporate entities. For instance, the SOM is currently not able to track late filings and filings with qualified audit reports, both of which should trigger enforcement actions. A large part of its activities consist of receiving the filings and storing them. The SOM does not have any electronic storage facilities. It sends reminder letters to companies which do not comply with filing deadlines, but the sanctions it can impose are reprimands for first cases of non-compliance and fines equivalent to 15 to 50 monthly minimum wages (between US\$2,100 and 7,500). These sanctions have limited deterrent effect.

Supervision of Issuers will be strengthened

Regarding listed companies, the former SV, now integral part of the SSF, performs two types of controls: (i) review of financial statements filed with SV's Registration Department and (ii) on-site inspections by the Supervision and Control Department. Infractions have been reported mainly on late filing of financials but for example there is no history of restatement of financial statements by regulated entities as a result of inspections or reviews. Overall, sanctions are both rare and light, and they are not published.

The new SSFL strengthens monitoring of and access to issuer' information, It will also improve sharing of information among superintendencies and will create new departments for overall off-site activities.

The integration could distract the reform agenda

Effective integration will likely take time and it is essential to ensure that capital market issues are given appropriate importance and are not subordinated by the banking sector agenda and the integration process itself.

...and the SSFL transfers the right to issue regulation to the BCR

As part of this regulatory restructuring the Central Bank (the Banco Central de Reserva, or BCR) will be in charge of issuing norms and regulations while the SSF will manage the supervisory function. This separation of regulation and supervision into two different authorities may represent a challenge for the integration process but can also serve to check and balance the power of the integrated supervisory agency and

should allow for a more macro prudential perspective in regulation and more effective crisis management arrangements.

To ensure effective coordination, SSF and BCR have signed a cooperation agreement.

In September 2011, BCR and SSF signed an agreement (Convenio) to define roles, responsibilities, sharing of information, and decision making in the regulatory process. It will be essential that the BCR acquire technical skills in the area of prudential supervision and capital markets, and that the BCR staff responsible for drafting regulations and the SSF supervisory staff work together closely.

BVES is the only Exchange in the country

The Bolsa de Valores de El Salvador, BVES is a fully demutualized self-regulated organization (SRO), and is itself a listed company. The current regulatory framework (-) requires all products and players to be listed on a domestic Exchange, (-) allows a direct control of the only central depository in the country, CEDEVAL, by the BVES (-) restricts non-exchange entities to provide alternative electronic trading facilities.

The governance of BVES has been put into question

The current governance of the BVES has been put into question in several assessments performed in the past as the current CEO of BVES is also owner of a brokerage firm, which can lead to potential conflicts of interest.

SHAREHOLDER RIGHTS

El Salvador's Commercial Code contains many of the basic rights required by shareholders. However, many of its provisions appear to be designed for small, privately held companies, and are not always appropriate for listed companies with wider ownership, and other public interest entities.

Shareholder Meetings

Shareholders are allowed to participate and vote in the general assembly. Meeting invitations are circulated at least 15 days prior to ordinary meeting (AGM) and/or extra-ordinary general meeting (EGM).² The ordinary meeting approves the financial statements, board appointments, and dividends, while extraordinary meetings approve changes to articles of association, issuance of debt, and any other topic specifically included in the by-laws of the company.³ The meeting notice has to be publicly disclosed and has to include the agenda, date of the meeting, location, and constituting and approval quorums needed for first, second, and third session of the AGM or EGM.

Meeting notices have to be published but laws and related regulations do not go further than that. In practice, some companies publish them in newspapers of wide national distribution, although there is no legal requirement to do so. There is also no guideline on what the agenda should contain and how it should be itemized. When board members are to be elected, the agenda does not include names and/or profiles of board candidates.

Shareholders representing 5% of the capital can call a general meeting,⁴ and any shareholder have also the right to add items to the agenda.⁵

Shareholders can vote in absentia, or can use electronic means to participate.

Increase or decrease of capital is decided at the EGM with constituting and approval quorums of $\frac{3}{4}$ of the shares. Shareholders can exercise pre-emptive rights 15 days after EGM decision is made and can acquire shares of new issuance in proportion to their shares.

Companies can also waive the obligation to circulate notice and agenda if all shareholders or the representatives of all the shares agreed to do

Shareholders have the right to participate at the GMS, but....

...companies are not required to widely distribute meeting notice and agenda tends to be succinct

Shareholders can call an AGM and add items to the agenda

Shareholders have pre-emptive rights

Company can void circulation of notice

² Art. 228, Commercial Code

³ Art. 224, Commercial Code

⁴ Art.231, Commercial Code

⁵ Art. 235,Commercial Code

and agenda

so.⁶ In practice, as the vast majority of companies in El Salvador tend to be family owned and ownership is concentrated in the hands of a few family members, AGM and EGM can take place without the need to follow the provisions of the Commercial code. Although this flexibility is welcome for the vast majority of the closed joint-stock companies, this practice has obvious consequences on issuers' disclosure and transparency of corporate practices, decision making processes, and may impede adequate oversight by the pertinent supervisory authorities, ie Bolsa and SSF.

Minority shareholders can elect board members but the right is subject to stringent conditions

Appointing board members

Minority shareholders are entitled to elect one board member (art. 263 of Commercial Code) but only if the board is composed of at least three members and the board seat is requested by shareholders representing at least 25% of the shares. As this threshold is fairly high, ownership is very concentrated, and boards tend to be very small in size, this right is practically never exercised and ultimately board composition mirrors the interest of the controlling owners.

Minority shareholders have fairly weak protections in the law on a number of aspects

Minority shareholder protection mechanisms

Minority shareholders have very limited protections under the law:

Ex-Ante provisions

- *Shareholders are not protected from abusive dilution* While shareholders control the increase in authorized capital, share issuance can be delegated to the board, and there is no time limit within which boards must act. As a result, boards and controlling shareholders have significant discretion. Although the Code of Commerce gives shareholders pre-emptive rights, they can be waived in the bylaws.
- *Shareholders are not protected from related party transactions.* There are no provisions in the Commercial Code or Ley de Mercado to define related party transactions and identify a decision making regime for them. Boards approve related party transactions and shareholders have no say via the General Assembly. Shareholder rights are further hampered by minimal disclosure of these transactions as in practice companies succinctly disclose them in the notes of the financial statements. Details on terms of the transactions, evaluation of the appropriateness of the transaction,

⁶ art.233 of Commercial Code.

and nature of the transactions are barely mentioned. This is confirmed by the Protecting Investors indicator in Doing Business.

	El Salvador	LCR	OECD
Extent of disclosure index (0-10)	3	4	6
Extent of director liability index (0-10)	0	5	5
Ease of shareholder suits index (0-10)	6	6	67
Strength of investor protection index (0-10)	3.0	5.1	6.0

Source: Doing Business. www.doingbusiness.org

- *Right to dividends is not regulated in the law.* Although shareholders can approve the distribution of profits during the general assembly meeting, the Code of Commerce does not require a minimum mandatory dividend. In addition, the company is not required by law to pay the dividends within a specific time frame and is not required or encouraged to have a dividend policy in place.
- *Rules for large / significant transactions are weak.* There are no legal requirements for shareholder approval of large (sometimes called “material” transactions), as required by the OECD Principles.
 - *No regulation on changes in control:* There is no requirement for a shareholder who crosses a certain threshold of ownership to make a general public offer for all outstanding shares
 - *Protecting shareholders from illegal insider trading is still minimal:* Illegal insider trading is regulated under the Ley de Mercado (art.35). Directors and managers have an obligation of secrecy of corporate information, and cannot use the information to their economic advantage. What the law does not require is to make trading by insiders public and to define closed or restricted periods during which boards and managers are not allowed to trade. Given the gaps in the framework, market participants believe that cases of insider trading may go undetected / unprosecuted.

Ex-Post provisions:

- *Minority shareholders can sue managers:* The liabilities of managers can be invoked only by agreement of the AGM, by injured third parties when the administrators have failed in the duties expressly imposed, or by shareholders representing at least twenty-five

percent of the capital stock.⁷ Assets obtained as a result of the claim, after deducting the expenses of the trial, will become part of the capital stock. Law suits are not very common and the introduction of a law on commercial dispute resolution alternatives has not been yet picked up by the market.

Companies and CEDEVAL keep a book of shareholders which can be consulted by shareholders and regulatory authorities

Shares in listed companies are fully transferable

Shareholder Recordkeeping

All companies must have a book of registry of shareholders that shareholders and those with a demonstrated legitimate interest have the right to inspect at any time. The companies that issue shares by electronic annotation are registered at CEDEVAL (Art. 40 Commercial Code), which maintains the Register of Shareholders. The Depository provides online information to regulatory agencies so they can establish that the percentage of shares of each shareholder in the audited company is within the limits of law. Currently, only two issuers (Cedeval and BVES) have de-materialized their shares.

Shareholders in listed companies are by law able to freely transfer their shares. Salvadorian companies can issue bearer shares and nominative shares and are not required to de-materialize their shares.

⁷ Article 279 and 280 of the Commercial Code.

DISCLOSURE AND TRANSPARENCY

Company Reporting

The law subjects a large number of companies, including small businesses, to the accounting and auditing requirements.

All joint stock companies must prepare annual financial statements, including a balance sheet, income statement, statements of changes in equity and related notes in accordance with “the evaluation criteria and accounting principles issued or authorized by the Accounting and Auditing Monitoring Board (*Consejo de Vigilancia de la Profesión de Contaduría Pública y de Auditoría* or CVCA).

Financials are reported frequently

Issuers are required to provide financial statements to the SSF on quarterly basis, and the statements are then made available to shareholders via the SSF website. Companies also publish non-audited financial statements on a semiannual basis in a national newspaper. Statements are audited once a year and filed with the BVES, the SSF, and to the Internal Revenue Service. Corporate groups and financial conglomerates are required to present consolidated statements.⁸

Non-financial disclosures for issuers are very limited

In the prospectus, prospective issuers have to disclose to the public a series of governance related information from board and executive composition to members’ CVs.

The Ley De Mercado requires also companies to communicate to the authorities (BVES and SSF) relevant facts (*hechos relevantes*) that will then be posted on the BVES and SSF website. Relevant facts are defined as any information that has a positive or negative impact on the legal, economic, and financial situation of the company. This norm has been recently (2011) integrated with a guideline that lists what should be considered relevant.^{9,10} Items include: changes in executive and board membership, changes in the organizational structure, shareholders with more than 10 percent, group structures, and auditor’s certification.

Banks are also encouraged to prepare a governance report

Banks are encourage to integrate the non-financial disclosure with a board report which includes general information about the institution, its affiliates, and the conglomerate composition, ownership structure, main shareholders and related stakes; main shareholders of the controlling corporation, number of AGM and EGM general meetings celebrated during the year. It also has details on board, i.e. members, number of meetings, members of the senior management, members of the audit committee, risk committee.

⁸ Art. 282 Commercial Code

⁹ Art. 34 of Ley de Mercado, and Instructivo 1-2011 of BVES.

Accounting and Auditing Standards

El Salvador decided in 2000 to adopt IFRS and ISA...

...yet implementation of IFRS standards have proven to be an issue

Financial requirements differ from company to company

In 2000, El Salvador decided to adopt IFRS and ISA, a step consistent with the goal of enhancing the economy's integration in world markets and attract FDI.

CVCA established a phased-in adoption schedule and some efforts have been made to prepare companies and auditors. However, the process of adoption has been much slower than anticipated, for a variety of reasons, including:

- A lack of preparedness by interested parties;
- Lack of identification of the key implementation challenges;
- Adoption of the 2003 version of IFRS, which differs significantly from the most current version;
- Translation of the standards has proven to be more difficult than expected, as in other Spanish speaking countries.

The scope of IFRS application to local Salvadorian companies has been modified several times.¹¹ The financial reporting requirements of Salvadoran corporate entities resulting from this process are summarized in table below.

Accounting standards required by type of business entity¹²

Type of entity	Applicable standard prior to IFRS	Year of implementation – Applicable standard	
		Per previous CVCA Resolution (December 5, 2003)	Per current CVCA Resolution (December 22, 2004)
Listed companies except those regulated by SSF	No legal definition	2004 – full IFRS	2004 – NIF/ES
Companies regulated by SSF	SSF Norms	2004 – full IFRS	SSF Norms, IFRS otherwise
Large ³¹ non-listed enterprises	No legal definition	2005 – full IFRS	2005 – NIF/ES
Small and medium enterprises (SMEs ³¹)		2006 – “SME” IFRS	2006 – “SME” IFRS
Very small businesses		Exempt from applying IFRS	
Pension funds and AFPs	SP Norms	Outside the scope of CVCA – SP Norms apply	
SOEs		Government accounting standards	

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Accounting standards' uncertainty has generated confusion

Currently, the overwhelming majority of licensed auditors do not know the standards well enough to be able to ensure that they are applied by the companies they audit. It also appears that the companies themselves

¹¹ Key milestones in the process for adopting IFRS in El Salvador include: in 2000, CVCA issued a Resolution (Acuerdo) requiring all corporate entities in El Salvador to apply International Accounting Standards (IAS, since then incorporated into IFRS). In 2003 the CVCA issued a Resolution that postponed the application of IFRS to the year 2004. In 2004, the CVCA issued a new Resolution to exempt SSF-regulated companies (i.e., banks, insurance, etc.) from the requirements to apply IFRS.

¹² CG ROSC Assessment for Accounting and Auditing, 2005.

¹³ CG ROSC Assessment for Accounting and Auditing, 2005.

have not made much effort to prepare for IFRS.

Requirements to become an Accountant and Auditor are minimal

Lack of preparedness by the accounting industry is also due to low requirements to become accountants. The main requirement is a bachelor degree in accounting but no minimum standard has been set for the content of universities' accounting curricula. In addition, in El Salvador accountants do not have to take a professional certification exam and no practical experience is required. This does not ensure that licensed practitioners have adequate technical knowledge and professional competence to perform quality audits.

CVCA oversight of the profession is minimal

CVCA does not monitor accountants and auditors' compliance with ISA. It has plans to introduce periodic quality control but no process has been defined at this point. A continuing professional development obligation for public accountants has been established; however, this obligation is not adequately monitored and sanctions for non-compliance are relatively mild.

CVCA has limited resources

At present the CVCA depends almost exclusively on budgetary allocation from the Ministry of Economy. Also, there is no full time, executive level position within the CVCA.

Standards of Audit for issuers

Auditors of listed enterprises are required to have three years of experience, and no criminal conviction. In addition, external auditors cannot be members of the board of the company they audit, and cannot audit an institution if they have outstanding borrowings for more than 50%. No rotation of the audit team is required but auditors' independence and audit plan are regulated in fair detail in the norms.

In financial institutions, standards of audit are higher

With respect to the conduct of audits for financial institutions, auditors need to register to SSF. Auditors can register if they have a minimum of five years of experience, knowledge of the ISA Standards, cannot be board members or employees of the audited company and cannot have outstanding borrowings (up to 50%) with the company they audit.

The most innovative requirement is represented by a score card that the SSF has recently introduced to evaluate independence, qualifications, and professional experience of the auditors before granting registration. All the factors (see below) are weighted and auditors have to score at least 60% to obtain the authorization to register.

Factor	Assigned Weights
1. Independence	30
1.1 Economic Independence	15
1.2 Number of Audited companies	15
2. Academic Background	25
2.1 Degree Level	10

2.2	Professional Auditors	10
2.3	Special Studies	5
3.	Quality and Experience	35
3.1	Length of professional experience	5
3.2	Diversity of audited companies	10
3.3	Experience in Financial Sector	5
3.4	Work Quality	15
4.	Organizational Efficiency	10
4.1	Organization and defined functions	5
4.2	Audit Teams and composition	5
Total		100

BOARD PRACTICES AND COMPANY OVERSIGHT

The Role of the Board

The board of directors is where key corporate governance issues converge. The board is responsible for strategic guidance and oversight of management, and functions as a trustee for shareholders. These are important responsibilities, and the way that the board organizes itself will be an important factor in determining how well it fulfills its responsibilities. A professional, independent and vigilant board of directors is essential for good corporate governance.

Board standards for issuers are low but for financial institutions they have been recently upgraded

Issuers and financial institutions in El Salvador have to incorporate as joint-stock companies (sociedad anonima) and follow the provisions of the Commercial Code and the Ley de Mercado de Valores. Overall the provisions of the Commercial Code and the Ley de Mercado de Valores related to boards of directors are still fairly basic and do not capture many international governance standards. Standards for financial institutions are more sophisticated (Banking Law and related regulations) and have been recently enhanced in February 2012 with the issuance of a specific regulation (Norma NPB4-48).

Issuers

AGM elects boards and boards appoint CEOs

Companies in El Salvador are supervised by a one-tier board, and managed by the top executive, i.e. the CEO. The AGM appoints the board and can delegate to the board the appointment of executives (Art.117 and Art. 270 of Commercial Code). In practice, boards appoint and select the CEO based on a profile indicated by the AGM, which is often controlled by the majority owner. The board is responsible for electing, overseeing, and advising the CEO and ultimately responsible for the overall administration of the company (art.254). The board can be composed of executive (managers) and non-executive directors.

Board responsibilities are not defined

The Commercial Code defines the board as ultimately responsible for the company. However, it does not describe board details and responsibilities for oversight of management, internal controls, and governance.

Board Size and CEO/Chairman separations are not regulated

Boards are not required to have a minimum or a maximum number of members, but members of the board cannot serve for more than seven years (art.255). CEO and Chairman positions are not separated. In the practice, the majority owner typically serves as board chairman or CEO and at times serves both roles.

Appointment of alternates

The AGM is required (Art. 264) to designate at least one alternate per board, unless the company by-laws require a higher number. The practice shows, at least in banks and some corporations, that each member of the board has at least an alternate which is fairly involved in the board functioning. In addition, the Commercial code allows minority shareholders (25%) to appoint their respective deputy/alternate.

The practice of appointing alternate directors is not consistent with modern views of the role and duty of the board, which stresses each individual's membership in a collegial body, and can instead result in a "representative" board in which each member acts in the interest of those who appointed him or her, and not in the interests of the company.

Fiduciary duties are not fully addressed in the Commercial Code...

Commercial Code and Ley de Mercado do not define duty of loyalty and duty of care but briefly mention that directors should have the capacity required to do business and not to be 'incompatible' with the provisions of the Commercial Code.¹⁴

...but there are liabilities associated to the job at the top

Board members are jointly and severally liable for damages resulting from willful misconduct or ordinary negligence in the course of management oversight.¹⁵ This liability translates into civil law considerations:¹⁶ ordinary negligence is defined as lack of care and diligence that individuals ordinarily employ in their own business. The criminal Code also contemplates liabilities when the person in charge of the management, administration or care of others property, who prejudices its owner or obtain for its own or for third parties unfair advantages in detriment of others can be punished with prison from three to five years.¹⁷

A financial liability regime for directors is present in the law

Under the Commercial Code, companies can require board members of listed companies to set aside a non-transferable guarantee, to cover any liabilities that they may incur in the performance of their duties. ¹⁸This practice has not been widely adopted in company charters.

Issues around remuneration have not been tackled yet

The legal framework does neither require nor encourage boards to set remuneration policies or to publicly disclose them. Executive remuneration policies do exist in some companies, and are generally developed by the board, but are not disclosed. The framework also does not require or encourage non-executive directors or the constitution of remuneration committees to take the lead in the development of executive remuneration.

¹⁴ Art. 257 of Commercial Code.

¹⁵ Art.274 of Commercial Code.

¹⁶ Art.42 of Civil Law.

¹⁷ Art. 215-218 Criminal Code.

¹⁸ Art 259, Commercial Code.

Committees, independent members and board member profiles

Issuers are not required or encouraged to set up board committees or have independent members. Board composition and the profiles of board members are only disclosed to the public when the prospectus is submitted. Changes in board membership are communicated to BVES and SSF as 'relevant fact', and then to the public via the SSF website.

Financial Institutions

Financial Institutions present higher standards

The standards for governance in financial institutions are quite different. The Banking Law and especially the recently enacted voluntary guidelines in Norma NPB4-48 bring the practices of financial institutions one step closer to international standards.

Board Responsibilities are well assigned in the Banking Law and in Norma NPB4-48

According to the applicable laws and Norma NPB4-48, boards of financial institutions are in charge of approving strategic plan and annual budgets; policies on risk management, conflicts of interest and related party transactions; remuneration policy and performance evaluation; and policies for the development of internal control systems. Also the board is charged to appoint, compensate and dismiss the Executive Director or General Manager. The board is also in charge to approve the operating organization and functions of the institution, to ensure the integrity of the accounting and financial reporting, and to approve a code of ethics.

Fiduciary Duties are well detailed in the Law and integrated by the NPB4-48

The Banking Law requires board members, executives, and alternates to ensure that public deposits are managed with the honesty, prudence and effectiveness, as good merchants in their own businesses.¹⁹ They also have to refrain from carrying out their duties in a way that intentionally distorts the objectives of the prudential regulations. Last but not least, they are liable for the information provided to the SSF and to the public, which has to be truthful and reflect transparency, and the true financial situation of the institution.

These fiduciary responsibilities are further expanded by the Norma NPB4-48 as board members and executives have to: I) protect the rights and interests of the depositors, insured persons and clientele; II) protect the rights and interest of the shareholders and establish mechanisms of equal treatment; III) develop communication and information policies with the shareholders and clientele; and IV) perform their functions putting the company interest first.²⁰

¹⁹ Art. 32, Banking Law.

²⁰ Art. 9, Norma NPB4-48.

Board Size

The banking law requires at least three members (and three alternates) on the board. ²¹In practice, both board members and alternates attend board meetings together. [More on practices of meeting attendance].

Qualification criteria are present

Beside the fit and proper test performed by the SSF, the banking law provides some guidance on qualifications that board members and the alternates are supposed to meet. They need to have recognized honesty and extensive knowledge in financial and management matters. The chairman or his alternate has to have a minimum of five years of experience in management positions or as senior manager in banks or financial institutions. Financial institutions are also encouraged to disclose the category of each director under the Norma NPB4-48.

Financial institutions set up Audit Committees...

This is a requirement that is present in the Banking Law, new SSFL, and in Norma NPB4-48. The audit committee is formed by at least two non-executive members of the board of directors and one internal auditor, meets at least once a month, and is chaired by the non-executive director that carries auditing or financial experience. The responsibilities of the Audit Committee are well defined in the laws and include: a) Ensuring the implementation of the board, SSF, and BCR resolutions; b) monitoring reports from the internal auditor, external auditor and SSF; c) assisting in the design and implementation of internal control processes by proposing corrective actions; d) monitoring compliance of the external auditor and leading the process of responding to the observations made by the external auditor in the Management Letter; e) evaluating the quality of the work of internal audit and compliance with its program of work; f) proposing to the board and in turn to the AGM the appointment of external auditors and tax auditor.

...and can have one independent board member

To strengthen the general oversight function, the board can have at least one independent member (Art. 13 #2 of Norma NPB4-48). The independent member is not required to sit in the Audit Committee and no specific functions are assigned.

Definition of Independence

The definition of independence (Art. 12 of Norma NPB4-48) is well laid out and captures most of the details that can ensure true and objective judgment, which is the main rationale for having independent members on the board in the first place. The members of the board of directors should meet the following conditions: i) cooling off period from the institution and the related companies if part of a financial or economic group, of at least two years; ii) no direct or indirect ownership of the shares of the institution, iii) no relationship within the second grade of consanguinity or first grade of affinity with the board members.

²¹ Art. 33, Banking law.

**Risk Committee and
Corporate
Governance Code**

Norma NPB4-48 also encourages financial institutions to draft a corporate governance code and set a risk committee composed of non-executive member and management.

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Recommendations

Improving governance practices and effectively aligning them with international standards will support El Salvador's effort to accelerate broad-based equitable economic growth and development of sustainable capital markets. Specifically, improved governance would advance the following key goals:

Improving the investment climate. One of the priorities of the Salvadoran Government is to stimulate private sector growth. In order to reach that goal, El Salvador will need to update its company law and related standards. The goals should be to simplify legal requirements for less complex company forms, and to raise standards for listed companies, banks and other financial institutions and state-owned enterprises.

Leveraging the development of the private pension funds system. Increasing quality and reliability of corporate governance and shareholder protection will create opportunities for pension fund managers to diversify their investments into private sector securities, thereby reducing their dependence on the banking sector and offering prospects to increase average returns on investment.

Enhancing economic integration on regional and international levels. Regional integration will require the accelerated convergence of standards and practices of governance to international benchmarks to achieve greater integration with the major trading blocks. Institutional development and governance are needed to give perception and reality that the country has reliable laws and regulations.

Key Areas for Reform

The recommendations present a path to achieve the key goals and aim to address areas in need of legal and regulatory attention.

The recommendations are organized in three sections and relate to enhancement of board practices, shareholder protections, and financial and non financial disclosures.

- **Draft a corporate governance code** including strengthening the role of the board;
- **Update the Commercial Code**, including amending shareholders protections;
- **Update regulations and institutions for financial reporting and**

disclosure, aimed at addressing accounting, auditing, and disclosure weaknesses.

Draft a Code of Corporate Governance for El Salvador

Findings of the ROSC

The ROSC shows that board practices and the underlying legal principles are still fairly basic. However, many aspects of international good practice related to boards of directors are aspirational and are difficult to legislate. Instead, in many countries the authorities have chosen to address board issues through a “code of corporate governance”.

Corporate governance codes of best practice are sets of nonbinding recommendations aimed at improving and guiding the governance practices of companies in a specific legal environment and business context. Codes are typically based on principles and focus on country-specific issues. Codes of best practice have now been adopted in many countries as a way of introducing and building awareness of international standards, and adapt them to the local environment.

The public and private sectors should work together to draft a corporate governance code

The regulatory authorities, namely SSF, BCR, and SOM should consider drafting a corporate governance code based on a ‘comply and explain’ rule; companies are not required to comply with the Code, but must disclose their compliance with it. The committee that drafts the code should include industry associations, companies, and institutional investors, in addition to government authorities and superintendencies. The key objective of the committee should be to meet investor demand and companies needs through the lens of corporate governance. In this respect, the committee should: (i) identify the key corporate governance obstacles that pension funds and companies face and (ii) draft a code that addresses these weaknesses.

The Code should apply to all “public interest entities”

The scope of the Code should be set by the drafting committee, but should include at a minimum all public interest entities (including issuers, financial institutions, and possibly state-owned enterprises).

The board of directors should be the main focus of the Code

In El Salvador, many of the issues identified in this assessment relate to the role, responsibilities, and functioning of the board of directors, and should address the following areas:

Board Size: the Code should recommend a minimum and maximum board size

Alternates: Companies adhering to the code should not elect alternate directors to the board

Separation of Roles: Companies adhering to the code should separate the

positions of CEO and Chairman.

Board duties. The Code should clearly state that directors owe their loyalty to the company and all shareholders, and discuss how to balance this against duties to the institution that may have appointed them.

Functionality. The Code should list the responsibilities of board members (in line with the OECD Principles), and distinguish the responsibilities of the board from management.

Board member commitment and compensation. The Code should set recommendations for increasing the frequency of board meetings, and at the same time increasing board member compensation in line with the increased commitment, and higher expected levels of professionalism, qualifications, responsibility, and liability.

Disclosure: Board and executive member profiles should be fully disclosed

Self-Evaluation: Boards should adopt board self-evaluations

Update the Commercial Code

Minority shareholders have relatively limited protection under the law and the ROSC has highlighted several areas that need urgent attention. A reform plan for the Commercial Code should be considered. The focus areas regulators should pose the attention to are:

- *Abusive dilution* While shareholders control the increase in authorized capital, share issuance can be delegated to the board, and there is no time limit within which boards must act. As a result, boards and controlling shareholders have significant discretion. Although the Code of Commerce gives shareholders pre-emptive rights, they can be waived in the bylaws.
- *Fiduciary Duties:* Duty of loyalty and duty of care should be stressed in the Commercial Code or regulation. They should be properly defined according to the OECD principles and should pave the way to set shareholder redress mechanisms in case of fiduciary violations.
- *Related party transactions regime.* There are no provisions in the Commercial Code or Ley de Mercado to define related party transactions and identify a decision making regime for them. Boards approve related party transactions and shareholders have no say in the process. Shareholder right is further hampered by minimal disclosure of these transactions as in the practice companies succinctly disclose them in the notes of the financial statements. The regulation or the update of the Code should be able to provide: (-) definition of related parties, (-) identification of transactions, (-)

Minority shareholders have fairly weak protections in the law on a number of aspects

requirements by the board to express a binding evaluation on the appropriateness of the transaction. Transactions should be approved by the AGM and nature, terms, and parties disclosed to the public.

- *Dividends.* Although shareholders can approve the distribution of profits during the general assembly meeting, the Code of Commerce does not require a minimum mandatory dividend, a time frame for payment, and a dividend policy. These three elements should form the grounds to enhance the dividend regime.
- *Large / significant transactions.* There are no legal requirements for shareholder approval of large (sometimes called “material” transactions). Large transactions should be defined and clear thresholds identified. Companies should seek EGM approval for these transactions.

Addressing financial reporting and vetting of financial information disclosure

The reporting process of financial and non-financial information in El Salvador is still weak and requires attention. Three dimensions should be considered in this respect: (-) accounting standards implementation, (-) strengthening audit profession and oversight and (-) disclosure of board practices.

Bring forward the IFRS and ISA adoption agenda

CVCA should put in motion a detailed adoption plan grounded on the following key action:

- The CVCA should adopt the most current issue of IFRS
- CVCA should seek to enter into cooperative arrangements with other Latin American countries that have adopted IFRS

CVCA should develop a training plan for accountants, both in public practice and in companies

Strengthening the accounting and auditing profession

To increase the credibility of the audit profession El Salvador should implement the concept of certified public accountant. This would be an important move to strengthen the reputation of the Salvadoran accounting profession, both domestically and abroad. A professional examination is one of the cornerstones of a certification system in any country. Such system should also include as a pre-requisite three years of professional experience in accounting and auditing and an adequate academic background in those fields.

**Strengthening
Institutions
responsible for
oversight: CVCA...**

A system of professional oversight as the one El Salvador has sought to establish cannot function without adequate resources, which include information technology, a permanent staff and funds to compensate practitioners who assist the oversight board in fulfilling its functions. Registered public accountants should be required to pay a membership fee to the CVCA. Moreover, the oversight system is intended to benefit the members of the profession by fostering a practice of quality and providing guidance on the application of accounting and auditing standards. Accordingly, it is only natural that registered members should contribute to funding such system.

....and SOM

The Superintendency of Corporate Obligations (SOM) should establish enforcement guidelines and increase its institutional capacity to carry out its supervisory functions. In order to make the best use of its resources, the SOM should develop a risk-based strategy for supervising companies, taking into account the type of sectors, the economic size and the track record of companies in terms of their compliance with corporate obligations. A set of written guidelines and a supervision manual should also be defined. The information system used by the SOM should be upgraded to allow the screening of companies that do not comply.

**Improve non-
financial disclosure**

Information about boards that should be disclosed to the market includes:

- Nomination and election processes of board members;
- Board member profiles
- Director's length of service as a board member
- Basic information about the primary employment of board members
- Other board seats directorships whether is listed or non-listed sector
- Attendance records of board members in board and committee meetings
- Minutes of the previous shareholder meeting on their corporate website as relevant information.

Action steps

- **Short Term**

1. The SSF in conjunction with the BCR should adopt a regulation/code for the corporate governance of issuers and a related supervisory module grounded on qualitative and quantitative indicators
 - ✓ The SSF in conjunction with the BCR should form a task force to serve as a steering committee and drafting team with international support as needed
 - ✓ The task force should identify the key corporate governance issues and regulatory gaps on the basis of the CG ROSC findings and ensure these are addressed in the regulation/code.
 - ✓ The SSF in conjunction with the BCR should organize a thorough stakeholder engagement process to ensure that there is widespread buy-in.
 - ✓ In the same vein, it would be appropriate to develop corporate governance score cards for each individual issuer.

Medium Term

2. Each issuer should develop a corporate governance implementation plan, addressing how they will implement the corporate governance regulation.
3. The SSF supervisory framework should incorporate the supervisory module of corporate governance.
 - ✓ The SSF in conjunction with BCR should organize an in-depth training on corporate governance for its supervisors – both on- and off-site.
 - ✓ The SSF in conjunction with BCR together with other government authorities should help encourage the development of a training course on corporate governance for issuers' officials:
4. Over the medium-term, a corporate governance training institution should be identified that can act as a training institute on governance.

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