ABSTRACT

Corporate governance is a group of relations between owners, stockholders and other groups of interest or influence. Actually it is a group of relations between different participants of the corporation business who work on determining then direction and successfulness of the corporation.

Corporate governance is shown through several different mechanisms that enable the management to govern the corporation for the welfare of one or more interested parties. The management is represented as the agent that runs the corporation for the welfare of different principals. Adequate and transparent reporting is one of the most significant internal mechanisms of corporate governance and is very important for the existing and future investors on the market of capital because it is a picture of behavior and work of the management of the corporation.

Through the presentation of previously made financial statements the banks provide information about themselves and their business running to investors, creditors, analysts and other interested parties, i.e. they make their business running transparent. Transparency in financial reporting means insuring the simplicity and easiness of access to information, their accuracy, quality, timing, presentation in clear and simple terms, and all that provides control over debtors and owners discipline, market evaluation of the bank, control of risks, responsibility of managers and bank directors.
The goal of this work is to analyze the use of Internet with the purpose of financial statements and improvement of transparency of financial statements of banks in Bosnia and Herzegovina. Transparency in banking industry is the crucial element of supervising process and efficient market discipline, but it is also one of crucial internal mechanisms of corporate governance. Special attentions will be given to congruency of presented information and the directions of third column of Basel II, with the purpose of ensuring market discipline and EU Directive of Transparency.

JEL classification: G21, M4

Key words: corporate governance, transparency, internal mechanisms of corporate governance, financial statements, Basel II, EU Directive of Transparency

1. INTRODUCTION

In the broadest meaning, corporate governance is a relation between a manager (administration) and investors who invested capital in the corporation. If we observe this in a narrower meaning, corporate governance is the system, which ensures to the owner (investor) that the supreme management, named and set in order to achieve aims of the organization, would accomplish the main accepted obligation, which is making additional capital value for the owners. The setting of the corporate governance should provide all material data concerned with corporation including financial situation, work results, ownership and managing the association in time and precisely.

Transparency in bank industry is an important feature in supervision process and in making efficient market discipline. We can talk about market discipline only when market participants have total access to timely and precise information which enables them to join bank’s activity and to measure risk in bank’s activities and bank financial situation, its risk profile and the managing risk system. Public announcement and supervision information have to promote safety and reliability of bank’s system as well as protect the consumer. Transparency in the states of central and southern east Europe has special place because banks are in instant structural changes in financial department: financial innovations, growing complexity of the business transactions, financial conglomerates, rising consumers’ requests, banking internationalization, exposing to risks. Only the existent and improvements of transparency only can help to prevent financial crisis.
Many companies use Internet today as instrument for business and communications, from online goods orders and services to information assurance for investors, creditors and other interested users. Banks can use the Internet to ensure financial information about their business via corporative web site. Internet can be used to publish the financial performances, financial issues (capital, solvency and liquidity), and exposure to risks, accounting principles, as well as information about corporate bank governance in public.

2. THE TERM OF CORPORATE GOVERNANCE

The term of corporate governance is pretty wide open and there are a lot of approaches, which can help to define it. Corporate governance is linked to corporations in which the ownership is separated from governance and thereby we can define it:

According to OECD definition (Organization for Economic Cooperation and Development) corporate governance includes...set of the relations between management, administration, stockholders and the rest interested groups. Corporate governance also represents the structure inside which the goals of the business are determined as well as funds for achieving those goals and monitoring its business transactions. Good corporate governance should offer proper encouragement for the administration and management in order to achieve goals, which are of great interest for business and stockholders...”

"Corporate governance is relation between different participants while determining direction and efficacy of the corporation. The main participants of this process are the owners of the corporations, management and supervisory committee. The rest of the participants are employees, buyers, suppliers, creditors and wider social community.”

According to Cadbury: corporate governance is managing and controlling of the corporation.”

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6 Dunlop, A.: Corporate Governance and Control, Kogan Page Publisher, 1998, p.3.
To develop effective corporate governance we have to cover three fields: (1) control of the management – where board directors are controlling choice and verifying actions of the headmasters; (2) Reporting the stockholders – revision and including in making important decisions of the owners, and (3) monitoring and valuation of the long – term strategies and business activities valuation.\(^7\)

### 3. MECHANISMS OF THE CORPORATE GOVERNANCE

Corporate governance manifests throughout many different mechanisms, which enables for management to administrate corporation for welfare of one or more interested parties. Management manifests as agent administrating corporation for different principals’ welfare (stockholders and stakeholders).

There is a variety of different mechanisms which ensure corporate governance’s efficiency, as great stockholders, creditors, internal control and supervision systems, external and autonomous auditors, and off course legal sets inside which a corporation operates.

All these mechanisms are put into two main groups: internal and external.\(^8\) Outer (external) mechanisms include: legal set (frame), market influence and competition and minority owner’s interest’s protection. Internal mechanisms in the most cases are: directors committee, motivation politics of the management, ownership concentration, relations with stakeholders and transparency in current financial actions and reporting.

#### 3.1. Transparency as corporate governance mechanism

The fifth internal mechanism is transparency in financial and current business, and it is about adequate and transparent disclosure of relevant information about the business (disclosure – routine notion or term).

Adequate and transparent disclosure is very important for existing and future investors on the capital market, because it brings picture about corporation management behavior and actions. This issue is elaborated in V. OECD’s corporate governance principle (Data disclosure and transparency).

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\(^8\) Tipurić, D.: nadzorni odbor i korporativno upravljanje, Sinergija, Zagreb 2006, p. 56
From V. OECD’s corporate governance principle we can conclude that the corporate governance frame should enable timely and precisely to disclosure all issues important for corporation, including financial situation, results, ownership, and corporate governance.\(^9\)

This principle requests public disclosure, at least once a year, but some countries request periodical disclosure on semi – annual or quarter ground, or even more frequent, if some important events, with influence on corporation are taking place. Corporations often undertake voluntary to disclosure data, which goes even further from minimal requests, and it matches to market requests and needs.

Stockholders and potential investors request for delivery of the sure, comparable, and detailed enough information in order to judge relations within the administration and to make decisions about value, ownership, and votes by virtues of stocks. Insufficient or inexplicit information can endanger market’s functionality; can raise capital’s costs and can lead to unsatisfactory resources distribution.

3.2. Institutional set for financial report transparency in Federation of Bosnia and Herzegovina

The most regulations from the corporate governance in Bosnia and Herzegovina are defined by entity lows. At the state level, at accounting domain and accounting regulations there is a state Low about accounting and audit of Bosnia and Herzegovina\(^10\), which fortifies standards for accounting and audit implementation in Bosnia and Herzegovina. Nevertheless, beside afore-mentioned low at the state level there are entity lows and these are: The low about accounting and audit in Federation of Bosnia and Herzegovina\(^11\) and The low about accounting and revision in Serb Republic.\(^12\)

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\(^10\) Low about accounting and audit of Bosnia and Herzegovina, Official Gazette of Bosnia and Herzegovina, Number 42/04.

\(^11\) Low about accounting and audit of Federation of Bosnia and Herzegovina, Official Gazette of the Federation of Bosnia and Herzegovina, Number 32/05.

\(^12\) Low about accounting and audit of Republic of Srpska, Official Gazette of Republic of Srpska, Number 67/05.
International accounting standards, i.e. International Financial Report Standards are grounds to create native accounting regulations, which onwards regulate all actions concerned with creating financial reports.

Commissions for securities (stocks) in both entities have different obligations for annual reporting. Joint – stock company in both entities are obliged to prepare annual financial reports and reviser reports or supervisory board’s reports for revision. (Federation of Bosnia and Herzegovina) or supervisory and authority board (Republic of Srpska), which are to be presented to main stock’s congress and to be available for stockholders.

Annual financial reports must be the revision and consolidation issue, they are to be delivered to specialized agency FIP in Federation of Bosnia and Herzegovina and AFIP in Serb Republic. Regulations in Serb Republic bind joint – stock companies whose stocks belong to at least one hundred stockholders or at least to one PIF (Privatization investing found) to disclose annual summary financial reports, as well as to publish the report about the most important events and activities in daily newspapers. Joint – stock companies with marketable securities (practically all of them) also have to deliver annual reports about business activities to their Commission for securities and to stock market including summary financial reports, revision report as well as report about the latest activities and future plans.

The low about securities in both entities are obliged by joint – stock companies to prepare semi – annual reports about activities in business. They contain the main financial data, which were not the revision issue. Investment funds in Federation of Bosnia and Herzegovina are bind to prepare quarterly reports while other joint-stock companies in Bosnia and Herzegovina are not. Apart from few, reports are simple. Less than a half of joint – stock companies in both entities disclose reports or deliver them to their Commission for securities or stock market.

3.3. Transparency and bank financial reporting

The market can be efficient only on the grounds of proper, useful and timely available information. Actually, in bank business activities it is necessary to provide information clarity from financial reports, to make the way they are published more simple as well as to enable debtors and owners discipline supervision, bank market valuation and to provide manager’s responsibility.
This is possible to achieve with implementation of accounting standards and behavior standards. Banks within European Union whose securities are used for trade on financial market have been obliged to implement International Accounting Standards and thus raise publicity access to information with regard to possibilities offered by national accounting standards. However, European banks rating on American stock markets must implement International Financial Report Standards, because with their implementation they achieve similar level of transparency as U.S. GAAP standards.

Financial reports composed according to standards must give precise and fair view on property, obligations, financial position and benefit or waste on consolatory level.

Transparency, efficiency and integrating financial market would contribute in achieving unique community market and would contribute to its faster growth, as well as would contribute to opening new workplaces, better allocation of capital as the result of costs reduction. Transparency provides that investor feels safety and it allows more simple performances and bank property valuations, but for other participants at financial market too. Actually transparency must achieve two goals: investor’s protection (creditors, depositories) and to enable market efficacy. Transparency represents some way of the bank’s self – regulation.

4. BANKS TRANSPARENCY IN BOSNIA AND HERZEGOVINA

Bank management in Bosnia and Herzegovina according to existing lows about accounting is responsible to enable financial reports prepared for each year according to International Financial Report Standards which give truthful and fair value for the period given. Annual banks report includes:

- Responsibility for financial reports
- Autonomous reviser’s report
- Balance sheet
- Success balance
- Report about cash flew
- Report about changes in share capital
- Notes about financial reports
In 2006 we studied thirty three banks in bank system of Bosnia and Herzegovina, and we fortified those twenty eight banks has an Internet site, or eighty five percent, while five among banks has not internet connection or it is in reconstruction. At this eighty five percent of banks web pages offer financial information, but timely publications vary. From this pattern seventy six percent of banks have financial reports published on the Internet i.e. they have developed Internet financial reporting. Annual financial reports have been published on the Internet.

In 2007 we studied 32 banks in Bosnia and Herzegovina. All of them, i.e. 100% had internet page and all of them had financial reports available, but the way reports were published and the way they were shaped vary, these two segments were not standardized. There are corporative reports from wide ones, which are standardized for banks’ centrals to those with contracted financial reports with copy of the reversionary judgment. It could be said; the ways of reporting were not standardized. Just five banks had reports about business actions in 5-year period, which was ordered by EU directive about transparency.

In 2008 all banks had Internet pages, but till the time this work was done (1st of March 2009) neither of them had reports published.

However we have to consider interest of some banks for minor or more indigent transparency for many reasons: time assurance institute, precise and detailed accounting system, resources for reporting function, reports composed according to international standards and revised by external reviser, and for all this costs are high, especially for smaller banks.13

In order to advance transparency and to reach higher transparency level necessary for business action in globalized financial world we need to adjust national legislative and practice to the guidelines of EU Directive transparency the third Basel post.

5. TRANSPARENCY DIRECTIVE

Where bank transparency is concerned, primarily monitoring the area in euro integrations context and approaching to euro zone countries Transparency Directive 2001/34/EC i 2004/109/EC could not be avoided. Directive purpose is transparency request harmonization, i.e. establishing request for public reporting current

and periodical information for the entities whose stocks are traded on the EU markets. Transparency Directive regulates the deadlines for publishing certain types of publications, and its implementation has started since the end of 2006 in national euro zone lows, whereas for implementation twenty-four months are needed.

The main Transparency Directive features are:\textsuperscript{14}

- Common deadlines for publishing – four months after the reporting period is over – annual financial report and two months for temporary financial reports.
- Annual reports must contain: revised financial reports, manager’s report
- Publications must be available for publicity at least for five years
- Semi-annual financial report, according to International Accounting Standards 34 must contain added manager’s report
- Temporary managers’ reports (process review and business performances reviews and position as well as main risk factors description and incertitude to which management is confronted) for eminent action in first and third quarter
- Obligation to publish reports on the Internet
- Ad hoc reporting harmonization

In order to carry away obstacles and to introduce effective new transparency requests in community special control of national competent bodies is needed for directive to enable timely available information. Financial market participants are obliged to translate all current and periodic information in all languages spoken in countries members in whom their actions are traded.

6. BANK TRANSPARENCY AND MARKET DISCIPLINE

Market discipline, as the third post of the New Basel standard has its purpose to put together requests which have become banks’ issues in the first post (minimal capital adequacy) and those from second post (supervisory control over banks). This Basel’s standard post determines big influence of national supervisor over bank in order to work with effectiveness, fiducially, and with certain amount of safety. Guided by this, the Basel committee for bank supervision made number of re-

quests to enable market participants to have access to key information about bank’s actions.

Establishing market discipline it is attempted to enable for every single participant on the market to dispose equally with information about bank, which enables better and easier decisions making. That’s the reason why Basel II puts upon adoption of informing public politicks as a need which is to be adopted by the administration of every bank, and with in it is defined information mould and volume which will be available for publicity and frequency of their publishing.15

6.1. Financial performances
Market participants and supervisors need information about bank’s financial performances. Particularly important is to publish information:

- Bank’s profitability and profit variability to make easier judgment about potential change in financial position and possibilities of deposit and commitments repayment, cash flow
- Incomes and costs reviews in order to fortify wage quality, to fortify reasons for bank profitability changes, netto interest margin, relation between costs and interests
- Financial contribution review of different bank’s activities and geographical areas on financial performances
- Managers’ reports about events which effected current and would effect future financial bank performances

6.2. Financial position
Information about bank financial position is important to predict bank’s abilities in identifying obligations and financial obligations. Information are published about:

- property mould and amount, obligations, capital including both maturity structure and repayment plan useful for liquidity valuation, bank solvent and financial power
- fees and provision by losses and the way they are formed, ability to manage the losses is represented through this

• active and passive structures in off – balanced record
• regulatory capital and stockholder’s capital in order to get information about bank’s ability to absorb future potential profits and their future growing
• property mould and amount concerned with collaterals

6.3. Strategies and practices in risk governance

The public needs to have ensured information about strategies and practices governance and risk control. Information’s, which needed to be published, are: management risk psychology, politics and methodology; risk resources; method of governance and controlling the risks; using derivates in risk governance.

6.4. Exposure to risk

Market participants and supervisors are to be delivered qualitative and quantitative information about: exposure to risk including governance strategy and efficacy governance strategy; risk profile i.e. risks in balance positions and off – balanced record at the current moment as well as bank’s appetite for taking over the risks; credit risk, market risk, interest risk, exchange rate and liquidity risk;

Information published in a due time would guide to a better market discipline.

7. CONCLUSION

Market works well when identifies financial institution in risk, in, otherwise healthy financial system – as black sheep among white sheep. That’s the reason why it’s the key thing developing and advancing transparency in superficial financial systems as financial systems in countries of the southern east Europe. As long as there are information about financial condition in business activities the stocks price and conditions for getting onto debt will maintain bank risk. In order to avoid problems in business actions and bank crisis we must close “informatics’ gap” as well as to give information to market participants both to identify financial performances and positions and to identify financial institution risk profile.

For transparent system in providing financial reports and corporate governance improving it is necessarily to follow the accounting and revision mode in a persistent ways, to introduce standard shape for annual report, to strengthen directly information publishing via central records, adjust the Low about securities as well as other lows.
Also, we have to endure in publishing information about important indirect ownership according to EU transparency directive, we have to improve approach to the information about companies, including online court register and web portals, integrated interface which should cover Sarajevo’s stock market as well as Banja Luka’s stock market and to introduce “a window” for informing about the companies.

Higher reporting transparency contributes to a higher corporate governance quality, strengthen confidence among investors, developing financial market, better identification of different institutions and managing financial crises, all these are extremely important elements in social – economics conditions of Bosnia and Herzegovina for long – term stability and development.

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