



**Economic Commission
for Africa**

Codes and Standards for Good Economic and Corporate Governance in Africa:

Summary of Key Issues and Declaration of Principles

Prepared for the NEPAD Steering Committee



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Introduction

1. In the context of improving economic and corporate governance in Africa, the NEPAD Heads of State and Government Implementation Committee, at its October 2001 meeting, agreed that “African leaders should set up parameters for Good Governance to guide their activities at both the political and economic levels”. In that regard, it was also decided that they would “consider and adopt an appropriate peer review mechanism and code of conduct”. The ECA was given the task to develop a technical document entitled *Guidelines for Enhancing Good Economic and Corporate Governance in Africa*. This was done in consultation with the NEPAD Steering Committee and other partners. The development of the Guidelines also benefited from review and input by a Committee of African Ministers of Finance and Governors of Central Banks at a meeting held in Addis Ababa from 3 to 4 March, 2002.

2. This Summary of Key Issues and Declaration of Principles is intended to assist all African governments in their efforts to improve the quality of economic and corporate governance in their respective countries. It identifies a prioritized list of codes and standards that all African countries should strive to observe, within their capacity capabilities, and it suggests an African owned and managed peer review mechanism for African countries to implement as an innovative idea toward self-monitoring, and as a demonstration of their commitment to public accountability (See Annex). A draft version of this entire document as well as the Guidelines upon which it is based were approved by the Heads of State and Government Implementation Committee at their meeting on 26 March 2002 in Abuja.

3. Increasingly, African leaders have recognized that the process of achieving good economic and corporate governance in their countries is also heavily influenced by a considerable number of political factors. Good political governance is a prerequisite for good economic and corporate governance. This is captured in the NEPAD framework document (Para. 79) in the following manner: “It is generally acknowledged that development is impossible in the absence of true democracy, respect for human rights, peace and good governance. With the *New Partnership for Africa’s Development*, Africa undertakes to respect the global standards of democracy, the core components of which include political pluralism, allowing for the existence of several political parties and workers’ unions, and fair, open, and democratic elections periodically organized to enable people to choose their leaders freely”. These issues on political governance are being addressed by the sub-committee on Peace and Security chaired by South Africa.

4. Fundamental to the interaction between political governance, on the one hand, and economic and corporate governance on the other, is the ability of the state to provide the requisite institutional framework to support good governance outcomes. As recognized in the NEPAD framework document (Para. 83), for African public institutions to function effectively, considerable

reform and capacity-building will be required. “Those institutional reforms will need to focus on:

- Administrative and civil services;
- Strengthening parliamentary oversight;
- Promoting participatory decision-making;
- Adopting effective measures to combat corruption and embezzlement; and
- Undertaking judicial reforms”.

The Importance of Good Economic Governance to Africa

5. The key factors that enhance good governance of an economy are transparency, accountability, an enabling environment for private sector development and growth, and institutional capacity and effectiveness. Good economic governance is necessary in order to enhance the capacity of the state to deliver on its economic mandate. That mandate includes eradicating poverty and improving economic growth. However, the majority of our countries now lack the capacity to meet that mandate due to deficiencies in their economic governance structures. Those deficiencies include the lack of an appropriate institutional framework to guide economic policy-making and execution; an emerging and fragile civil society unable to contribute effectively in formulating government actions; similarly new parliaments; and the lack of consultative mechanisms for engaging the private commercial interests for inputs into sectoral planning or other national economic decision-making processes.

6. Good economic governance would attempt to evolve well-defined structures; harmonious and complementary fiscal, monetary, and trade policies; and establishment of monitoring and regulatory authorities for promotion and coordination of different economic activities. It consists of the entire institutional framework of a government engaged in the evolution and implementation of general economic policy affecting its internal and international economic relations. That institutional framework must be competent to undertake the implementation of economic policy and capable of making the necessary adjustments as necessitated by government policy. In fact, good economic governance is regarded as being primarily dependent on the strength of its institutional framework; the flexibility, maneuverability, and resilience to the changing political, economic, and social development; and the ability and competence of the personnel to take bold, practicable, and rational decisions.

7. Recognizing that the responsibility for governance issues lies first and foremost with the respective national authorities, African states must therefore commit to improving economic governance for, among others, the following reasons:

- To enhance their ability to implement development and poverty reduction policies with scarce resources;
- To execute public management functions in an accountable manner;
- To create a credible policy environment in which domestic and international investors can have confidence and trade can be enhanced;
- To strengthen absorptive capacity to attract and mobilize development assistance flows;

- To demonstrate transparent and participatory economic policy-making and execution as well as an open flow of information available to all stakeholders; and
- To signal an adherence to standards of institutional functioning free of corruption.

8. The foregoing reasons for achieving good economic governance on the African continent give rise to a number of benefits. These include maximizing the gains from globalization; accelerating growth; reducing poverty; and creating a more stable, predictable macro-economic environment. Reaping the gains from globalization, for example, is the antithesis of economic marginalization.

The Importance of Good Corporate Governance to Africa

9. Good corporate governance is a source of competitive advantage. Where the rules of the game, and the mechanisms and instruments contributing to those rules, enable all corporations (whether private, publicly traded, or state-owned) to understand their rights and obligations better, the greater the likelihood that corporations will consider doing business in those countries than in countries where the rules of the game are arbitrary. The rules of the game include all of the necessary laws and regulatory instruments applied in a consistent culture of enforcement and compliance that is also credible and well understood, both internally and across borders, so as to instill investor confidence.

10. Predictable rules of the game attract long-term private domestic and foreign investment. Private investment, in turn, is a necessary ingredient for employment generation, spurring economic growth, and the reduction of poverty. It also contributes to national treasuries through the payment of corporate taxes. Currently, in sub-Saharan Africa, gross domestic investment stands at about 17 percent of GDP and falls far short of investment in other parts of the world. In addition, sub-Saharan Africa accounts for a very small share of foreign direct investment (1 percent) in the world economy. By moving toward good corporate governance, African countries can greatly facilitate private domestic and foreign investment in their quest for renewal. Current estimates suggest that achieving the 7 percent growth rate required to reduce poverty by one-half by the year 2015, will require investment equal to 33 percent of GDP.

11. Good corporate governance also influences private investment through the globalization process. African leaders recognize that globalization can facilitate much needed inflows of private investment and transfers of technology, in addition to increasing the access of their countries' exports to world markets. However, negative perceptions of the continent's economic and political activities have contributed to the weakness of the continent in attracting capital flows. Fundamentally, the globalization process, as exhibited through the international financial architecture, necessitates that African countries move toward much more robust corporate governance. As indicated in the NEPAD framework document (Para. 151), "the first priority is to address investors' perception of Africa as a 'high-risk' continent, especially with regard to security of property rights, regulatory frameworks and markets".

12. Among the key elements of that international financial architecture is the requirement to broaden and deepen local capital markets to attract investors. Capital markets contribute to the strengthening of financial systems which, in turn, contributes significantly to domestic and international financial intermediation, helping to mobilize savings and channel them efficiently to productive investments. If African capital markets are to develop and grow,

corporate governance standards will need to improve to give investors the protection required to encourage them to provide capital.

13. Moreover, some of the recent financial crises in emerging market economies have demonstrated that all developing countries need to put in place good corporate governance mechanisms which can inhibit speculative transactions and flows of short-term capital while, at the same time, encouraging long-term capital inflows, especially foreign direct investment. By bringing African financial sectors up to more modern standards, African countries can improve decision-making and create an environment that encourages investment and savings. A stable and transparent environment for commercial transactions is essential for the mobilization of investment, finance, technology, skills, and other important resources across borders, in order to promote growth and development.

14. While, as indicated, sound practices on corporate governance are essential to attract more private investment into Africa, especially for foreign portfolio and direct investors, the overall private sector development challenge facing the continent is much broader than building a competitive corporate sector. The bulk of private sector operations in African countries is in the hands of small and medium-sized formal enterprises or in the informal sector. They are typically owner-operated organizations, not incorporated under company law, or family businesses with no outside investors. The issues of governance that they face are therefore not the same as those faced by large corporations.

15. Given the important contribution that these small and medium-sized enterprises make to the growth of African economies, their further development must be vigorously promoted and support provided to them through strong public institutions which can work in partnership with the private sector not only in the area of governance but also with respect to access to markets for their goods and services; professional management techniques covering production management and investment planning; training for staff; and the introduction and use of appropriate management information systems especially in accounting and control systems to keep track of revenues and costs.

16. As major corporations have grown to become some of the wealthiest and most influential entities on the planet there has been a growing demand by citizens to ensure that they are subjected to basic requirements for accountability. Public outrage over environmental disasters and human rights abuses, such as sweatshop practices and forced displacement from areas of oil exploration, which have been linked to some multinational companies and their subcontractors, have put the media spotlight on corporate ethics. The agenda of corporate responsibility is important to Africa. Transnational corporations investing in Africa need to recognize the positive role they can play in strengthening an otherwise fragile social fabric in Africa, and thus lowering the risk to their investment.

17. The Global Compact initiated by United Nations Secretary-General Kofi Annan in 1999 provides a framework for good corporate citizenship. This set out to give a human face to the global market by focussing on the responsibility of businesses to “embrace, support and enact a set of core values in the areas of human rights, labor standards, and environmental practices”. In 2000, more than fifty major transnational corporations from diverse sectors took a public stand on the Global Compact and its principles.

18. Reflecting the Global Compact and related initiatives, some of the core components of good corporate citizenship include the following:

- a. Upholding environmental codes of conduct, such as those developed by UNEP and adopted at the 1992 UNCED Rio Declaration.
- b. Respecting labor standards, as developed by the ILO. These include upholding freedom of association and the right to collective bargaining, eliminating all forms of compulsory or forced labor, abolishing child labor, and eliminating discrimination in employment and occupation.
- c. Engaging with human rights organizations, including the UN High Commissioner for Human Rights and key partners such as Business for Social Responsibility.

19. It is clear that while globalization has raised living standards for many, it has made life more difficult for those dislocated by the whirlwind of change and it threatens to leave part of the world behind. There is a growing concern among many that an unchecked globalization might create disparities in the allocation of resources that will be hard to remedy. It is no coincidence that the disappointing economic performance of Africa reflects a failure to integrate into the world economy and thus to trade successfully and attract investment. The foremost challenge of globalization is to ensure that its fruits extend to all countries. Another important challenge of globalization is to tackle problems complicated by trade and investment ---income inequality and environmental degradation, for example.

Prioritizing the Codes and Standards of Good Economic and Corporate Governance Practices for Africa

20. Given the diversity of African countries in terms of economic development, political development, and institutional development, it is not possible that there can be an effective and efficient observance of all the relevant codes and standards across the continent. Despite the fact that many African countries already subscribe to some of the codes and standards, what is suggested here, instead, are those “fundamental” internationally, regionally, and domestically accepted codes and standards that all African countries should strive to observe within their capacity capabilities. In other words, the codes and standards that need to be complied with as a minimum requirement, given a country’s capacity to do so.

21. The fundamental aspect being referred to here is the broad consensus that permanent observance of these codes and standards will be good for the poor. The logic is that, in many African countries, those who are better off can afford to pay for the deleterious effects of bad governance (through bribery, for instance), whereas the poor are the least capable of bearing such costs. By extension, therefore, priority must be given to codes and standards, or best practices, that lead more quickly to pro-poor development outcomes, and African countries should commit to these.

22. The eradication of poverty on the continent is the ultimate goal. However, as acknowledged in the NEPAD framework document (Paras. 25-26), some bad policies and processes have led to the “entrenchment of a vicious cycle, in which economic decline, reduced capacity, and poor governance reinforce each other, thereby confirming Africa’s peripheral and diminishing role in the world economy”. Today, the weak state remains a major constraint on sustainable development in a number of African countries. Indeed, one of the major challenges is to strengthen the capacity to govern and to develop long-term policies that can improve the well-being of Africans in a transparent and accountable manner.

23. Keeping all of these factors in mind, we have prioritized the codes and standards as discussed below. They have the potential to promote market efficiency, control wasteful spending, consolidate democracy, and encourage private financial flows – all of which are critical aspects of the quest to reduce poverty and enhance sustainable development. These codes and standards have been developed by a number of international organizations through consultative processes that involved the active participation and endorsement by African countries. Thus, the codes and standards are multilateral and genuinely global, as they were agreed by experts from a vast spectrum of economies with different structural characteristics

24. The priority codes and standards on economic and corporate governance, given the perspective we have outlined above, are suggested to be the following:

- Code of Good Practices on Transparency in Monetary and Financial Policies;
- Code of Good Practices on Fiscal Transparency;
- Best Practices for Budget Transparency;
- Guidelines for Public Debt Management;
- Principles of Corporate Governance;
- International Accounting Standards;
- International Standards on Auditing; and the
- Core Principles for Effective Banking Supervision.

25. These codes and standards can be grouped into four main categories, according to the key economic policy objectives that they seek to foster:

- **Promoting sound macro-economic and public financial management and accountability.** To improve macro-economic and public financial management and accountability, African countries would engage in fiscal reforms that contribute to budgetary discipline, equitable public resource use, efficient revenue mobilization, and fiscal transparency. This recognizes the need to restore and maintain macro-economic stability, especially by developing appropriate standards and targets for fiscal policies, and introducing institutional frameworks to achieve them.
- **Protecting the integrity of monetary and financial systems.** The integrity of monetary and financial systems, central in promoting transparency and accountability, includes monetary and financial transparency, independence of central banks, and effective regulatory and supervisory institutions in the monetary and financial sector. This is an important category in its own right but also in the context of fostering the development of capital markets and instilling confidence in African economies as viable places to conduct business.
- **Strengthening accounting and auditing systems.** Orderly and efficient use of public funds is essential for the proper handling of public finances and the effectiveness of the decision-making. Accounting systems should be comprehensive, integrated, and reliable. Each country should have a supreme audit institution whose independence is guaranteed by law. The specific objectives of auditing, include: the proper and effective use of public funds; the development of sound financial management; the proper execution of administrative activities; and the communication of information to public authorities and the general public through the publication of objective reports.
- **Developing an effective corporate governance framework.** A sound corporate governance framework fosters transparency, accountability, efficiency, effectiveness, integrity, and fairness. Devising policy and institutional arrangements to promote these attributes entails creating an effective legal framework that protects

property rights, codifies the rights and obligations of a company, its board, management, shareholders, and other stakeholders. It also requires a regulatory framework that ensures financial disclosure and effective supervisory arrangements for the corporation.

ANNEX: The African Peer Review (APR) Mechanism

1. The APR mechanism that is proposed here builds on the concept of African ownership to allow for action on assessments of economic and corporate governance issues, in African countries, that have been conducted by fellow Africans in a credible manner. A credible APR process would have both an accountability and a broader development perspective. The accountability perspective is derived from the need to demonstrate, first and foremost, that the political commitment and will exists to engage in self-monitoring and to take corrective actions where required. The development perspective is derived from the need to effect systems of good economic and corporate governance to encourage private investment and a climate for enhanced donor flows to stimulate growth and reduce poverty.

2. Ideally, the APR process would allow for the interests of donors and African countries to converge. But even more importantly, a single peer review encompassing both the political and the economic/corporate aspects of governance should be conducted for a given country where required. This would not only be a smooth, efficient, and cost-effective way to go about it but, as previously stated, the nature and quality of economic and corporate governance are also heavily influenced by the nature and quality of political governance. Consequently, it would be a sensible approach to combine the two peer reviews but through the use of two separate tracks. We, therefore, advocate that some consideration be given to this idea.

3. The APR mechanism is an idea whose time has come. It is therefore a diagnostic tool that is designed to provide an assessment of the differences in country performance and diversity with respect to economic and corporate governance. It would also validate, or qualify, any relevant assessments conducted by external partners. As a credible self-monitoring mechanism, it can also serve as a starting point for deliberations with donor agencies rather than relying entirely on assessments conducted by the latter.

4. In addition, the implementation of the APR mechanism can give effect to the need for targeted capacity-building in priority areas. State capacity-building is a critical aspect of creating conditions for development. As stated in the NEPAD framework document (Para. 86), “the state has a major role to play in promoting economic growth and development, and in implementing poverty reduction programs. However, the reality is that many governments lack the capacity to fulfil this role. As a consequence, many countries lack the necessary policy and regulatory frameworks for private sector led growth. They also lack the capacity to implement programs, even when funding is available”.

Objectives of the APR Mechanism

5. The APR mechanism will focus on the key features of economic and corporate governance in the country being reviewed and, in that regard, its primary objectives will be the following:

- To enhance African ownership of the development agenda;
- To monitor and track progress towards agreed NEPAD goals, and codes and standards;
- To identify, evaluate, and disseminate good practices;
- To ensure that policies are based on the best current knowledge and/or the practical experience of peer countries;
- To assess how good practices can be effectively transferred to other African states;
- To use peer persuasion and encouragement to induce the adoption of good practices and adherence to agreed codes and standards; and
- To identify capacity gaps and recommend African and international approaches and possible solutions to address those gaps.

Implementation Modality for the APR Mechanism

The Process

6. The process for the implementation of the APR mechanism will be in three stages. In Stage One, an analysis will be conducted of the development and governance environment in the country to be peer reviewed. Such an analysis will require intensive use of national surveys on issues of good governance. The analysis would also build on on-going research conducted by national, regional, and international institutions. This systematic collection and analysis of data on key governance issues will provide a basis for informed dialogue and a credible assessment. Key issues will be identified for the country, as relevant, including the broad understanding and good background information on the following:

- **Political Representativeness:** to cover issues of political systems and electoral processes, representation, and participation of various stakeholders in decision making,
- **Institutional Effectiveness:** including issues related to the nature and workings of the legislature, judiciary, and executive branches of government, as well as the state of the non-government sector.
- **Economic Management and Corporate Governance:** addressing issues of macroeconomic management, public financial accountability, monetary and financial transparency, accounting and auditing systems and regulatory oversight bodies. As well as issues of capacity, effectiveness and accountability of the

economic decision-making and service delivery systems and processes.

7. Stage Two of the APR process will entail a mission team visiting the country under review. The mission's work here will be significantly informed by the Stage One analysis and will be focused on economic and corporate governance issues with particular emphasis on public financial management and accountability, including the legal and administrative framework for fiscal management, budget formulation and execution, financial reporting, and auditing practices, for example. Although, much of the information and data here will be obtained from government sources, other independent sources of information will also need to be consulted, given the data intensive nature of a peer review process.

8. In this stage Two APR process, mission members will interact with, and interview extensively, the relevant government officials; parliamentarians, including from the opposition; banking and financial sector representatives; private sector representatives; officials of resident missions of regional and international organizations; and representatives of civil society groups, including the media, NGOs, universities, and trade unions, for example.

9. The mission will prepare a report on its findings, a draft of which will be discussed with the government concerned. Those discussions will be designed to ensure the accuracy of information and to offer the government an opportunity to rebut the mission's findings as well as provide its own views on how the identified shortcomings may be addressed. These responses of the government will be integrated into the mission's report.

10. Stage Three, the final stage of the APR process, will involve discussions of the outcomes of a mission and the recommendations regarding the next steps. These discussions will occur in a forum of a Committee of Ministers of Finance and Central Bank Governors. This forum will be convened periodically through the APR Secretariat for this purpose. The deliberations and decisions of this forum will be conveyed to the NEPAD Heads of State and Government Implementation Committee through the NEPAD Steering Committee.

Administrative Arrangements

11. First, it is proposed that the APR mechanism should be managed by, and situated in, a Secretariat that has the technical capacity to undertake the analytical work that underpins the peer review process. Such a Secretariat must necessarily be located in a credible and independent institution that is separate from the political process and NEPAD structures.

12. Second, countries would volunteer to be peer reviewed. The experience elsewhere has shown that pressure for change is generated by public exposure rather than through mandatory actions. However, the Heads of State and

Government Implementation Committee may want to consider whether they should be able to select countries for peer review and under what circumstances such a scenario would be triggered.

13. Third, the members of the peer review mission team, as well as their terms of reference, should be approved by the NEPAD Steering Committee and recommended to the Heads of State and Government Implementation Committee. Such an approved team would be comprised of an eminent African personality and representatives from at least two other countries. Additional members of the team will be provided by the APR Secretariat to enhance technical expertise and ensure the robustness and credibility of the process and its outcomes. **All members of the team should not be citizens of the country to be peer reviewed.**

Conclusion

14. Africans have to take responsibility for improving governance in their countries. To be sure, many of the countries are already addressing governance problems. The APR mechanism outlined here can provide a new form of peer group pressure to help spread this experience. However, the donor community must also display a willingness to provide support where capacity constraints are identified.

15. Understandably, the APR mechanism is a significant innovation, but it will also take time to build up trust amongst the countries for its implementation. This has been the pattern in the OECD where member countries mandatorily assess each other's economic performance and compliance with international commitments. The experience there has also been that pressure for change is generated by public exposure rather than sanctions. As previously stated, the APR mechanism is an idea whose time has come. As a self-monitoring process, it has the potential to track progress and contribute to the development of a transformed relationship with external partners based on mutually agreed performance targets and standards for both donor and recipient, rather than the past model of donor-imposed conditionalities.

16. Mutual accountability is a core aspect of the NEPAD framework. It is a critical dimension of Africans taking responsibility for the continent's destiny while at the same time overcoming the development gap that has widened over centuries of unequal relations. It is also intended to reduce the transaction costs associated with the need to negotiate with, and account separately to, different donors supporting the same project; to eliminate or reduce the tying of aid; and to create an environment of more long-term predictable resource flows, for example.