

Russian boards: selection, nomination and election

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Foreword



The composition of the board of directors continues to be at the heart of corporate governance discussions in Russia. Attention is centered around the balance on the board, primarily in terms of independence and professionalism. To ensure that the board has the appropriate range of independence, experience, knowledge and skills, an effective director selection, nomination and election process is vital.

This survey was prepared for the OECD Russia Corporate Governance Roundtable (25-26 October in Moscow). It looks at director selection, nomination and election procedures in place in Russian joint stock companies (primarily, public ones) as well as how the role of board of directors¹ and, in particular, independent directors, is evolving. To do this, we've sought the views of over 70 board members representing over 200 Russian joint stock companies. Inter alia, we have interviewed several outstanding representatives of Russian boards, including independent and senior independent directors, non-executive directors, executives, chairpersons of boards and board committees.

To provide a detailed analysis, we've supplemented the findings of our survey with data collected from annual reports and other public information sources of the top 50 public² Russian companies. The vast majority of the 50 companies on the panel are listed in Russia and/or overseas. At the same time, these companies occupy top positions in the Expert-400 rating.³ In addition, we included in the survey several large Russian companies de jure registered overseas. However, we excluded from the panel some of Russia's largest companies if they fail to meet high corporate governance standards and/or have a poor record of disclosing their corporate governance practices. We have studied the companies' in-house charters, policies and procedures and looked at how they comply with these in practice (as far as such data are publicly disclosed).

¹ For the purposes of this survey, "boards of directors" refers to boards of directors and supervisory boards of joint stock companies.

² For the purposes of this survey, the term "public company" refers to an open joint stock company that offers its securities for sale to the general public through a stock exchange.

³ Expert-400 is a ranking of the 400 largest Russian companies in terms of revenues and 200 largest Russian companies in terms of capitalisation and compiled annually by Expert RA Rating Agency (<http://raexpert.org/ratings/expert400/>).



In our survey, when analysing Russian companies' compliance with corporate governance standards and requirements (either set locally or recognised internationally), we refer to the Federal Law No. 208-FZ of 26 December 1995 "On Joint Stock Companies" (hereinafter – "Law on JSC"); the Code of Corporate Conduct approved by the Session of the Government of the Russian Federation on 28 November 2001 (minutes No. 49), which was recommended by the Federal Commission for the Securities Market in 2002 (hereinafter – "Russian Code"); the Moscow Exchange listing requirements as stipulated in the FSFM Regulations on the Activity for Trade Organisations on the Securities Market (hereinafter – "Moscow Exchange listing rules"); the OECD Principles of Corporate Governance, 2004 (hereinafter – "OECD Principles"); and the UK Corporate Governance Code, 2010 (hereinafter – "UK Code"). We think it is worth referring to the latter due to the fact that many large Russian companies have their securities traded on the London Stock Exchange and are subsequently required to comply with the UK Code's provisions (or explain non-compliance).

Also, for purposes of benchmarking against international best practices, we refer to the PwC UK Non-executive Director Survey, 2011 (hereinafter – "UK NED Survey") and the Spencer Stuart Governance Survey of S&P 500 boards, 2011 (hereinafter – "2011 Spencer Stuart Board Index").

We thank all the participants who responded for their contribution to this survey and the insights they have provided into the director selection, nomination and election issues that they face in the boardroom. If you would like to discuss any of the matters raised in this survey, please feel free to contact us.

Executive summary



The director selection, nomination and election practices in Russia differ significantly from international best practice so far, but in recent years we have noted that both the professional community as well as the state and regulators have begun to pay close attention to these and related issues.

Our survey shows that the role of the board of directors and, in particular, independent directors, has been evolving to entail more engagement and responsibilities. Almost half of our respondents (and, inter alia, most board and nomination committee chairs) consider that their role has become more attractive over the last few years, primarily due to its challenging nature, the growing professionalism of boards and, above all, the ability to add value. On the other hand, the evolving role inevitably poses higher requirements to board candidates and to the board as a whole, which puts an even sharper focus on board composition and director selection, nomination and election.

Board composition

- On average, the boards of directors of the top 50 Russian public companies have 10 members, including four independent directors
- None of the companies surveyed have the roles of board chairperson and chief executive occupied by the same individual, which is in line with Russian legal requirements
- 20% of the top 50 Russian public companies have an independent board chairperson and 10% have a senior (lead) independent director
- Across all board member roles of the top 50 Russian public companies, only 7% are held by females; 43% of our respondents reported that their boards had no females at all, while 44% consider that broadening the diversity of the board would have a positive impact on its effectiveness



Selection, nomination and election

- 94% of the top 50 Russian public companies have a nomination committee (or equivalent body); 70% of these committees have an independent chairman and 26% are fully independent
- 15% of respondents claim that their companies employ external consultants in the director search and selection process
- 94% of companies set formal requirements or recommendations related to board candidates' experience, skills and knowledge
- 37% of our respondents reported that the companies' in-house procedures for board candidate selection were not formalised and/or not transparent
- According to our respondents, most boards primarily target retired and active top executives when searching for independent directors

Board development, performance evaluation and succession planning

- 92% of our respondents believe board performance evaluations are useful and 65% claim their boards carry out their performance evaluation annually
- According to our respondents, 20% of the boards bring in a third party when conducting their performance evaluation and 64% disclose the evaluation results
- According to our respondents, technical reading and attending seminars and conferences are the most popular tools for directors to stay up-to-date with regulatory, technical and other developments
- In all the surveyed companies, board directors are elected for terms of one year or less, in conjunction with Russian legal requirements

Director perspective

- When accepting a directorship, our respondents primarily consider a company's reputation and the possibility of adding value and making a real difference, as well as the business strategy and financial strength of a company
- 48% of our respondents (and most of the board and nomination committee chairs) believe that their role has become more attractive over the last few years

10.3

Boards of directors of the top 50 Russian public companies have 10.3 members on average

1. Board composition and independence

1.1. Board size

The UK Code states that “the board should be of sufficient size that the requirements of the business can be met and that changes to the board’s composition and that of its committees can be managed without undue disruption, and should not be so large as to be unwieldy.”⁴ The optimal board size will obviously vary depending on the nature of an individual company’s business and can be expected to change over time as the company matures.

The Law on JSC states that “the quantitative composition of a company’s board of directors shall be determined by the charter of the company or by decision of a general meeting of shareholders but may not be less than five members.” Further, according to the law, for a company with more than one thousand holders of voting stock, the quantitative composition of the board of directors may not be less than seven members and for a company with more than ten thousand holders of common and other voting stock, not less than nine members.⁵ Yet, the law does not stipulate a maximum number of board members.

In addition, the Russian Code of Corporate Conduct provides for general principles of determining the number of board members: “Companies should primarily seek a number that will

enable the board of directors to hold productive and constructive discussions, make prompt and rational decisions, and efficiently organise the work of its committees.”⁶

Our survey shows that, in practice, 90% of the top 50 Russian public companies set limits on the number of board members in their in-house documents (e.g. charters, articles of association, terms of reference): among them, 64% set the exact number of board members, another 8% set the interval (those registered overseas), 16% set only the minimum, and one company sets only the maximum number of directors.

In practice, boards of directors of these companies have 10.3 members on average (minimum five and maximum 18). 80% of the companies have seven to 11 directors and close to 20% of the companies have over 11 board members.

These are compatible with the results of our UK NED Survey which indicates that FTSE 100 companies have 11 board directors on average, while FTSE 250 companies have eight directors.⁷ Further, according to the 2011 Spencer Stuart Board Index⁸, the average size of S&P 500 boards remains approximately at 10.7 directors over recent years (with a minimum of five and maximum of 32 directors in 2011).

⁴ UK Code, Section B, B.1.

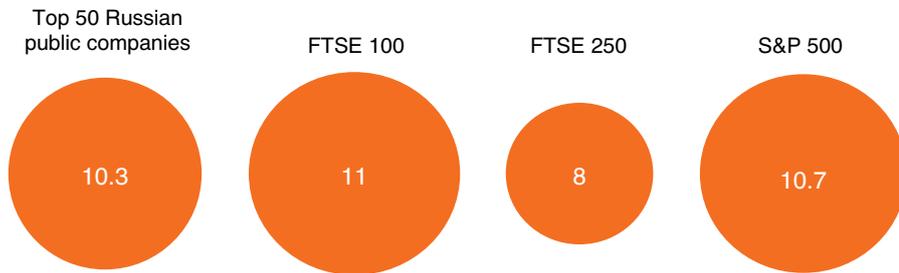
⁵ Law on JSC, Chapter VIII, Art. 66.

⁶ Russian Code, Chapter III, Par. 2.1.4.

⁷ UK NED Survey, p.11.

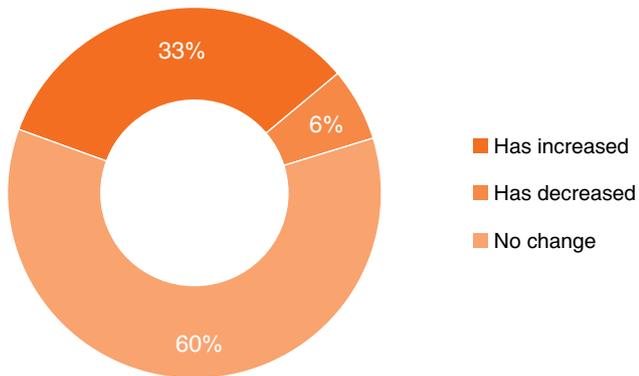
⁸ 2011 Spencer Stuart Board Index, p.14.

The average number of board members:



According to most respondents, their board size had not changed over the last three years, 33% noted an increase in the board size and only 6% reported a decrease.

Over the last three years, the board size:



“In our opinion, we are moving towards relieving the board of directors from having to deal with technical or purely executive issues in order to have directors more involved in global and strategic issues.”

Bella Zlatkis

“The board structure is also about the shareholding structure because if a company belongs to a small number of owners, then inevitably you will get most of the directors representing the interests of certain shareholders. However, independent directors should of course represent the interests of all shareholders, especially minority shareholders, and this is our main contribution. I think the more independent directors a board has, the better. It is important that they have complimentary skills and that they realise their job is to challenge management strategically and not be passive about performing their duties.”

David Hexter

“We have reached a balance between the interests of the controlling shareholder and an independent, unbiased approach which ensures open and sometimes critical review of issues. It is also a matter of the culture of the board and the company as a whole, a matter of taking a professional and strategic approach to the board's work.”

Dominique Fache

“Different companies have different situations. For the majority of state-owned companies for whom the concept of independent directors is relatively new, having independent directors in and of itself will likely not be able to guarantee that they can ensure a balance. Nevertheless, the role of independent directors, as well as committee leaders, has no doubt expanded over the last few years.”

Anna Belova

1.2. Board independence

Principle VI of the OECD Principles states that “where board decisions may affect different shareholder groups differently, the board should treat all shareholders fairly. In carrying out its duties, the board should not be viewed or act as an assembly of individual representatives for various constituencies. While specific board members may indeed be nominated or elected by certain shareholders (and sometimes contested by others) it is an important feature of the board's work that board members, when they assume their responsibilities, carry out their duties in an even-handed manner with respect to all shareholders.”⁹ In this view, the board should be able to exercise objective independent judgment on corporate affairs.

Since first recommended by the Cadbury Report in 1992, it is now widely accepted that an effective board is one that comprises “a combination of executive directors, with their intimate knowledge of the business, and of outside, non-executive directors,

who can bring a broader view to the company's activities.”¹⁰

Under the Law on JSC, executive directors are defined as “members of the board of directors concurrently holding positions as members of the managerial board (a collective executive body),” and they may not make up more than one quarter of the company's board of directors.

At the same time, limiting the share of executive directors on the board does not in itself guarantee adequate protection of shareholder interests. Efficient performance by the board of directors requires that some of its members are independent directors.¹¹

The Law on JSC does not set any requirements for the number of independent directors on the board. Whereas the Russian Code recommends that, “in order to enable independent directors to influence actively the decision-making process and ensure that the board of directors considers the widest possible spectrum of opinions on matters being discussed, their number

should comprise at least one-fourth of the total number of board members. In any event, it is recommended that the company's charter should provide that the board of directors include at least three independent directors.”¹²

The following requirements on the number of independent directors on the board are provided for by the Moscow Exchange listing rules: at least three independent directors for list A1 and A2, and at least one director for lower lists.¹³

By comparison, the UK Code sets out that, “except for smaller companies¹⁴, at least half the board, excluding the chairperson, should comprise non-executive directors determined by the board to be independent. A smaller company should have at least two independent non-executive directors.”¹⁵

Also, companies' own voluntary corporate governance codes, policies and regulations may set up either general recommendations or specific numbers and percentages of independent members on boards.

⁹ OECD Principles of Corporate Governance, 2004, Principle VI.

¹⁰ Report of the Committee on the Financial Aspects of Corporate Governance and Gee and Co. Ltd., 1992, Par. 4.1.

¹¹ Law on JSC, Chapter VIII, Art. 66.

¹² Russian Code, Chapter III, Par. 2.2.3.

¹³ As stipulated in the FSFM Regulations on the Activity for Trade Organisation on the Securities Market, Appendices 1, 3, 4.

¹⁴ A smaller company is one that is below the FTSE 350 throughout the year immediately prior to the reporting year.

¹⁵ UK Code, Section B, Par. B.1.2.

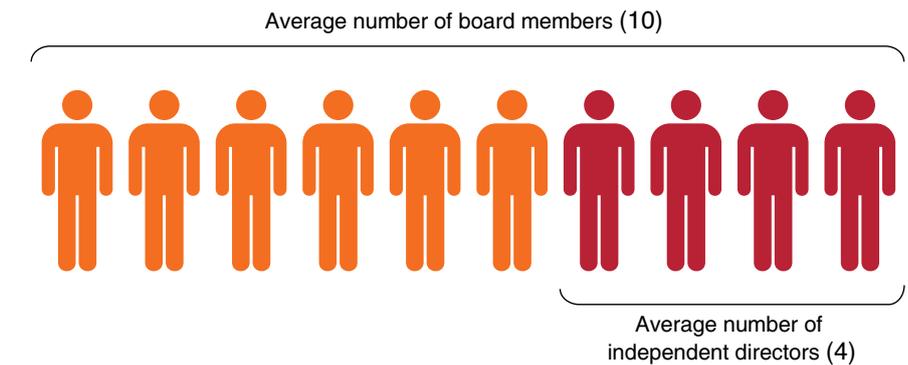
39%

On average, independent directors make up 39% of the board members of the top 50 Russian public companies

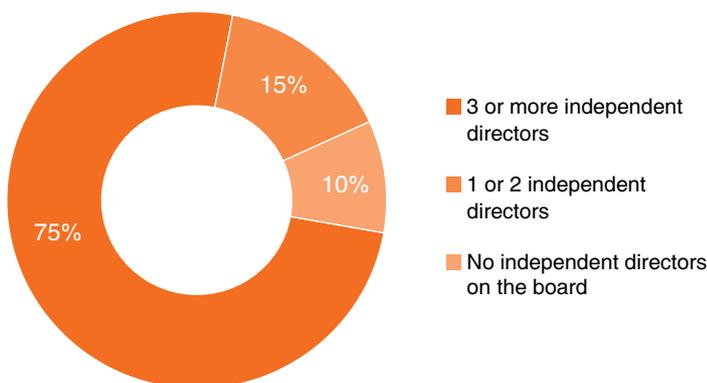
Most of the top 50 Russian public companies have set the minimum number (or share) of independent directors on their boards, which varies from one to five. Only 4% of companies require that at least half the board or its majority should be independent directors.

In practice, on boards of the top 50 Russian public companies, there are from one to nine independent directors who make up 9% to 86% of the board members. On average, roughly four out of ten board members of these companies are independent directors. To compare with the 2011 Spencer Stuart Board Index: overall, independent directors make up 84% of all board members of S&P 500 companies.¹⁶

Our survey shows that the practice of appointing independent directors to the board is widespread among Russian companies. According to our respondents, independent directors make up 39% of their boards on average. 75% of the companies have



three or more independent directors on their boards (in accordance with the independence criteria applied by each particular company). On the other hand, 10% of the respondents reported there were no independent directors at all on their boards.



¹⁶ 2011 Spencer Stuart Board Index, p.14.



Independence criteria

The law on JSC provides a definition of “independent director”: “An ‘independent director’ means a member of the board of directors (supervisory board) of a company who, in the year preceding the year of the decision, is not and had not been:

- a person performing the functions of the company’s sole executive body, in particular, its executive, member of the collective executive body, a person occupying positions in the managerial bodies of the management organisation;
- a person whose spouse, parents, children, siblings and half brothers and sisters, step-parents and step-children occupy positions in the company’s management bodies listed above, the management organisation or are managers of the company;
- an affiliated person of the company, except for a member of the company’s board of directors (supervisory board).¹⁷

These criteria do not appear to be sufficient due to the loose definition of “affiliated persons” in the legislation.

The Russian Code of Corporate Conduct states that, “in defining eligibility criteria for independent directors, the company should consider their ability to make independent judgments. This means that there should be no factors capable of affecting their position.

An independent director should be a director who:

- over the last three years has not been an officer (manager) or employee of the company, or an officer or employee of the company’s managing organisation;

- is not an officer of another company in which any of the company’s officers is a member of the appointments and remuneration committee of the board of directors;
- is not an affiliated person of an officer (manager) of the company (officer of the company’s managing organisation);
- is not an affiliated person of the company or an affiliated person of such affiliated persons;
- is not bound by contractual relations with the company, whereby the person may acquire property (receive monies) with a value in excess of 10 per cent of such person’s aggregate annual income, other than through receipt of remuneration for participation in the operations of the board of directors;
- is not a major business partner of the company (a business partner with an annual value of transactions with the company in excess of 10 per cent of the asset value of the company); and
- is not a representative of the government.

No director may be deemed to be independent if he has acted in the capacity of a member of the board of directors of the company for seven years.¹⁸

These criteria are reflected (with minor modifications) in the Moscow Exchange listing rules.¹⁹

Yet, these criteria to define an independent director have been widely criticised for lack of scope and detail.

¹⁷ Law on JSC, Chapter XI, Art. 83.

¹⁸ Russian Code, Chapter III, Par. 2.2.2.

¹⁹ As stipulated in the Regulations on the Activity for Trade Organization on the Securities Market approved by the Order of FFMS of Russia № 07-102/pz-n on 9 October 2007, Appendix 1.

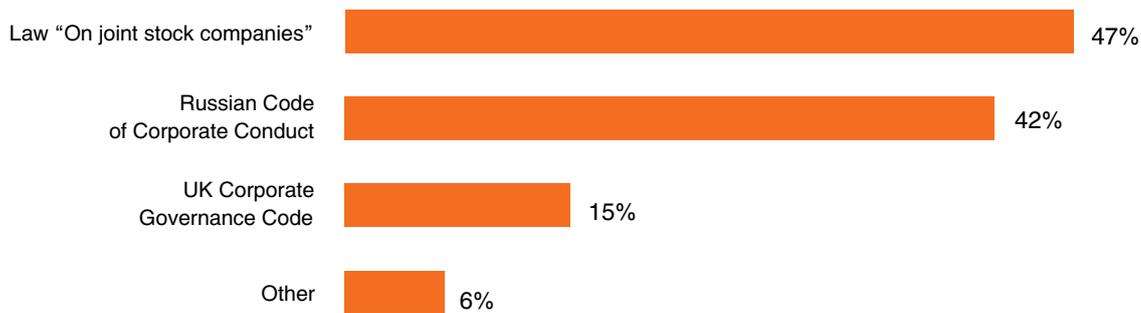
47%

47% of our respondents reported their boards applied the minimum independence criteria set out in the Law on JSC

70% of the top 50 Russian public companies spell out in their in-house documents the director independence criteria applied by their boards.

According to our respondents, when determining whether or not a director is independent, almost half of the companies apply only the minimum independence criteria set out in the Law on JSC. With this, 42% of companies use the criteria set out in the Russian Code and 15% (primarily, companies listed overseas) use those set out in the UK Code.²⁰

What director independence criteria does your board apply when determining whether or not a director is independent?



²⁰ UK Code, Section B, B.1.1.

“Various code definitions of independence do not actually describe the human qualities you are looking for. I think the heart of the issue is independence of spirit, which means that you bring an objectivity, that you have a combination of capability as independent director, experience and self-confidence to enter into any board debate, to test, challenge and, in the end, support the conclusion of the board, provided that you are satisfied with the direction that things are going.”

Sir Robert Margetts

“An independent director should be able to roll with the punches and stand their ground. They should have a very strong, professional personality. Of course, work experience is important, including experience as a top manager as well as a strategist and specialist, who has a good idea of the procedures involved with planning and risk management.”

Anna Belova

“An independent director needs to be professional, industrious, meticulous in his work and responsible. I would also like to emphasise such personal qualities as communication skills, diplomacy, and the ability to openly stand one's ground when making arguments.”

Irina Shitkina

“The key quality of an independent director is actually the ability to challenge individuals and ideas, even though it may sometimes be an uncomfortable process. You have to walk a very thin line between a critical approach and its implementation in such a way which is not considered aggressive, arrogant or offensive because, after all, we do depend on constructive working relationships. So the key quality is to be prepared for critical assessments, but also I think it is a skill to do it in a way so that people feel comfortable with you. If they don't feel comfortable with you, whether it's other board members or especially management, they will start covering things up and your ability to understand what is going on becomes compromised. If that happens, the whole thing becomes a self-defeating exercise. What I am trying to emphasise here are the interpersonal skills, being able to talk to people in a firm but friendly way.”

David Hexter

“An independent director should have an adequate level of knowledge and essential inner restraints or, in other words, "conscience". A board member may be competent in a number of various areas or may be an expert in a particular field. The breadth or depth of his/her knowledge is not important in this case. What is important is that his/her knowledge should be useful and sufficient to become a director of this particular company.”

Vladimir Gusakov

“In my opinion, an independent director should be fully independent, have his own point of view and be a real professional. But the most important thing is that he should have his own position and be able to hold his own.”

Vladimir Gusev

“We work to ensure that an independent director is de-facto independent. The main thing for a board of directors is that its members should represent and protect the interests of the entity whose board they are serving on at that time.”

Bella Zlatkis

20%

20% of the top 50 Russian public companies have an independent board chairperson

“The corporation as a system is aimed at preventing conflicts of interest and achieving balance. This is the reason why we have executive management who deal with day-to-day operations, while the board of directors performs the functions of shareholding control and strategic management. If each of them performs their function properly, the "checks and balances system" is maintained.”

Irina Shitkina

The objectivity of the board and its independence from management may be strengthened by the separation of the role of chief executive and chairperson or, if these roles are combined, by designating a senior (lead) independent director to convene or chair sessions of the independent directors.

Separation of the roles of chief executive and board chairperson is regarded as good practice, as it can help to achieve an appropriate balance of power, increase accountability and improve the board's capacity for decision making independent of management.

The Law on JSC explicitly articulates the responsibilities that the board assumes and those for which management is accountable. Furthermore, according to the law, a person exercising the functions of a sole executive body may not be chairperson of the company's board at the same time.

Accordingly, none of the companies surveyed have the roles of board chairperson and chief executive occupied by the same individual.

Best international practice further implies that the board chairperson should be an independent director. For instance, the UK Code states that the chairperson should meet the independence criteria upon appointment.

In fact, 20% of the top 50 Russian public companies have an independent board chairperson. This is comparable with the 2011 Spencer Stuart Board Index results: 21% of boards of S&P 500 companies have truly independent directors.²¹

²¹ 2011 Spencer Stuart Board Index, p.10.

10%

10% of the top 50 Russian public companies have a senior (lead) independent director on the board

“I think the concept of lead independent director was born when shareholders became frustrated with the discussions with management and the board chairman because the chairman backed up the chief executive. So, they wanted another road. The senior independent director is often regarded as the person who leads the chairman’s performance evaluation or the person who, also on behalf of the directors, ensures the chairman is acting in the interest of the board as a whole.”

Sir Robert Margetts

The designation of a senior (lead) director is also regarded as a good practice alternative to having an independent board chairperson. Such mechanisms can also help to ensure high quality governance of the company and the effective functioning of the board.

Again, according to the UK Code, “the board should appoint one of the independent non-executive directors to be the senior independent director to provide a sounding board for the chairperson and to serve as an intermediary for the other directors when necessary. The senior independent director should be available to shareholders if they have concerns which contact through the normal channels of chairperson, chief executive or other executive directors has failed to resolve or for which such contact is inappropriate.”²²

Five out of the top 50 Russian public companies (or 10%) have a senior (lead) independent director on the board and two of these companies are registered abroad. It is notable that three of these five companies have an independent board chairperson as well.

To compare with the 2011 Spencer Stuart Board Index: 92% of S&P 500 boards have appointed a senior (lead) independent director.²³

It is notable that roughly three-quarters of the top 50 Russian public companies have no form of independent board leadership — neither an independent chairperson nor a senior (lead) independent director – versus 3% of S&P 500 boards, according to the 2011 Spencer Stuart Board Index.

²² UK Code, Section A, Par. A.4.1.

²³ 2011 Spencer Stuart Board Index, p.24.

44%

44% consider that broadening the diversity of the board would have a positive impact on its effectiveness

“Diversity is an interesting issue, because who you ideally want as an independent director is somebody with the right capability and experience base who can understand all the issues that the company faces and then examine the different modes of addressing issues by relating to his or her own experience. Ideally, one would seek diversity, provided it does not compromise capability and experience.”

Sir Robert Margetts

“Foreign board members in Russian companies often bring best global practices of corporate governance to the companies.”

Alexander Berlin

1.3. Diversity on the board

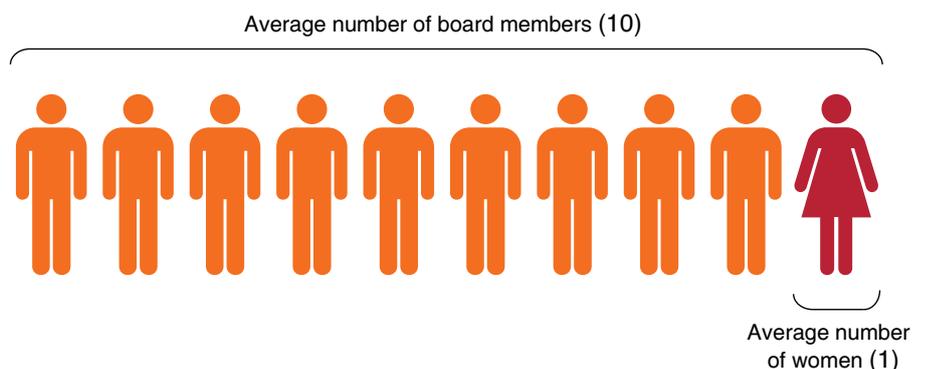
In addition to selecting board members on merit, international best practice now places greater emphasis on appointing directors against objective criteria, taking into account the benefits of diversity when considering the composition and selection of new members of the board. Diversity is considered an important driver of a board’s effectiveness, creating a breadth of perspective among directors and breaking down a tendency towards group thinking.

The UK Code supports this drive by stating that diversity should be considered in the appointment of directors, which includes gender diversity.

The PwC UK NED Survey and 2011 Spencer Stuart Board Index show that diversity is high on a board’s agenda. For instance, females make up 15% of NEDs among the FTSE 100. According to the 2011 Spencer Stuart Board Index, 58% of S&P 500 companies have two or more females on the board, while 18% have three or more.

However, in Russia, promoting gender diversity is not yet a trend. In 2012, across all board member roles of the top 50 Russian public companies, only 7% are held by females with a maximum of three females on board. None of these companies have a female as a board chairperson.

According to our respondents, females make up 11% of all directors on their companies’ boards.



²⁴ UK Code, Section B, Par. B.2.

²⁵ UK NED Survey, p.10.

²⁶ 2011 Spencer Stuart Board Index, p.19.

7%

Across all board member roles of the top 50 Russian public companies, only 7% are held by females

43%

43% of our respondents reported that their boards had no females at all

“Generally, I’ve always been against any quotas. But, perhaps introducing quotas for women in boards makes sense at the initial stage. This would mould the market and allow generating demand thus providing necessary stimuli for shaping an extensive segment of professionals.”

Anna Belova

According to the respondents, 43% of the companies have no females at all on their boards, versus only 9% of S&P 500 boards.²⁷

Almost the same share of respondents (44%) consider that broadening the diversity of the board would have a positive impact on its effectiveness.

However, today there are still not many Russian companies demonstrating the intention to promote gender diversity in practice. None of the companies represented by our interviewees have a formal policy on female representation on the board. According to our interviewees, the issue of introducing such formal standards has not been discussed by their boards.



²⁷ Source: 2011 Spencer Stuart Board Index, p.19.

2. Selection, nomination and election

37%

37% of our respondents reported that the companies' in-house procedures for board candidate selection were not formalised and/or not transparent

“As a rule, in large state-owned companies, those included in the board are the result of a fairly lengthy internal process and an unpublicised government process. To speak of some sort of absolutely open public procedure is, unfortunately, a bit premature right now. However, the procedure is becoming much more transparent especially at the first stage of selecting candidates. Rosimushchestvo portal was created along with registers of independent directors. The self-nomination procedure has been developed.”

Anna Belova

The adequate composition of the board should ensure that it can fulfill its key responsibilities. Principle VI of the OECD Principles lists a number of criteria. The board itself plays a key role in identifying potential board members with the appropriate knowledge, competencies and expertise to complement the existing skills of the board, thereby improving its value-adding potential for the company.²⁸

2.1. Board candidate selection, nomination and election process

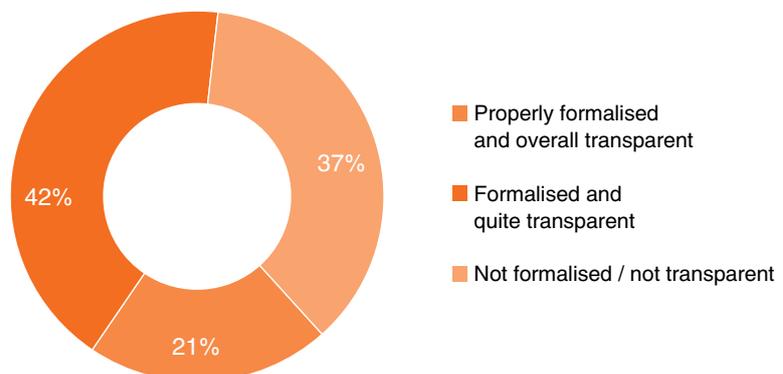
It is recommended by the Russian Code that “election of the board of directors be conducted in accordance with a transparent procedure that takes into account the diverse opinions held by shareholders, ensures that the composition

of the board of directors is in compliance with statutory requirements, and allows the election of independent directors.”²⁹

Similarly, one of the UK Code's main principles states that “there should be a formal, rigorous and transparent procedure for the appointment of new directors to the board.”³⁰

21% of our respondents consider that the board candidate selection procedures are properly formalised in the company's in-house documents and are, overall, transparent; 42% of respondents state that in their companies, these procedures are formalised and quite transparent; 37% of our respondents reported that such procedures were not formalised and/or not transparent.

Do you consider that the board candidate selection procedures are properly formalised in the company's in-house documents and are transparent?



²⁸ OECD Principles of Corporate Governance, 2004, Principle VI.

²⁹ Code of Corporate Conduct approved by the Session of the Government of the Russian Federation of 28 November 28 2001, minutes No. 49, Chapter III, Par. 2.3.

³⁰ UK Code, Section B, Par. B.2.

94%

94% of companies set formal requirements or recommendations related to the board candidates' experience, skills and knowledge

“Russian legislation governing nomination is not perfect. For instance, from a legal perspective, we are not required to request the nominee’s consent for nomination. Also, our current legislation does not include a provision stating that a company may advance certain qualification requirements to the board members. I believe that companies should have the right to put forward their requirements to the board members. However, at the same time, these requirements should not contradict the Russian Constitution or any international treaties. For instance, we must not impose gender, race or nationality limitations, however, it would be a good idea to impose qualification, profile and industry experience requirements.”

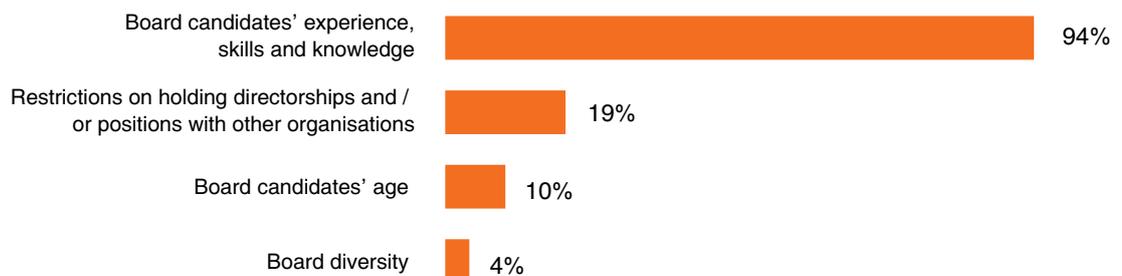
Irina Shitkina

The Russian Code recommends that the company charter explicitly set forth specific criteria for members of the board of directors.³¹

According to our respondents, 94% of companies set formal requirements or recommendations related to the board candidates' experience, skills and knowledge. 10% of companies set

requirements/recommendations as to the candidates' age (to compare, 73% of S&P 500 boards set a mandatory retirement age for directors³²). Only 4% of respondents stated that their companies' in-house documents contained provisions concerning diversity on the board.

Do the company's in-house documents contain any formal requirements or recommendations related to the following?



³¹ Code of Corporate Conduct approved on the Session of the Government of the Russian Federation of 28 November 2001, minutes No. 49, Chapter III, Par. 2.1.3.

³² 2011 Spencer Stuart Board Index, p.17.

19%

19% of companies have set formal limitations for board members on holding directorships and/or positions with other organisations

“In order to form an effective board of directors, we need people who actually possess the necessary and sufficient time to fully execute the duties they are entrusted with.”

Anna Belova

“Being able to dedicate time is essential to the independent director role. I’m in favour of few but good directorships – where you can really do something, where you can contribute.”

Ferdinando Beccalli-Falco

“In our opinion, an independent director can only work efficiently if he is a member of not more than three boards. For this reason, the company’s internal document establishing the status of an independent director provides for this criterion.”

Irina Shitkina

Principle VI of the OECD Principles says that board members should be able to commit themselves effectively to their responsibilities. For instance, serving on too many boards can interfere with board members’ performance.³³ In this view, whether multiple board memberships are compatible with effective board performance should be carefully considered when there is no

legal cap on the number of memberships, which is the case in Russia.

According to our respondents, given the time and commitment required for effective board service, 19% of companies have set formal limitations for board members on holding directorships and/or positions with other organisations. This is versus 74% of S&P 500 companies.³⁴



³³ OECD Principles of Corporate Governance, 2004, Principle VI.

³⁴ 2011 Spencer Stuart Board Index, p.15.



Disclosure of candidates' background

To further improve the selection process, the OECD Principles also call for full disclosure of the experience and background of candidates for the board and the nomination process, which will allow for an informed assessment of the abilities and suitability of each candidate. "Disclosure should include information about board candidates, including their qualifications, the selection process, other company directorships and whether they are regarded as independent by the board. It is important to disclose membership of other boards, not only because it is an indication of experience and possible time pressures facing a member of the board, but also because it may reveal potential conflicts of interest and makes transparent the degree to which there are interlocking boards."³⁵

The Law on JSC requires that "a proposal concerning nominees state the name of each nominee and data of the document certifying his identity, the name of the body to which he/she is proposed for election and also other information on him/her as stipulated by the charter or in-house documents of the company."³⁶

Further, the Russian Code states that "the board of directors is accountable to shareholders and must enjoy their

trust; therefore, shareholders should have an opportunity to receive full information about all candidates for members of the board of directors. In particular, it is recommended that shareholders be provided with the following information: the identity of the person proposed as the relevant candidate; age, education, positions held over the last five years; position held at the moment of nomination; nature of relations with the company; membership in the boards of directors or official positions held with other legal persons, as well as nomination for membership in the boards of directors or nomination for election (appointment) to official positions with other legal persons; information on relations with affiliated persons; the nature of relations with major business partners of the company; other information related to the financial status of the candidate or which may otherwise affect the discharge of the duties of a member of the board of directors of the company by the person. Accordingly, it is recommended that the company should, based upon specific eligibility criteria applicable to members of the board of directors, determine in its charter what information is subject to disclosure to shareholders about candidates for positions of members of the board of directors."³⁷

³⁵ OECD Principles of Corporate Governance, 2004, Principle V.

³⁶ Law on JSC, Chapter VII, Art. 53.

³⁷ Code of Corporate Conduct approved on the Session of the Government of the Russian Federation of 28 November 2001, minutes No. 49, Chapter III, Par. 2.3.1.

50%

Only 50% of the top 50 Russian public companies disclose background information on board candidates in general shareholder meeting materials

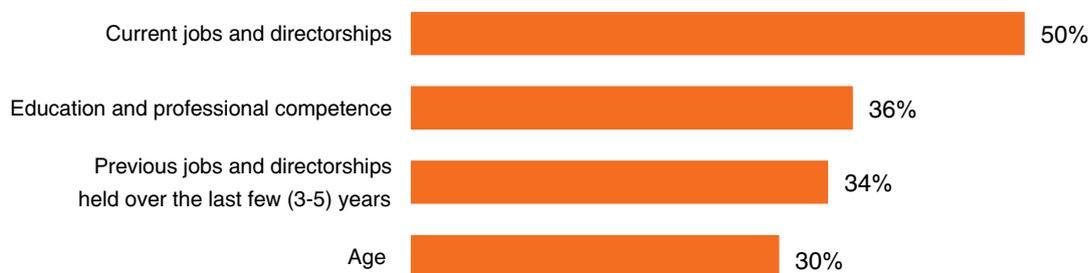
In practice, only half of the top 50 Russian public companies disclose background information on board candidates in general shareholder meeting materials. However, this information is limited and usually contains data on nominees' current

jobs and directorships, education and professional competence, previous jobs and directorships over the last few years and the nominees' age.

None of the companies publishes information about nomination for other

jobs and directorships, the nature of relations with the company or its major business partners, which could lead to conflicts of interest and affect a board's judgment.

Disclosure of information about board candidates:



“All directors are equally and individually responsible to all shareholders – not a particular portion of the shareholders, but to all shareholders. My own responsibility is to act to promote the well-being of the company and in the interest of all shareholders. Corporate law has become very clear on this, both in the West and also in Russia.”

Sir Robert Margetts

Roles and responsibilities in the director selection and nomination process

The OECD Principles promote an active role for shareholders in the nomination and election of board members: “To elect the members of the board is a basic shareholder right. For the election process to be effective, shareholders should be able to participate in the nomination of board members and vote on individual nominees or on different lists of them. In the meantime, the board itself also has an essential role to play in ensuring that all these and other aspects of the nomination and election process are respected and the established procedures are transparent...”

It has long been recognised that in companies with dispersed ownership,

individual shareholders might have too small a stake in the company to warrant the cost of taking action or for making an investment in monitoring performance... To overcome this asymmetry which favours diversification, they should be allowed, and even encouraged, to co-operate and co-ordinate their actions in issues concerning their basic shareholder rights, including nomination and election of board members.”³⁸

When electing board members, opinions of all shareholders should be taken into account, including those with small share holdings. This goal may be achieved only by electing members of the board of directors by cumulative voting. Election of members of the board of directors by cumulative voting is an important

protection of the rights of minority shareholders.

The Law on JSC regulates the director nomination and election process as follows: “The members of a company’s board are elected by the general meeting of shareholders by cumulative voting. The shareholders (or the shareholder) of the company who own in the aggregate at least 2% of the voting shares of the company are entitled to propose nominees for election to the company’s board of directors. The board of directors shall be entitled to put nominees in a list of nominees at their own discretion only in the event of lack or insufficient number of nominees proposed by shareholders.”³⁹

³⁸ OECD Principles of Corporate Governance, 2004, Principle I.

³⁹ Law on JSC, Chapter VII, Art. 53.

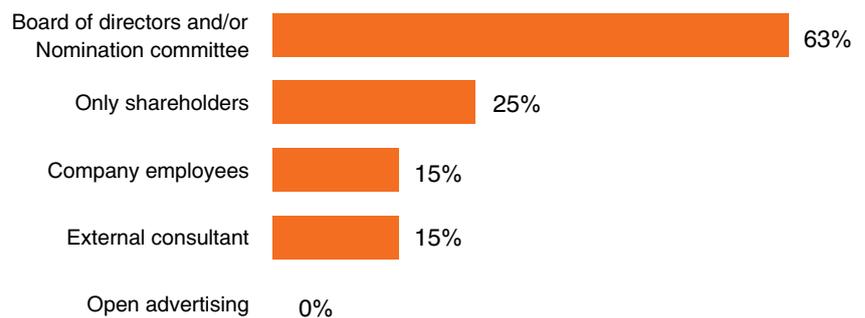
15%

15% of respondents claim that their companies involve external consultants in the director search and selection process

According to our respondents, in 25% of companies only shareholders are involved in the board candidate search and selection. In 63% of companies, the board of directors and/or its nomination committee participate

in carrying out the director search and selection as well. 15% of respondents claim that their companies (all of which are public) involve external consultants in director search and selection. None of the companies uses open advertising.

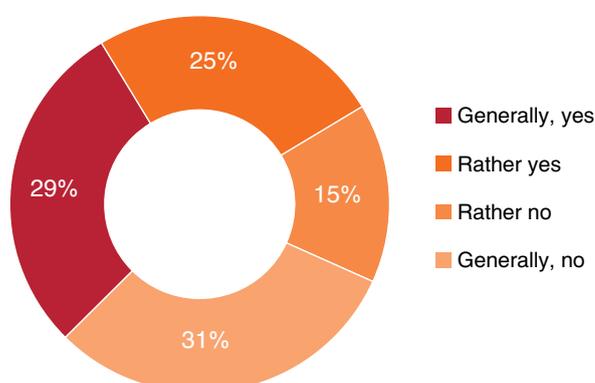
The board candidate search and selection process is carried out by/with the involvement of:



29% of the survey participants claim that, as a rule, minority shareholders do nominate candidates to the board. One-quarter stated that this is generally the case. However, 46% of respondents

reported that, generally speaking, minorities are not active in nominating directors. In approximately one-third of companies, minority shareholders generally do not nominate directors.

In practice, do the company’s minority shareholders nominate candidates to the board?



2.2. The role of the board nomination committee

The UK Code requires that there should be a (separate) nomination committee which should lead the process for board⁴⁰ appointments and make recommendations to the board. However, the Russian Code recommends that the board of directors should create a nomination and remuneration committee that should encourage attraction of skilled experts to the company’s governing bodies, as well as create incentives necessary for them to work effectively.⁴¹

The Russian Code also states that, “in order to ensure objectivity of the recommendations issued

by the nomination and remuneration committee, it is advisable that it is staffed exclusively with independent directors. When objective circumstances make this impossible, the committee should, as a minimum, be headed by an independent director and consist of those members of the board of directors who do not hold official positions with the company.”⁴²

The Moscow Exchange listing rules require company boards to establish a nomination and remuneration committee which is fully independent (failing this – non-executive) for the companies from list A1 and A2. For lower lists, such a committee is not required at all.⁴³

⁴⁰ UK Code, Section B, Par. B.2.1.

⁴¹ Code of Corporate Conduct approved on the Session of the Government of the Russian Federation of 28 November 2001, minutes No. 49, Chapter III, Par. 4.3.1, 4.10.1

⁴² Code of Corporate Conduct approved on the Session of the Government of the Russian Federation of 28 November 2001, minutes No. 49, Chapter III, Par. 4.10.3.

⁴³ FSFM Regulations on the Activity for Trade Organization on the Securities Market, Appendices 1,3,4.

94%

94% of the top 50 Russian public companies have a nomination committee (or equivalent body)

“In Russian state-owned companies, it does not appear to be common practice for the HR and remuneration committee to perform functions related to selecting candidates for the board of directors.”

Anna Belova

Subsequently, boards in many Russian public companies have established nomination committees to ensure proper compliance with established nomination procedures and to facilitate and coordinate the search for a balanced and qualified board. According to our respondents, 66% of companies (mainly, public ones) have a nomination committee (or equivalent body) under the board of directors.

Among the top 50 Russian public companies, such a committee is established in 94% of companies, while in 78% of these companies, the same committee fulfills both nomination and remuneration functions. 70% of these companies make the nomination

committee’s terms of reference available, explaining its role and authority, as well as the composition principles and general working procedures.

However, in practice, nomination and remuneration committees in Russian companies normally do little about NED search and selection. Indeed, their function related to nomination is often limited to suggesting candidates to top executive positions.

However, some of our interviewees believe the role of the nomination committee tends to evolve rapidly, and even today one can see some good examples of committees leading the process for board appointments.



26%

26% of the top 50 Russian public companies have fully independent nomination committees

62%

In nomination committees of the top 50 Russian public companies, independent directors make up 62%, with three to four committee members, on average

The Russian Code states that “the number of committee members should be determined so as to enable the committee to review matters under consideration in the most comprehensive fashion and to take into account the opinions of all members. As much as the work of a committee involves detailed review by committee members of each matter under consideration, it is recommended that board members’ participation in multiple committees be restricted.”⁴⁴

In selecting board members, there is always potential for conflict of interest. In view of this, boards should consider assigning a sufficient number of non-executive board members to this task who are capable of exercising independent judgment. It is considered good practice for independent board members to have a key role on nomination committees.

For instance, the UK Code requires that “a majority of members of the nomination committee should be independent non-executive directors, the chairperson or an independent non-executive director should chair the committee.”⁴⁵

The Russian Code does not provide for a minimum number (or share) of independent directors on board committees. It only recommends that “committees of the board of directors are headed by members of the board of directors who do not hold official positions with the company.”⁴⁶

Respondents reported their nomination committees had, on average, four members, with about 60% of them being independent directors. Similarly, in nomination committees of the top 50 Russian public companies, independent directors make up 62%, with three to four committee members, on average.

⁴⁴ Code of Corporate Conduct approved on the Session of the Government of the Russian Federation of 28 November 2001, minutes No. 49, Chapter III, Par. 4.7.2.

⁴⁵ UK Code, Section B, B.2.1

⁴⁶ Code of Corporate Conduct approved on the Session of the Government of the Russian Federation of 28 November 2001, minutes No. 49, Chapter III, Par. 4.10.3.

24%

24% of the top 50 Russian public companies engage external experts in the nomination committee work

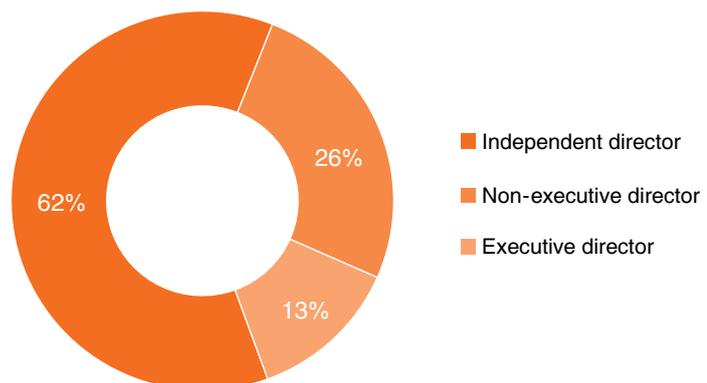
70%

70% of the top 50 Russian public companies have an independent chairperson on the nomination committee

One-quarter of the top 50 Russian public companies have fully independent nomination committees (comprising only independent directors).

The Russian Code allows board committees to enroll, if necessary, experts with required professional skills relevant to the work of a particular committee. In practice, according to our respondents, one-quarter of companies engage external experts in the nomination committee work.

70% of the top 50 Russian public companies have an independent chairperson on the nomination committee. According to the respondents, 62% of the companies that have a nomination committee (or an equivalent body) have an independent committee chairperson, one-quarter of companies have a non-executive committee chairperson, and 13% have an executive director in this role.



“It is necessary to engage intellectual people when they too are prepared to be engaged, as well as people with highly-regarded business reputations who are prepared not to give up the principle of independence in order to protect their business reputation.”

Irina Shitkina

“Today, creativity, the search for unconventional solutions, the creation of competitive playing fields where value is created not under conditions of rapid growth, but in the reality in which the economy currently operates, are in the foreground.”

Anna Belova

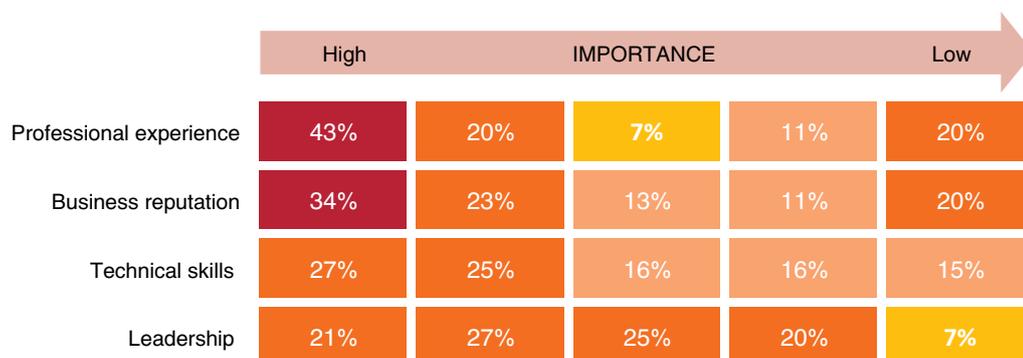
2.3. Key selection factors when appointing directors

Bringing the right skills to the role is a challenging task for the board and its nomination committee. If the board of directors is to discharge its duties properly and make a significant contribution to the management of the company’s affairs, its members should have the knowledge, skills and experience required to make decisions on matters within the usual scope of authority of the board of directors and for performing efficiently the functions of the board of directors of a particular company.

Russian Code stipulates that the board composition should optimise its effectiveness. The Code states that “the board of directors should enjoy the trust of shareholders – otherwise it will not be able to perform its functions effectively. The personal qualities of members of the board of directors and their reputation should not give rise to any doubts that they may not act in the best interests of the company.”⁴⁷

We asked our respondents to evaluate the importance of key selection factors and requirements when nominating directors to the board. According to their responses, professional experience comes first, followed by business reputation, then technical skills and leadership.

What are the key selection factors/requirements when nominating directors to the company’s board?



⁴⁷ Code of Corporate Conduct approved on the Session of the Government of the Russian Federation of 28 November 2001, minutes No. 49, Chapter III, Par. 2.1.1.

Most boards primarily target retired and active top executives when searching for independent directors

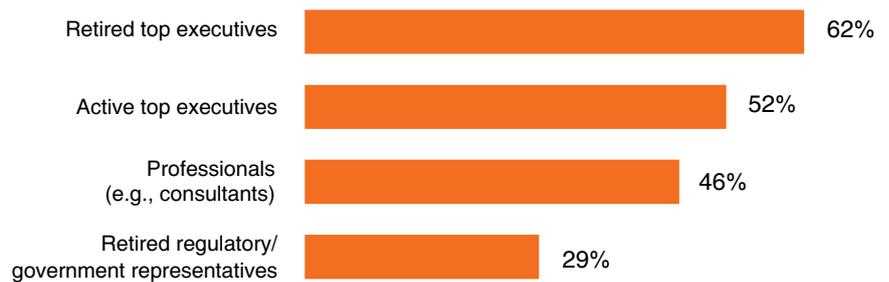
“When selecting candidates for the position of an independent director, we try not to engage too many former government officials, but we take into consideration the experience that some of them have and nevertheless invite them.”

Bella Zlatkis

According to our respondents, when selecting independent directors, 62% of boards target retired top executives, about 52% target active top executives, 46% seek to attract professionals (e.g. consultants), and 29% look for retired regulatory/government representatives.

The 2011 Spencer Stuart Board Index demonstrates that S&P 500 boards also put active and retired top executives at the top of their wish lists: half of the boards seek current top executives, while 34% look for retirees from those roles.⁴⁸

When searching for independent directors, the board targets:



⁴⁸ 2011 Spencer Stuart Board Index, p.12.

75%

75% of our respondents feel that their boards currently lack directors with particular experience, skills and knowledge

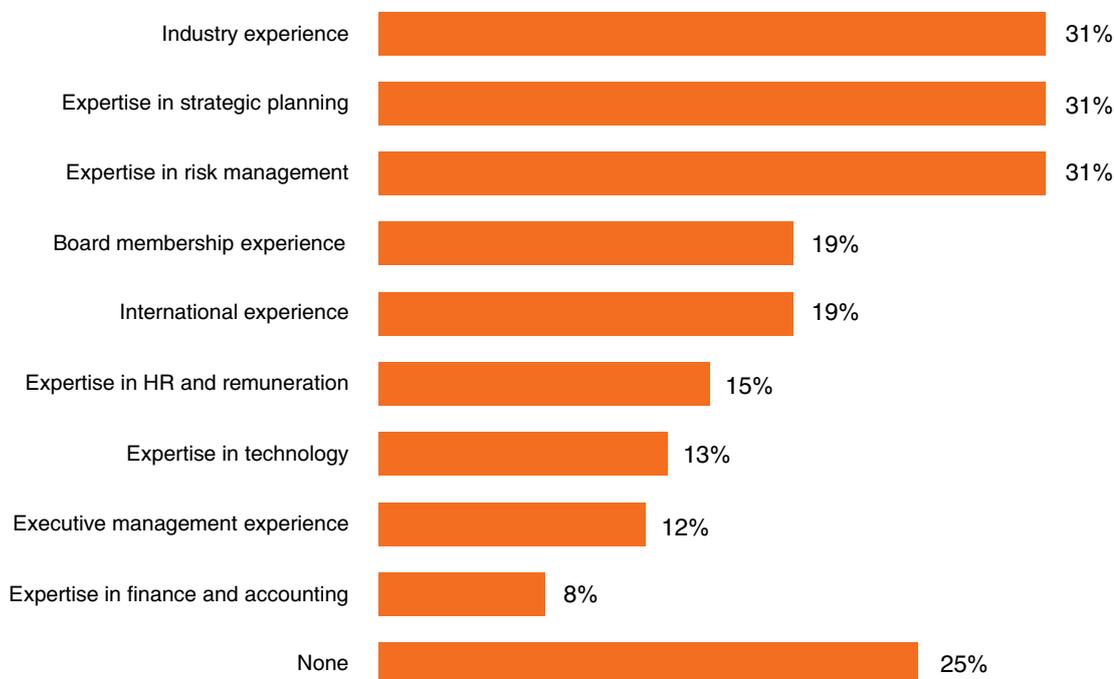
“The board of directors is the product of synergy and teamwork. The board works efficiently when its members have different competencies.”

Irina Shitkina

Three-quarters of our respondents feel that their boards currently lack directors with particular experience, skills and knowledge. Many boards note a lack of industry experience, expertise in strategic planning and risk management. Quite a few boards

wish to attract more directors with board membership experience and international experience. Some lack expertise in technology and executive management experience, although few still feel the need to increase board expertise in finance and accounting.

Do you consider that the company's board currently experiences a lack of directors with the following experience, skills and knowledge?



To compare with the 2011 Spencer Stuart Board Index, almost 30% of S&P 500 companies are looking to add new skills to the board. Around 40% of boards are looking for directors with

financial, industry and/or international expertise. Roughly 20% of boards are looking for candidates with regulatory/government, technology and/or risk expertise.⁴⁹

⁴⁹ 2011 Spencer Stuart Board Index, p.p.12-13.

3. Board development, performance evaluation and succession planning

85%

85% of our respondents claim their companies have an induction process for new board members in place

3.1. Induction process and development programs for directors

The concept of an induction process for newly-appointed directors is not a new one. In 2003, Sir Derek Higgs highlighted in his report that, “to be effective, newly-appointed NEDs quickly need to build their knowledge of the organisation to the point where they can use the skills and experience they have gained elsewhere for the benefit of the company.”⁵⁰

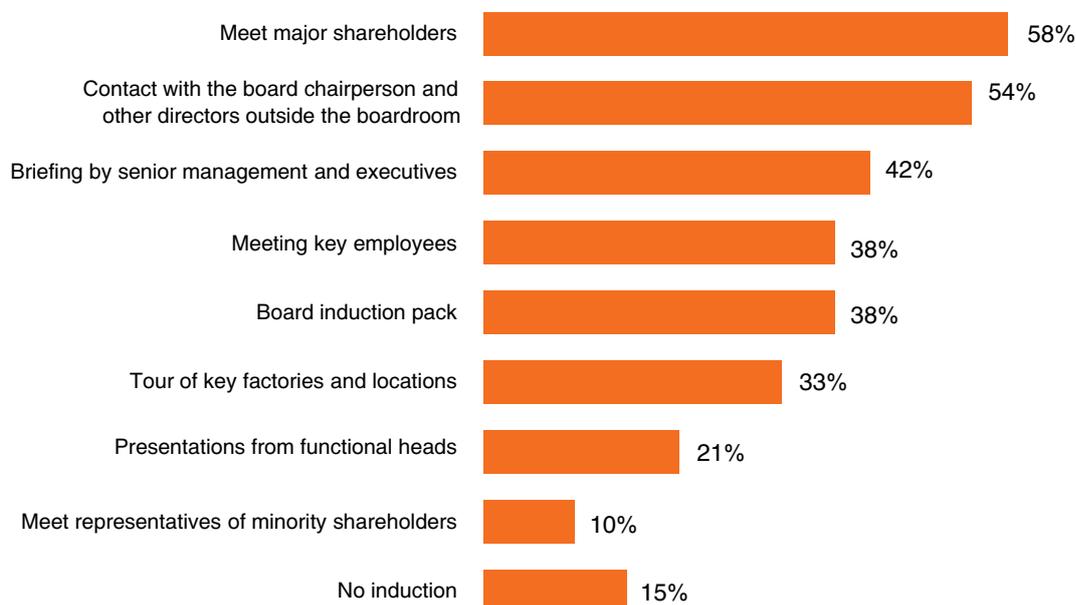
The UK Code states that “all directors should receive induction on joining the board and should regularly update and refresh their skills and knowledge... The chairperson should ensure that new directors receive a full, formal and tailored induction on joining the board. As part of this, directors should avail themselves of opportunities to

meet major shareholders... To function effectively, all directors need appropriate knowledge of the company and access to its operations and staff.”⁵¹

According to our respondents, 85% of companies have an induction process in place.

We asked our respondents what the induction process for newly-appointed board directors covered in their companies. According to the respondents, in most companies the induction process implies newly-appointed directors meeting major shareholders, as well as meeting the board chairperson and other directors outside the boardroom. In only 10% of companies “new joiners” meet representatives of minority shareholders as part of induction. Finally, in 15% of companies there is no induction for newly-appointed directors at all.

In practice, what does the induction process for newly-appointed board directors cover in your company?



⁵⁰ Higgs, Derek. "Review of the role and effectiveness of non-executive directors", 2003, Par. 11.1.

⁵¹ UK Code, Section B, B.4.

Technical reading and attending seminars and conferences are the most popular tools for directors to stay up-to-date with regulatory, technical and other developments

“You are successful to the extent that you are up-to-date. A board member who does not keep up-to-date with legislation, trends, global practice and analytics in his area is absolutely useless.”

Bella Zlatkis

“I think it’s very important if you are an independent director to be active – not just in the sphere of the particular company but to be active elsewhere in business and public life. By doing so, you can bring other experience and sources of information, other updates on what is happening in the world, such as on the latest requirements of the reporting system or the regulatory authorities in different locations in the world.”

Sir Robert Margetts

“A real professional is someone who knows a little bit more in a certain segment or area than his peers and can resolve an issue or achieve a result in the most efficient way. Talking with your colleagues who are on boards of directors, including on boards of large international companies, is a very useful practice. And of course, gaining practical day-to-day experience as an active board member is the most important.”

Anna Belova

Board development

“In order to improve board practices and the performance of its members, an increasing number of jurisdictions are now encouraging companies to engage in board training and voluntary self-evaluation that meets the needs of the individual company. This might include that board members acquire appropriate skills upon appointment and thereafter remain abreast of relevant new laws, regulations and changing commercial

risks through in-house training and external courses.”⁵²

The UK Code states that “the chairperson should ensure that the directors continually update their skills and the knowledge and familiarity with the company required to fulfill their role both on the board and on board committees. The company should provide the necessary resources for developing and updating its directors’ knowledge and capabilities.”⁵³

⁵² OECD Principles, Principle VI.

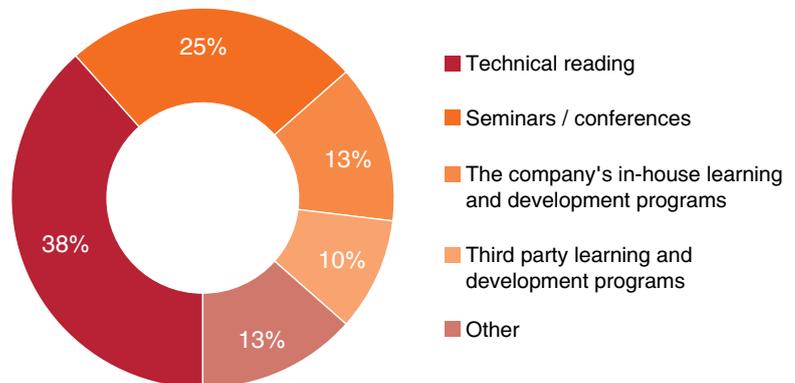
⁵³ UK Code, Section B, B.4.



We asked our respondents how they stay up-to-date with regulatory, technical and other developments that are relevant to their role. The most popular answer was technical reading. Next came seminars and conferences. The company's in-house learning and

development programs and third party learning and development programs are in third and fourth place, respectively. Some of the other sources our respondents mentioned were other directorships and exchanges with colleagues.

How do you stay up-to-date with regulatory, technical and other developments that are relevant to your role?



65%

65% of our respondents claim their boards carry out their performance evaluation annually

“We have a system for evaluating the performance of the board of directors, and the results of this evaluation affect the directors' compensation and their ability to be re-elected.”

Bella Zlatkis

3.2. Board performance evaluation

Boards are encouraged to continuously examine ways of improving their effectiveness. For instance, the UK Code recommends that “the board should undertake a formal and rigorous annual evaluation of its own performance and that of its committees and individual directors.”⁵⁴

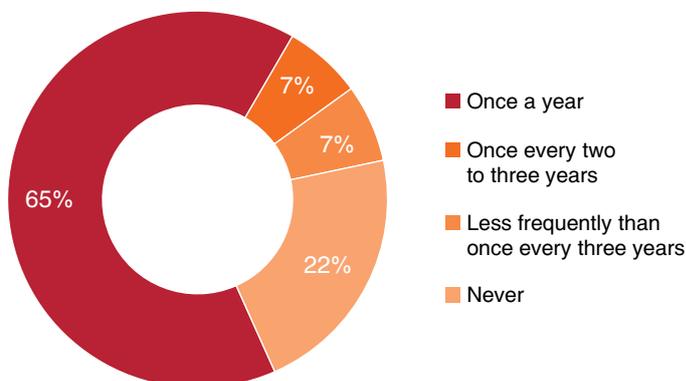
If it's conducted effectively, the evaluation process can provide companies with insights into whether they have the necessary balance of skills, knowledge and experience among the members of their board. This information can be used in succession planning and to better understand the time commitment and training needed by individual directors to carry out their role.

Frequency of board evaluations

According to our respondents, 65% of boards (among listed companies - over 70% of boards) carry out their performance evaluation annually, while 7% do this once every two to three years, and another 7% do this even less frequently. To compare: according to the UK NED Survey, board evaluations tend to be performed on an annual basis by 87% of the companies surveyed.⁵⁵

Yet, according to the respondents, 22% of boards never conduct board performance evaluations, versus 6% of UK companies and 2% of S&P 500 companies.⁵⁶ For Russian state-controlled companies, this rate is almost twice as high and makes up 42% of companies.

How often does your board carry out its performance evaluation?



⁵⁴ UK Code, Section B, B.6.

⁵⁵ UK NED Survey, p.6.

⁵⁶ 2011 Spencer Stuart Board Index, p.31.

20%

20% of the boards conducting performance evaluations engage a third party for this assignment

“In my view, conducting independent evaluations of a board of directors' activities is a positive practice which brings a system-wide, long-term positive effect. Unfortunately, this practice is not widely used in our country, particularly in companies with state participation.”

Anna Belova

“I'm not an advocate of external review processes because the key to improvement is the commitment of the directors. Board members are in the best position not only to identify the weaknesses, but also to put them right: they have the data, they know which things work well and which don't, and, in the end, they have a commitment to do better and to implement all desired changes.”

Sir Robert Margetts

Board evaluation tools

Overall, board evaluations tend to be performed on a regular basis. But still, the effectiveness of these evaluations and the benefit they provide depends on the quality of the process and the enthusiasm with which they're approached.

Our survey shows that most of the boards conducting their performance evaluation do this in the form of self-assessment through questionnaires. 34% of boards carry out self-assessment

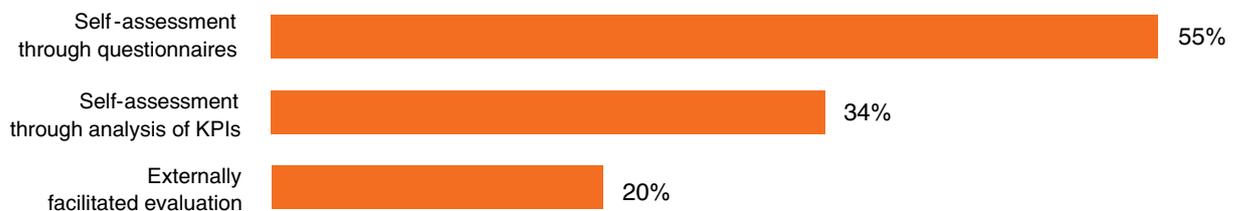
through analysis of KPIs. 20% of respondents, representing mainly public companies, claim that their boards conduct externally-facilitated board evaluations. This is versus 13% of UK companies⁵⁷ and 14% of S&P 500 companies.⁵⁸

To get the most out of board evaluations, an outside view of the board's effectiveness is essential. Indeed, external facilitation of board evaluations could potentially add objectivity or value to the process.

The UK Code now requires FTSE 350 companies to have externally-facilitated board evaluations at least every three years.⁵⁹

Until now, many companies haven't been open to external evaluations, preferring to undertake an internal process instead. However, we anticipate that over the next few years, more companies (at least, of those listed on the London Stock Exchange) will conduct external evaluations to comply with the UK Code.

How does your board conduct the board evaluation process?



⁵⁷ UK NED Survey, p.8.

⁵⁸ 2011 Spencer Stuart Board Index, p.32.

⁵⁹ UK Code, Section B, B.6.2.

64%

64% of the boards conducting performance evaluations disclose their results

“We are keen on developing more and more transparency which is, in our view, one of the greatest routes to enhance governance and accountability not only to shareholders, but to stakeholders more generally.”

Sir Robert Margetts

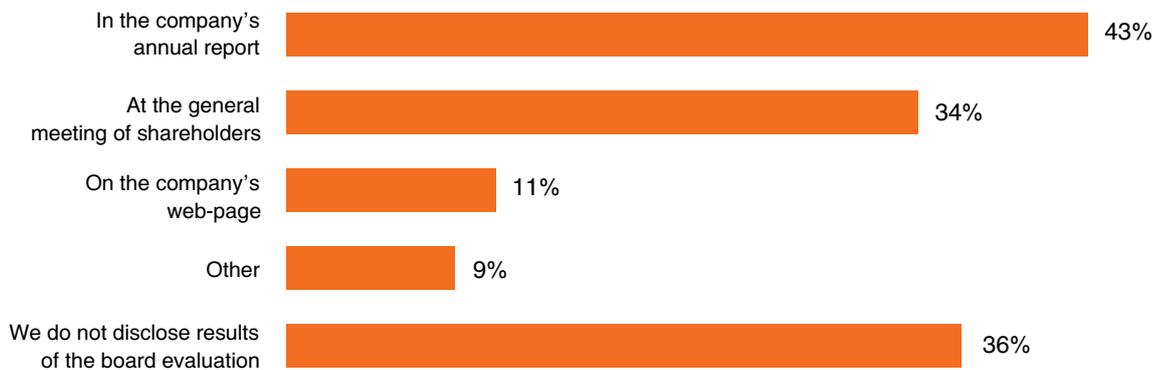
Disclosure of board evaluation results

According to our respondents, 43% of companies disclose the results of the board evaluation in their annual report and 34% disclose the results at their general meeting of shareholders. Only one-tenth of companies disclose the results of their board evaluation on their web pages.

Yet, one-third of companies do not disclose results of their board evaluations at all.



How does your board conduct the board evaluation process?



92%

92% of our respondents believe board performance evaluations are useful

“I strongly believe in board reviews. These are not about negative reviews, but it is about examining opportunities for improvement. To get the best out of the board review process, you have to make it a positive event. If it becomes a negative process, then I think it might endanger the quality of the review and the enthusiasm of people trying to submit their ideas for improvement.”

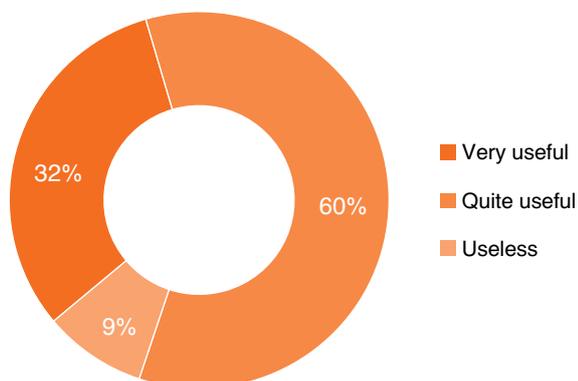
Sir Robert Margetts

Usefulness of board evaluations

Our surveys demonstrate that a majority of directors believe that there is great merit in conducting evaluations of the effectiveness of the board. Evaluations are becoming less of a compliance formality and are being used more as a development tool to better understand how the functions and dynamics of a board and individual directors can be improved.

Over 90% of our respondents consider board evaluations to be useful (or potentially useful, if this practice has not yet been introduced in their company). Among the boards that conduct performance evaluations, only 9% of directors consider this practice to be useless.

In your opinion, how useful are board evaluations?



In all the companies surveyed, board directors are elected for a term of one year or less, in line with Russian legal requirements

3.3. Succession planning

Companies are encouraged to regularly refresh their boards and committees. As part of this, boards are expected to have in place a succession plan which takes into account the evolving requirements of their company and the skills and expertise needed in the boardroom.

It has been argued that board succession is also considered necessary to make sure there's a refreshment of ideas so boards don't become stagnant and director tenure doesn't cause board or committee independence to be called into question.

The UK Code encourages that all directors be subject to annual re-election by shareholders, assuming their individual performance continues to be effective and they demonstrate commitment to the role following a formal performance evaluation. Following the Code's recommendation, 72% of UK companies have introduced annual re-election in 2011.

In Russia, annual director re-election is required by the law and is subsequently introduced in all joint stock companies.⁶⁰

The annual re-election is intended to increase accountability to shareholders.

It is argued, however, that it may create instability and a lack of continuity should directors not be re-elected by shareholders. The lack of continuity, in turn, could lead to directors adopting a short-term focus, a behavior that governance best practice has focused on eliminating.

With this in view, the UK Code recommends that "the board should satisfy itself that plans are in place for orderly succession for appointments to the board and to senior management, so as to maintain an appropriate balance of skills and experience within the company and on the board and to ensure progressive refreshing of the board."⁶¹

In fact, only 16% of our respondents (mainly those representing public companies) reported that the board succession planning was formalised in their company's in-house documents.

According to the questionnaire respondents, on average, two new directors per board were appointed at the 2012 annual general meetings of shareholders. 12% of respondents reported that no new directors had been appointed to their boards.

⁶⁰ The Law on JSC, Chapter VIII, Art. 66: "The members of the board of directors of a company shall be elected by the general meeting of shareholders for a term ending at the time of the next annual general meeting of shareholders."

⁶¹ UK Code, Section B, B.2.

“Before I accept a directorship, I do pretty thorough informal due diligence as to the character of the company and the reputation of the management and shareholders, because obviously some companies have higher integrity standards than others.”

David Hexter

“First of all, presence of shareholder’s commitment. The second important factor is understanding and acceptance of the shareholder’s strategic position on strategic development of the company and creating value in a long-run. Existing corporate procedures and quality of the company’s corporate management are also very important.”

Anna Belova

“What I look for when I consider an opportunity to become an independent director are interesting and stimulating activities, doing something different and new. What do I look at? First of all, the company must be involved in whatever you consider “worthwhile human activity.” Second, I do like global companies facing all the challenges that the world has to offer. So, I’ve got to be satisfied that it is going to be stimulating all the time. As to the particular characteristics of the company – it must be very clear to me that the company is committed to adopting the best global standards and is looking for people like myself to play a very active role and contribute to establishing those best global standards. What is also very important to me is the integrity and reputation the company has built up. I would not be joining a board where I would be embarrassed by differences in the ethical standards of a company. Finally, the quality of management leadership and its ambition is essential to all the other points I’ve made.”

Sir Robert Margetts

“The critical factor for making decisions on the board's membership is understanding one's mission on the board. It is important that the owner is prepared and agrees with the fact that an independent director will express his own opinion on key issues of the company's operations, which may be contrary to the owner's opinion.”

Alexander Berlin

“Accepting a directorship is generally when I find a company which, for one reason or another, is interesting for me – either because it gives me a chance to learn something new, which is important, or because it allows me to apply a lot of the knowledge and things that I’ve developed over my career so that I can help it achieve its objectives.”

Ferdinando Beccalli-Falco

“There is one single principle that determines my decision on membership: I consider whether there is a demand for my experience, whether the work on the board is of interest for me and whether the company will benefit from my participation.”

Bella Zlatkis

4. Director perspective

When accepting a directorship, our respondents primarily consider a company's reputation and the possibility of adding value and making a real difference, as well as the business strategy and financial strength of a company

4.1. Key factors when accepting a directorship

Appointing individuals is a two-way process. Companies might find it challenging to identify individuals who meet their criteria, but candidates will also undertake a sort of due diligence against their own criteria to ascertain whether a particular company may be a good fit for them.

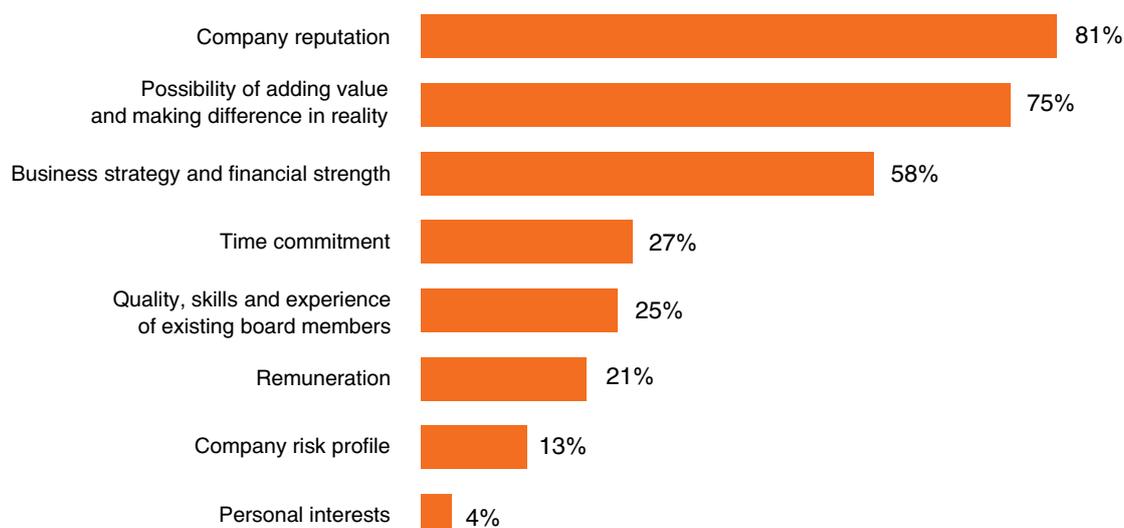
Our respondents were asked to select the three most important factors that they (as candidates) consider when accepting a directorship in a company.

The most popular answer (and the most important factor) is company reputation (chosen by 81% of respondents).

In second place is possibility of adding value and making a real difference with 75% of responses. Next comes business strategy and financial strength (58%).

Other popular answers include time commitment (27%), quality, skills and experience of the board (25%) and remuneration (21%). Not many directors focus primarily on company risk profile (13%) and personal interests (4%).

What key factors do you (as a candidate) consider when accepting a directorship in a company?



48%

48% of our respondents (and most board and nomination committee chairs) believe that their role has become more attractive over the last few years

“Directorship in the past was considered to be very much of honorific kind of role – you was appointed to the board because you had a certain background and achievements and not much was required from you. Today, board membership is a commitment where you have to act, you have to be involved, you have to do things. Before it was about just a presence, today it is an active role, even if it is a role of listening and giving recommendations.”

Ferdinando Beccalli-Falco

“In my opinion, membership on a board of directors has become very interesting work. If we say that, in the long-term perspective, we would like to see less government involvement and more effective management of the economy, then professional directors are exactly the solution.”

Anna Belova

“These days, the expectations of independent directors have been steadily increasing. With these expectations come accountabilities – not just from shareholders, but increasingly from regulators, politicians, the public, the media, and of course NGOs in some of those sustainability issues. When people are not satisfied with the company, clearly they have a go at management and then the next course is to say that independent directors are not doing what they should be doing, calling the management to account, and testing, challenging the management’s actions as they should be. I personally found that the role of independent director has become more challenging for me, and like I said, more stimulating.”

Sir Robert Margetts

“For me, this position is appealing because I know the subject, I feel useful, I see that the board needs me, and the main thing is that we see the results of our work.”

Bella Zlatkis

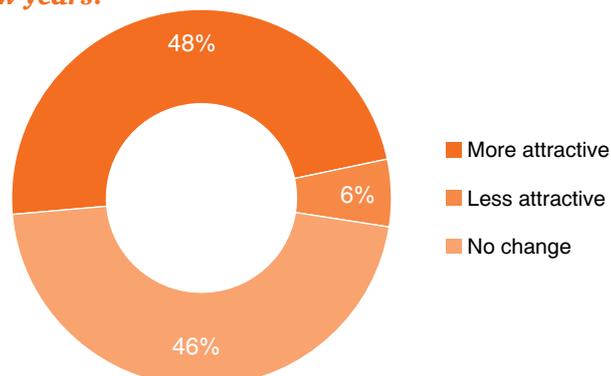
4.2. Evolution of director role

Almost half of our respondents (and most board and nomination committee chairs) believe their role has become more attractive over the last few years, primarily due to its challenging nature, the growing professionalism of boards and, above all, the ability to add value. Furthermore, directors note that board

membership contributes much to their professional development.

Those who think the role has become less attractive (6%) feel that the failure to properly distribute authority between the board of directors and top executives (e.g. when directors are involved in operational details) results in greater risks for directors.

Has the role of director become more or less attractive to you over the last few years?

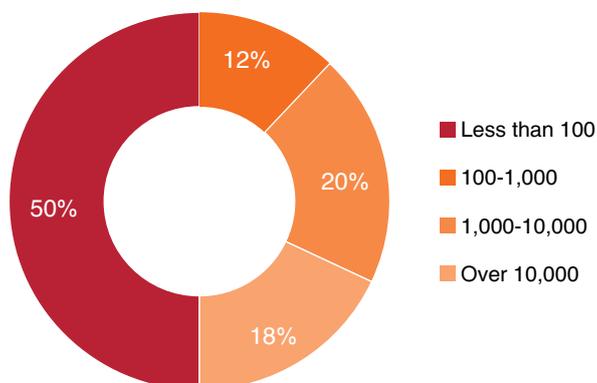


Appendix I: About our respondents



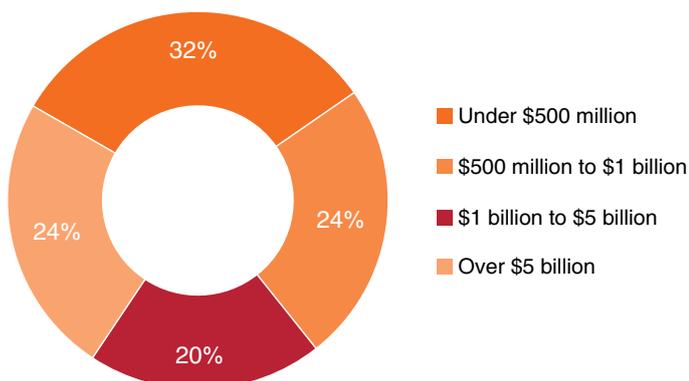
- Sixty-three directors responded to the online questionnaire.
- Our respondents, on average, are members of two boards of public companies.
- 50% of our respondents represent companies where there are less than 100 holders of ordinary shares, whereas 18% represent those with more than 10,000 shareholders.

How many holders of the company's ordinary shares are there?



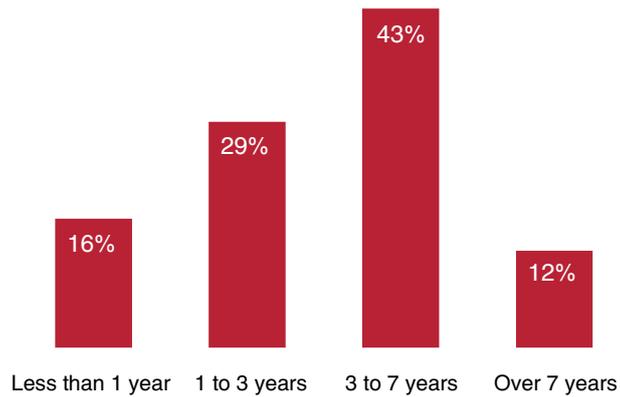
- Our respondents represent companies with very different annual revenues ranging from under \$500 million to over \$5 billion.

What are the annual revenues of the company?



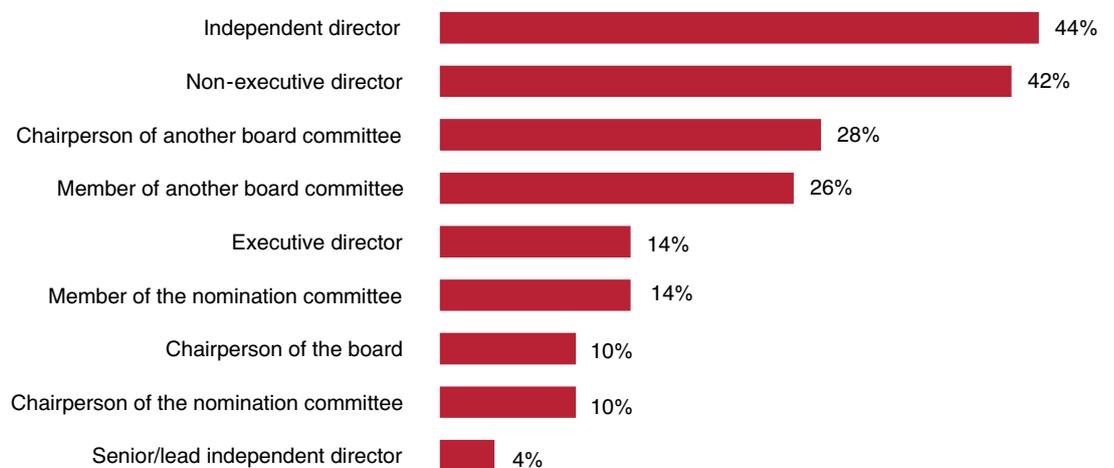
- 43% of our respondents have been board members with their companies for three to seven years, 29% for one to three years, 16% for less than a year, and the other 12% for more than seven years.

How long have you occupied the role of company board member?



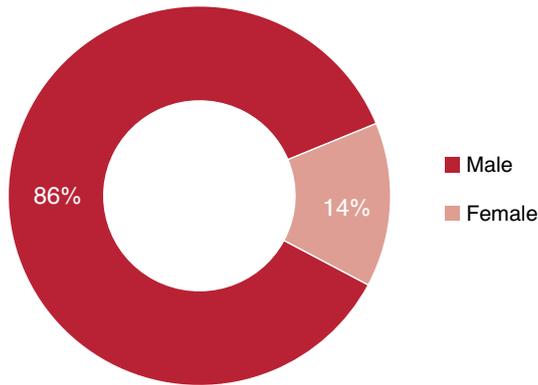
- 44% of our respondents are independent directors on their companies' boards, 42% are non-executive directors and 14% are executive directors.
- 10% of directors are chairpersons of nomination committees and 14% are members of such committees.
- 10% are chairpersons of their boards, while 4% of respondents are senior independent directors.

In the board of directors of your company, you are:



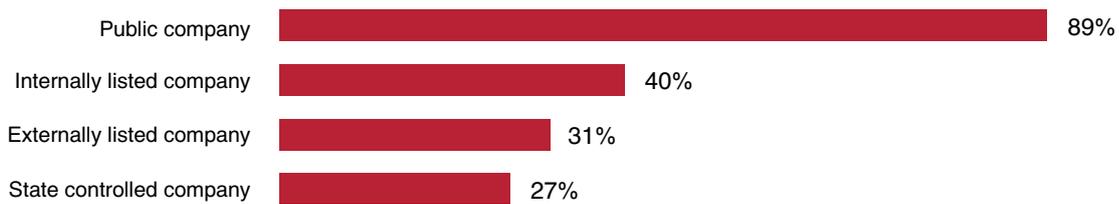
- 86% of directors that took part in our survey are male, while 14% are female.

Respondents' gender:

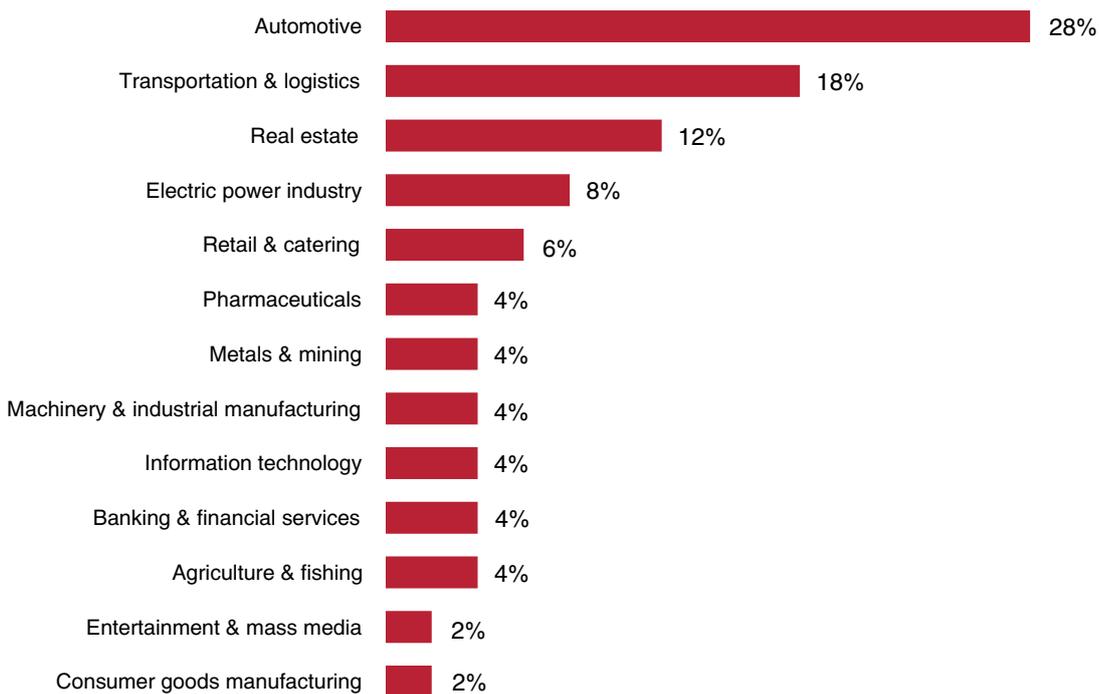


- 89% of our respondents represent public companies, among which 40% are companies listed in Russia and 31% are listed overseas.
- 27% of respondents represent companies under state control (direct or indirect), most of which are public, and one-quarter are also listed.

Companies represented by respondents:



Which of the following best describes your company?



Appendix II: About our interviewees



We have interviewed 10 representatives of Russian boards, including independent and senior independent directors, non-executive directors, as well as executives and chairpersons of boards and board committees:

1. Alexander Berlin
2. Anna Belova
3. Bella Zlatkis
4. David Hexter
5. Dominique Fache
6. Ferdinando Beccalli-Falco
7. Irina Shitkina
8. Sir Robert Margetts
9. Vladimir Gusakov
10. Vladimir Gusev

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The Independent Directors Association was established in 2002 to assist Russian companies to increase the value of their business by implementing the best practices of boards of directors and corporate governance. The main activities of the Association are training and professional development of the members of the IDA, assistance in improving the legislation and regulation of corporate governance and performance standards boards. The association hosts regular training sessions and workshops on the practice of the directors and boards, including international development programs for members of the Board of Directors IoD Chartered Director by assigning an international certificate. The current members of the IDA are more than 600 Russian and international boards of directors and senior executives who are interested in the development of independent directors.