THE OECD'S RECOMMENDATIONS ON CORPORATE GOVERNANCE

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BETTER POLICIES FOR BETTER LIVES

The OECD‘s main recommendations on corporate governance

- The OECD‘s Corporate Governance Committee oversees the Principles of Corporate Governance and the Guidelines on CG of SOEs
- Includes 37 OECD Member countries plus participation of G20/FSB Members

<u>Overarching objective of the Corporate Governance Committee</u>:

- To contribute to *economic efficiency*, *sustainable growth* and *financial stability* by improving corporate governance policies and supporting good corporate practices.

The G20/OECD Principles of Corporate Governance

- Originally issued in 1999
- International benchmark for corporate governance
- One of the Financial Stability Board's Key Standards for Sound Financial Systems, endorsed by G20
- Implementation assessed and promoted through World Bank and OECD accession reviews, FSB and thematic peer reviews
- Revised in 2004 and 2015
- Following COVID-19 crisis, potential demand to assess whether new revisions and recommendations will be needed.

The Principles' main chapters

I. Ensuring the basis of an effective corporate governance framework
II. The rights and equitable treatment of shareholders and key ownership functions
III. Institutional investors, stock markets, and other intermediaries
IV. The role of stakeholders in corporate governance
V. Disclosure and transparency
VI. The responsibilities of the board

Supporting Implementation of the Principles: OECD thematic peer reviews

- "*The Corporate Governance Lessons from the Financial Crisis*" (OECD, 2010) provided key lessons on remuneration, risk management, board practices and exercise of shareholder rights. This led to thematic peer reviews to assess and promote implementation:

1. Board Practices: Incentives and governing risks
2. The Role of Institutional Investors in Promoting Good Corporate Governance
3. Related Party Transactions and Minority Shareholder Rights
4. Board Nomination and Election
5. Supervision and Enforcement
6. Risk Management and Corporate Governance
7. Proportionality and Flexibility in Corporate Governance
8. Duties and Responsibilities of Boards in Company Groups

Global trends and challenges to CG frameworks

- Decrease in public listings, going private
  - LT trends in OECD countries
- Growth of intermediaries
  - Delegation of monitoring tasks to asset managers and proxy advisors
- Indexing, ETFs, Short-termism, high-frequency trading
  - Reduced incentives for monitoring and ownership engagement
- Role of stock exchanges
  - Profit-maximising
  - Reduced focus on attracting IPOs?
- Rise (and volatility) of emerging markets:
  - Concentrated or state ownership
  - Equity gap/dependence on bank finance

Key issues in the Principles of CG

I. Ensuring the basis of an effective corporate governance framework
   - Increased emphasis on supervision & enforcement (public & private)
   - Governance of regulators
   - Changing role of stock markets
   - International cooperation/MoUs

Key issues in the Principles of CG

II. The rights and equitable treatment of shareholders and key ownership functions

- Includes various provisions to better reflect increased shareholder rights since 2004, such as:
  - Say-on-pay
  - Electronic voting
  - Related-party transactions

Key issues in the Principles of CG

III. Institutional investors, stock markets, and other intermediaries

- New chapter: role of incentives in the investment chain for corporate governance
- Regulation versus stewardship codes
- Disclosure of fee structures, conflicts of interest
- Multiple stock market listings
- Proxy advisors

IV. The role of stakeholders in corporate governance

- Reference to international conventions and norms recognising the rights of employees to information, consultation and negotiation
- Extension of whistleblowing provisions to the competent public authorities and reference to National Contact Points

Key issues in the Principles of CG

V. Disclosure and transparency

- Internationally recognised accounting standards
- Non-financial reporting
- Related-party transactions
- CEO/Chair responsibilities
- Independent audit regulators

VI. The responsibilities of the board

- Tax planning strategies
- Risk management system
- References to Say-on-pay, malus and claw-back
- Audit and other board committees
- Internal audit function
- Direct board reporting on risk
- Board evaluation & training, diversity

The COVID-19 crisis and the role of corporate governance policy

- The COVID-19 crisis has made it difficult for many companies to meet legal and regulatory requirements, such as the organisation of annual shareholders' meetings and disclosure of financial statements.
- In response, governments have taken steps to adjust certain key corporate governance requirements.
- The crisis has also highlighted a number of issues that may call for an adaption of corporate governance policies and practices in the post-COVID era. These include:
  - Means to mitigate excessive systemic risk-taking in the non-financial corporate sector
  - Duties and responsibilities of boards in times of crisis
  - The management of ESG risks
  - Provisions with respect to the concentration of corporate ownership and company groups

Duties and responsibilities of boards in times of crisis

- Since the onset of the pandemic, corporate boards have been under intense pressure due to the uncertainty concerning the health crisis and consequent changes in the regulatory landscape.
- In some cases, shareholders have sued companies and directors for not properly disclosing pandemic-related risks and their impact.
- Common issues have been **inaccurate or misleading disclosures, stock price manipulation, insider trading, and non-compliance with emerging health regulations.**
- In addition, boards have been subject to challenges in several other areas, including **executive remuneration, digital security and insolvency.**

The management of environmental, social and governance risks

- The COVID-19 pandemic has brought increased attention to the importance of identifying systemic risks and unexpected shocks.
- At the company level, there is a need for **new types of expertise**, better analytical tools, and novel internal policies and practices specifically **tailored to assessing the company's ESG risks**.
- At the market level, **material information** related to ESG risks should be disclosed to the public.
- Need for principles that underpin the consistency, comparability and verifiability of ESG-related disclosures.

About the *OECD Guidelines on Corporate Governance of SOEs*

- ***An OECD instrument and internationally-agreed benchmark***. Internationally-agreed benchmark to assess and improve the way state exercises ownership in SOEs. All OECD countries must associate themselves with the recommendations laid down in the *SOE Guidelines*. Newcomers to OECD must demonstrate that they can credibly do so.

- ***Addressed to the SOE ownership***. The *SOE Guidelines* make recommendations to policy makers and public officials responsible for exercising the ownership of enterprises.

- ***Non-binding***. No government or SOE is in any given situation legally obliged to follow the *SOE Guidelines*.

- ***Not limited to OECD members***. Any country can, following a review of its national SOE sector, become an adherent to the *SOE Guidelines* and participate fully in OECD's work on SOEs.

The *SOE Guidelines* embody a shared vision

- **The general public is the ultimate owner of SOEs.** The *SOE Guidelines* are based on, and complementary to, the *OECD Principles of Corporate Governance*, which apply to stock exchange-listed companies. The idea is that SOEs should be as accountable to the general public as listed enterprises and the general public should be considered as their shareholder.

- **Concrete recommendations.** On how to manage ownership responsibilities, thus helping to make SOEs more competitive, efficient and transparent. Good practices on the legal and regulatory framework for SOEs, the professionalisation of the state ownership function and the corporate governance arrangements of SOEs.

- **Setting a high level of aspiration.** The *SOE Guidelines* establish a high bar for good practices. They are designed to serve as a lodestar for reform – not establish minimum standards. Not many countries have fully implemented the *SOE Guidelines*, but ongoing SOE reform is almost always consistent with their standards.

The rationale for the SOE Guidelines

Why is there a need for SOE Guidelines?

- In some OECD countries, and most emerging economies, the state is the largest single enterprise owner. Privatisation is often not an option.
- Too often SOEs display major governance failures in the form of unclear objectives, excessive politicisation, weak accountability, as well as outright corruption.
- Governance failures can deter investment and raise red flags regarding the costs and risks associated with doing business, especially if weak rule of law.
- Corporate inefficiencies have major fiscal, macroeconomic and structural impacts. SOEs prevalent in key sectors with important impact on competitiveness and impact on day-to-day lives of citizens (public service).

Directrices de la OCDE sobre el Gobierno Corporativo de las Empresas Públicas

1. Razones que justifican la propiedad pública
2. El papel del Estado como propietario
3. Las empresas públicas en el mercado
4. Tratamiento equitativo de los accionistas y otros inversores
5. Relaciones con los actores interesados y responsabilidad empresarial
6. Publicidad y transparencia
7. Responsabilidades de los consejos de administración de empresas públicas

The main priorities of the SOE Guidelines

- **A rules-based environment**. SOEs should be subject to the same rules and regulations as other enterprises. They should compete on a level playing field with private enterprises and not distort competition.
- **Reinforcing the ownership function.** The state administration should exercise SOE ownership on a whole-of-government basis. The state ownership function should be separate from the regulatory function to avoid conflicts of interest.
- **Equitable treatment of shareholders**. The state should not have any undue advantages over other investors in SOEs.
- **Transparency and disclosure.** SOEs' objectives and performance should be disclosed and reviewed.
- **Stakeholder relationship.** SOEs and their owners should treat employees, creditors and affected communities fairly and equitably.
- **Boards of directors**. The boards are the highest decision-making bodies within the SOEs. They should exercise their powers free of political interference.

The OECD "model" for SOE ownership and corporate governance

- The ownership of SOEs should be separated from regulation
- Each ownership decision should be taken at the appropriate level

Government	• Sets ownership policy • Coordinates at cabinet level
Ownership function	• Defines objectives for individual SOEs • Monitors performance
SOE board	• Approves strategy • Monitors management
Management	• Runs the company

Independent regulation

The Guidelines are fully relevant for Latin America

- Six Latin American countries have undertaken OECD reviews based on the SOE Guidelines (Argentina, Brazil, Chile, Colombia, Costa Rica, Mexico).
- Numerous reforms achieved in these countries to implement the SOE Guidelines' recommendations, strengthening ownership co-ordination and removing politicians from SOE boards.
- These and many other countries (Ecuador, Paraguay, Peru, Uruguay) are active in the OECD's Latin American Network on Corporate Governance of State-Owned Enterprises' annual meetings.
- The Guidelines are available on OECD web site in Spanish at https://www.oecd.org/corporate/guidelines-corporate-governance-soes.htm .

Resources

THANK YOU!

For more information on OECD work on corporate governance in both the private sector and state-owned enterprises, please visit:

https://www.oecd.org/corporate/