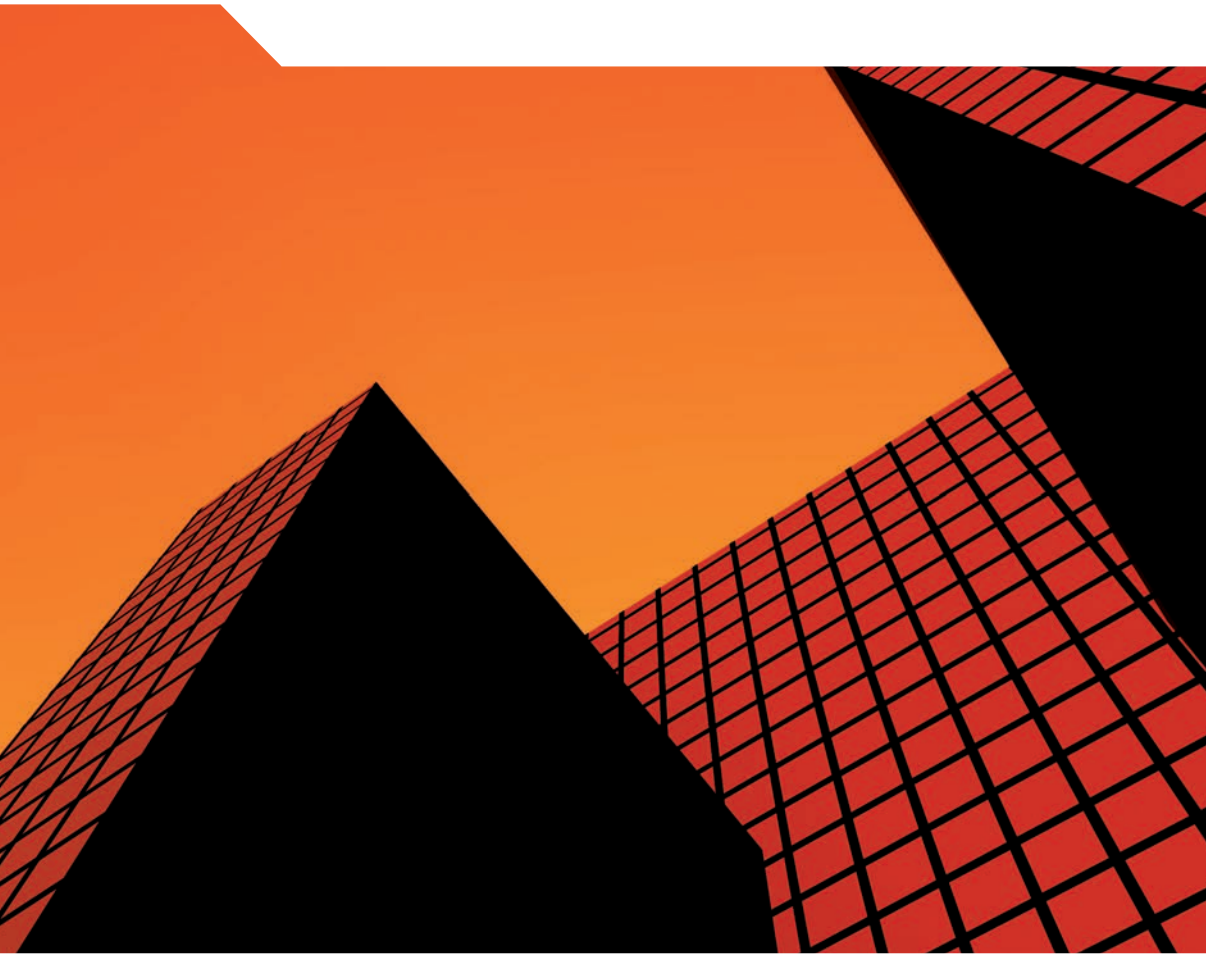
Corporate Governance

Boards of Directors of State-Owned Enterprises

AN OVERVIEW OF NATIONAL PRACTICES



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Foreword

This report provides practical guidance on board practices for directors of state-owned enterprises and identifies a number of "good practices" based on national experiences of a large number of participating countries. It extends the guidance provided by Chapter VI of the OECD Guidelines on the Corporate Governance of State-Owned Enterprises *on the "Responsibilities of Boards of State-Owned Enterprises". The report draws information from a questionnaire-based exercise as well as previous publications and background papers commissioned by the OECD.*

The report is an outcome of the OECD Working Party on State Ownership and Privatisation Practices project on "Enhancing the role of the boards of directors of state-owned enterprises". It was given final approval and declassified by the WP SOPP in December 2012. The draft report was prepared by Sara Sultan and Hans Christiansen of the Corporate Affairs Division of the OECD Directorate for Financial and Enterprise Affairs. Substantive input was provided by Jim Colvin acting as external consultant to the OECD. The development of the report has also benefited from comprehensive consultations with the Business and Industry Advisory Committee (BIAC), the Trade Union Advisory Committee (TUAC), civil society, academia and OECD partner economies.

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Preface

State-owned enterprises (SOEs) are an essential element in the international economic architecture. Across the OECD area and in emerging economies, they continue to dominate certain segments of the economy that matter greatly for the downstream competitiveness (notably in the utilities sector). In the face of growing expectations for improved performance, policy makers have focused their attention on the role of boards of directors.

Boards of directors play a fundamental role in corporate stewardship and performance. Over the last decade, OECD governments have sought to professionalise boards, ensure their independence and shield them from ad hoc *political intervention. In general these approaches have worked; most countries report better quality board discourse and ultimately improved SOE performance. Yet, more remains to be done to raise efficiency by implementing the aspirational standards of governance, accountability and transparency established by the OECD* Guidelines on Corporate Governance of State-Owned Enterprises.

Taking the Guidelines *as a starting point, this publication develops practical guidance on SOE board practices aimed at policy makers and corporate practitioners. The report is based on actual country practices, but it does not limit itself to providing an overview of where we stand today. It takes important steps toward identifying what remains to be achieved. This report does not advocate a one-size-fits-all approach: different national approaches to SOE ownership and oversight are taken into account and their consequences for what constitutes good board practices are considered.*

The Working Party on State Ownership and Privatisation Practices, the OECD body which I have the privilege of chairing, continuously monitors developments in this area. Assisting countries in implementing SOE board practices of the highest possible standard is part of its mandate. This work is by no means limited to OECD membership. The Working Party, in itself and through a number of regional networks across the globe, offers a forum for all interested SOE practitioners to turn to for inspiration and support.

Through this report, I feel that we have taken an important step forward toward identifying strong board practices for state-owned enterprises. I am confident that policy

makers will take steps to undertake relevant measures in this field, and look forward to engaging with a wide range of actors toward the implementation of our findings.

Anders Berg

Chair, Working Party on State Ownership and Privatisation Practices

Deputy Director General, Norwegian Ministry of Trade and Industry

Acronyms and abbreviations

AGM	Annual general meeting
APE	*L'Agence des participations de l'État* (Agency for State Holdings in France)
AUKN	*Agencija za upravljanje kapitalskih naložb Republike Slovenije* (Capital Assets Management Agency of the Republic of Slovenia)
BIS	Department for Business, Innovation and Skills (United Kingdom)
CEO	Chief executive officer
COMU	Crown Ownership Monitoring Unit (New Zealand)
DSP	*La délégation de service public* (public service delegation contract)
EU	European Union
GBE	Government Business Enterprise
GBPFAU	Government Business and Private Financing Advice Unit (Australia)
GCA	Government Companies Authority (Israel)
HSHC	Hungarian State Holding Company
IA	Independent Assessor
LLC	limited liability companies
NZSC	New Zealand Securities Commission
PhD	Doctor of Philosophy
OCPA	Office of Commissioner of Public Appointments
OECD	Organisation for Economic Co-Operation and Development
OSD	Ownership Steering Department (Finland)
SEP	*Sistema de Empresas* (Public Enterprise System of Chile)
ShEx	Shareholder Executive (United Kingdom)
SOE	State-owned enterprise

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Executive summary

This report summarises the practices of governments in OECD and other countries in dealing with the boards of directors of state-owned enterprises (SOEs). Focusing on non-executive directors (or supervisory boards), it draws from relevant OECD publications since 2005 and a recent questionnaire-based exercise answered by delegates and observers to the OECD Working Party on State Ownership and Privatisation Practices. The report is organised in seven chapters summarised as follows. Each chapter identifies a number of "Good Practices" drawing on national experiences and annotations to the *OECD Guidelines on Corporate Governance of State-Owned Enterprises* (the "*SOE Guidelines*"). To assist the reader, these practices are highlighted in the box below.

The Role of boards of directors. Boards play a central function in SOE governance. It carries the ultimate responsibility, through its fiduciary duty, for performance. The board acts as an intermediary between the state as a shareholder and the company and its executive management. This three-layered approach, which is consistent with company laws of most countries, has been implemented by a number of governments to good effect. SOE boards have shifted as oversight bodies entrusted with compliance toward driving performance and setting strategy. However, in a minority of countries SOE boards are not adequately empowered to assume such a role, circumvented by direct ministerial appointments of executive management and/or are bypassed through informal channels of communication and instructions. This may detract from the value-adding of boards.

Procedures and practices for board nomination and appointment. The nomination of SOE directors is in almost every case a government responsibility. According to ownership structures (centralised, widely dispersed or dual structures involving two ministries) this may rely on individual ministers or the entire cabinet and/or executive powers. In exercising these powers, ministers should be mindful that they are custodians of the public interest rather than owners of companies. The process should be rules-based and overseen by a governmental ownership function (which could be central, co-ordinating or placed within a ministry). Insofar as the ownership function has discretionary powers, it is well advised to exercise them along private sector practices. This could rely on external recruitment consultants, databases of pools of directors and involving the incumbent board. Where SOEs have minority non-state

Summary of good practices

Role of boards of directors

- The board plays a central function in SOE governance and should act as an intermediary between the ownership function and the SOE's executive management.
- The role of the board should be clearly defined and founded in legislation, preferably according to general company law.
- The role of the board of directors should focus on strategic guidance and corporate performance, and shift focus away from a traditional "conformance" role.
- The state should inform the board of its objectives and priorities through proper channels to ensure the board maximum autonomy and independence.

Nomination framework and practices

- A robust nomination framework is one that clearly specifies the nominating power is transparent and is consistent in its application.
- Ministerial or executive powers normally have the ultimate responsibility for nominations. This brings legitimacy to the process, but it should not undermine the role of the ownership function.
- Where feasible, board appointments should be subject to co-ordination or consensus on a whole-of-government basis.
- Board appointments, even in wholly-owned SOEs, should be entrusted to the annual general meeting of shareholders
- Establishing a transparent and consistent method to identify applicants from a wider pool of talent will improve board composition and bring uniformity in the assessment process.
- Specialised bodies in charge of advising or accrediting the nominations can bring further objectivity and transparency to the nomination process.
- The Board should be involved in the nomination process in an advisory capacity.
- Mechanisms should exist to facilitate non-government shareholders' participation in the board nomination process.

Board composition

- Persons directly linked with the executive powers should not sit on SOE boards. Other state representatives should be nominated based on qualifications, subject to specific vetting mechanisms.
- Independent directors should be independent from management, government and business relationships. Specific safeguards should be established to verify that nominees comply with requirements.

Summary of good practices *(cont.)*

- Employee representatives can enrich board discussion; the appointment process should ensure that such persons are qualified, as well as representative of the SOE's staff.
- Certain eligibility requirements may be needed, but good practice increasingly relies on tailored approaches to identify the right mix between skills, experience and personal characteristics.
- For all other than direct ownership representatives, relevant commercial or financial expertise is viewed as essential qualifications.
- Reasonable limits on maximum number of board appointments are important to ensure that directors have sufficient time to carry out their duties.
- Diversity preferences may add value to boards, but should not rise to the level where the ability to attract candidates with the right skills and capabilities is imperiled.
- Restricting board membership to nationals should be limited to cases where there is a demonstrated need for such rules, considering that it can act as a barrier to attract the right talent.

Training and induction

- Induction programmes should match the needs of each board. They should serve as a way to improve effectiveness of board members.
- General training for boards of directors should not be a formal requirement; however, on-going professional development should be encouraged and supported.

Remuneration

- Board remuneration should reflect the market conditions to the extent that this is necessary to attract and retain highly qualified directors.
- Remuneration policies of civil servants serving on SOE boards should be carefully considered to ensure the right incentives.

Boardroom efficiency

- The key to the board efficiency is a Chair who can build an effective team by exercising leadership, diplomacy and a deep understanding of the business.
- Specialised committees can contribute to the efficiency of the board, but should not detract from the responsibility of the full board.
- Board committees should be made up of independent and technically literate board members to ensure efficiency.

Summary of good practices *(cont.)*

Board evaluations

- Board evaluations should favour focus on performance of the board as an entity. They should not be limited to "box-ticking" exercises.
- The use of external facilitators can be useful to structure the discussion of board performance.
- Well structured board evaluations can act as a helpful tool informing the nomination process.

investors, their adequate board representation should be ensured. Cumulative voting occurs but is relatively rare. In many countries formal arrangements (including through legal provisions or corporate bylaws) safeguard minority representation, or the state engages in shareholder agreements.

Constraints and guidelines for board composition. A central recommendation is that SOE boards should exercise "independent and objective judgment". SOE boards are usually composed of a mix of civil servants, other individuals tasked with pursuing the public interest and "independent" directors. The trend, fuelled by growing commercialisation of SOEs, is toward greater reliance on independent directors and persons with relevant commercial experience. The recruitment process should be based on eligibility rules and appropriate vetting mechanisms (i.e. nomination committees) before the ultimate decision of ministers. Many countries limit the number of board positions while promoting board diversity. Employee representation on boards generally follows private sector practices, but can differ for some SOEs.

Training and induction. In all countries board induction is provided to new directors, in some cases mandated (and arranged) by the ownership function, in other cases organised informally by SOEs. Education and continuous training of board members is considered good practice, especially where public officials are nominated. Countries with professionalised boards nominate directors who are in little need of further training. Where offered it is mostly "off the shelf" training by institutes of directors and not materially different from what is offered to boards of private enterprises.

Remuneration of directors. In most countries, the remuneration of SOE board members falls below market levels for the competencies and experience required. As a general rule, governments tend to limit the remuneration and incentive awards of both executives and directors. Some countries seek to align pay with market rates, but not be market leading; others are considerably more restrictive. The models used are: *i*) limiting remuneration to an attendance fee per board meeting; *ii*) capping directors' remuneration at

a multiple of average salaries in the SOE or the national economy; and *iii)* developing a "fee policy" taking into account factors such as the size of SOEs, time requirements and formal qualifications. Some countries may have problems attracting talent to boards because of lower remuneration; in others, qualified directors agree to sit on SOE boards for non-pecuniary benefits such as prestige, and useful experience and networking opportunities.

Boardroom efficiency. As SOE boards become more "professional", the issue of boardroom efficiency moves to the forefront. A well-functioning board is responsible for setting strategy, value creation, and acting as a collegial entity with shared responsibility. It has become important to identify directors fulfilling demands for skills and competencies. Therefore, the board size has shrunk, the role of directors as "team players" has grown and, the role of the chair has been strengthened. However, it has also led to an increase in the workload and time commitment, which has in some cases posed challenges in recruitment and remuneration.

Board evaluations. Regular board evaluation is considered good practice. It serves to assess and improve the board's *modus operandi*, and provide the Chair and ownership function with valuable information concerning possible changes to board composition. Country practices differ in this respect. Administrations that run SOEs relatively close to general government tend to rely on top-down approaches through which the ownership function evaluates the board in light of corporate objectives. In more commercial SOEs the trend is to rely largely on self-evaluations. Evaluations assess the workings of the board as a whole; and some extend to an assessment of individuals. In an increasing number of SOEs, external evaluation is also required. An evolving consensus is that evaluation can feed back into the board nomination process.

Introduction

The importance of boards of directors is well documented in corporate governance theory and practice. Boards of directors play a fundamental role in company stewardship and performance, in determining corporate strategies and monitoring managerial performance. They are subject to duties of loyalty and care and expected to act in the best interest of all shareholders as well as, dependent on national law, the company.[1] OECD governments, acting as owners, have increasingly looked at the role of boards with the aim of improving the governance and performance of their state-owned enterprises (SOEs), while also strengthening the State's responsibility to exercise its ownership functions.

The widespread "commercialisation" of SOEs in recent decades has induced governments to take action to professionalise boards of directors and give them greater powers and autonomy. This includes shielding boards from ad hoc political or politicised intervention and ensuring independence in decision-making. Another important step has been to pay closer attention to the composition of the board to ensure the right mix of skill and experience to achieve company goals. These approaches have apparently worked. Countries which pursue these strategies report a better quality of board discourse, more professional boards, and ultimately improved SOE performance. Furthermore, better boards seem to protect governments from operational missteps, political fallout, and allow them to better gauge and manage the risks of operating an enterprise in a commercial environment.

Yet, even where governance reforms have shown good results, expectations of SOE boards continue to grow. These expectations emanate from governments, public and financial markets and the SOEs themselves. Even in countries that have long operated under the core expectation that SOEs will act commercially, the demand for better performance persists. One of the key differences between the function of a board for a state-owned and other enterprise is the fact that the State is usually different to other types of shareholders. Its priorities may be other than a return on shares, including delivering on public policy objectives (OECD, 2011). As such in order to help the board work effectively, the State's policies should be explicitly acknowledged in the boardroom, along with the obligation of directors to meet those policy

objectives, especially where policy objectives are not consistent with profitability.

This report seeks to shed light on good practices in SOE boards drawing on the *OECD Guidelines on Corporate Governance of State-Owned Enterprises* (the "*SOE Guidelines*", OECD, 2005) and national practices. For this reason, each chapter is organised around relevant guidance and corresponding annotations to the *Guidelines* (mostly Chapter 6, which deals with SOE boards) which are indicated in shaded boxes throughout the text. It is further supported by examples of national practices which are indicated in transparent boxes throughout the text. The report is organised around seven chapters, examining: *i)* the role of boards of directors in a SOE; *ii)* board nomination framework and practices; *iii)* constraints and guidelines in the composition of boards; *iv)* board training and induction; *v)* board remuneration; *vi)* boardroom efficiency; and *vii)* board evaluations.

The analysis in this report is limited to practices related to non-executive directors. For jurisdictions with a two-tier board structure, the focus is on supervisory board members. The report seeks to interpret non-executive director widely and include any ex-officio directors, and directors for the State, but it does not concentrate specifically on these issues. The focus is on fully incorporated SOEs (joint stock or limited liability companies) that are not listed on stock exchanges. Listed companies are not considered in detail, on the basis that their board practices will mostly be consistent with listed private sector companies.[2]

The report is relevant for all institutions and individuals that are involved in SOE governance, ranging from the government a whole, the ownership Ministries or ownership function, and the SOE management function. It can also serve as a useful reference point for board members themselves. The report is based on earlier research by OECD supplemented by a questionnaire-based gathering of evidence which took place in the first half of 2012.[3] The respondents included delegates and observers to the OECD Working Party on State Ownership and Privatisation Practices, as well as participants in the Asia Network on Corporate Governance of State-Owned Enterprises. Responses were received from the following 31 countries: Australia, Austria, Belgium, Brazil, Canada, Chile, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Israel, Italy, Korea, Latvia, Lithuania, Malaysia, Mexico, New Zealand, Norway, Pakistan, Poland, Portugal, Slovenia, Sweden, Switzerland, Turkey and United Kingdom.[4] The findings, by country and topic, are summarised in a collection of overview Tables in Annex A.

Readers need to keep in mind that board practices are significantly influenced by the ownership and legal structure of the national SOE economies. The underlying assumption in many jurisdictions is that

incorporating SOEs accordingly to ordinary company law and the further listing of SOEs can lead to more transparent board practices. Nevertheless, good practices cited in this report depend, *inter alia*, on legal traditions, administrative capabilities and board structures, that all vary across jurisdictions and over time. As noted by the *SOE Guidelines*, what matters for outcomes is the consistency of the overall framework, with many different constellations of good policy "choices" being functionally equivalent. What appears to be a "good" practice must be seen in the overall context. To help the reader, such practical guidance in the form of "Good Practices" is suggested (highlighted in bold) throughout the text.

Notes

1. Some corporate legislation stipulates a board fiduciary duty solely toward the owners, whereas other extends this duty to the company as well. The *OECD Principles of Corporate Governance* recommends the latter approach (Principle VI.A).
2. Board practices in listed companies are the subject of a number of recent OECD reports; see OECD (2011) and OECD (2012).
3. The national practices cited in this report are in large part based on an initial stocktaking report drafted by Mr. Jim Colvin acting as external consultant to the OECD.
4. Australia submitted a partial response. Some aspects of SOE boards in Russia are covered in a forthcoming *OECD Working Paper*, see Kostyleva and Lehuedé (2012).

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Chapter 1

The role of boards of directors

The overall directions of SOE Guidelines *imply that boards play a central function in the governance of SOEs. The board carries ultimate responsibility, including through its fiduciary duty, for SOE performance. In this capacity it acts essentially as an intermediary between the state as a shareholder, and the company and its executive management. This three-layered approach, which is consistent with general company laws of most countries, has been implemented by a number of governments to good effect. SOE boards shifted from their historic role as oversight bodies, entrusted with ensuring compliance toward driving performance, to setting strategies and co-operating with management towards their implementation. However, in a minority of countries, SOE boards are not adequately empowered by their governments to assume such a strategic role, circumvented for instance by direct ministerial appointments of corporate executive management and/or informal channels of communication and instructions. This may detract from the value-adding of boards.*

The *SOE Guidelines* recommend clarifying the roles of the State, ownership entities, boards and management. The aim is to assign decision-making powers to those who are most capable, and to segregate decision-making from ownership responsibilities in order to avoid conflicts of interest and disincentives. Clarifying these roles further ensure that decision-making is made on a rational and informed basis, and in line with stated objectives.

This chapter focuses on defining roles and responsibilities for a well functioning board, to some extent, therefore, plotting some ideal outcomes that the good practices identified in Chapters 2 to 7 should help to achieve. It examines various ways in which the board itself can be structured. It also looks at the extent to which the board is involved in conformance versus performance, and how it adds overall value to the performance of the company.

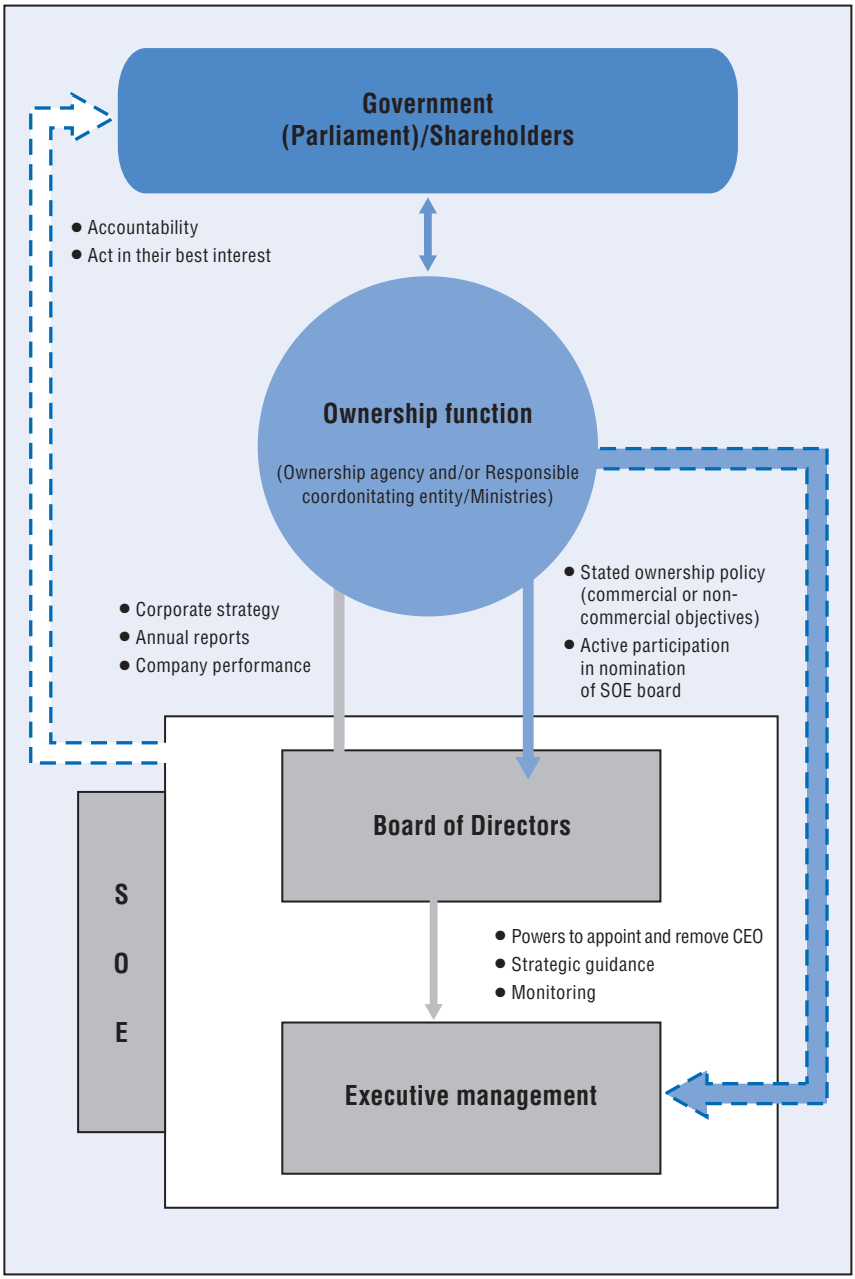
Defining roles and responsibilities

The overall directions of *SOE Guidelines* imply that the board plays a specific function in a governance structure essentially involving three layers, each with a distinct role. As demonstrated in Figure 1.1, the State ownership function is responsible for defining and communicating an ownership policy, overall "expectations" and company-specific objectives to the SOEs it oversees.[1] The board of directors is charged by the State with overseeing the development of a strategy to achieve the objectives, and to monitor progress. It is ultimately responsible for the company's performance toward State and non-State stake- and shareholders. The executive management in most cases propose a corporate strategy for the board's approval, though in a minority of cases strategies may be imposed top-down. In any case, the executive management is accountable to the board for implementing the strategy.

Under this ideal schema, the board plays the central function in the governance of the SOE. It carries the ultimate responsibility, including through its fiduciary duty, for SOE performance.[2] For this, it needs the authority, autonomy, and independence to make decisions that determine performance. It acts essentially as the intermediary between the State, as the Shareholder, and the executive management/company. According to OECD recommendations it has a duty to act in the best interest of both.

In the case of wholly-owned SOEs, the owner and shareholders are essentially the same, but the board still has a duty to act in a way that represents both the "owner's" interests, (i.e. the ownership function) and the

Figure 1.1. **The role of the board in a three-layer governance structure**



shareholders interest (i.e. the general public – assumed to be represented by government/parliament). Board members must act in a way that does not compromise their duty of loyalty to both interests. In the case of listed companies it may also apply to other shareholders that hold a stake in the company, including minority shareholders.

Good practice: The board plays a central function in SOE governance and should act as an intermediary between the ownership function and the SOE's executive management.

A number of countries have implemented this model to good effect, including those which have corporatised their SOEs along the lines suggested by the *SOE Guidelines* (i.e. fully consistent with general corporate law[3]) and subjected them to a competitive environment. For SOEs that operate on a fully commercial basis best practices for boards are arguably quite indistinguishable from those applied to private companies.[4]

The role of the boards according to the *SOE Guidelines*

The role of an SOE's board of directors according to the *SOE Guidelines* follows as much from concerning the State's role as an owner as from concerning the role of the board. The fundamental recommendation concerning the role of the board *vis-à-vis* the ownership entity is to ensure its independence, autonomy and authority.

Guideline II.C: The state should let SOE boards exercise their responsibilities and respect their independence.

In most countries many of the functions and responsibilities of boards are defined by company law requirements. The extent of these responsibilities vary from country-to-country but can include strategic monitoring of the company, development and reviewing the organisational strategy, negotiation with shareholder ministries of the business plan and objectives, monitoring executive management performance and sometimes compliance-checking.

Good practice: The role of the board should be clearly defined and founded in legislation, preferably according to general company law.

However, in a considerable number of countries the respective roles of the Board and the ownership function remains a bit blurred. In some jurisdiction the ownership function may be more or less involved in aspects of strategic management, as well as in the appointment of the CEO and succession planning and executive remuneration and incentive schemes. Good practice suggests that most if not all of these responsibilities should fall within the competency of the board.

It is important to have clearly defined roles for the board, especially *vis-à-vis* the ownership function, to ensure the most efficient use of resources, effective allocation of responsibilities and accountability in the performance of the enterprise. In addition, it ensures that the competency of the board is put to full use.

Conformance vs. performance

The question of "conformance versus performance" refers to the two principal ways that boards may view their roles, as bodies that: 1) focus on conformity with rules and compliance with the directives of the owner, versus; 2) focus on corporate performance. An important aspect in the role of the board of directors is to focus on strategic guidance and performance. This implies shifting a focus away from "conformance" and compliance checking.

SOE boards have traditionally been prone to a greater conformance mentality than private sector companies. This may have origins in direct state control where boards served to ensure that instructions from the state were complied with. It may also emanate from governance traditions where the setting of detailed quantitative performance targets and monitoring achievement against such targets was viewed as the best way to encourage and manage the SOE for results.

Good practice: The role of the board of directors should focus on strategic guidance and corporate performance, and shift focus away from a traditional "conformance" role.

Certainly, the focus on conformance emanates from view that the role of the board is to prevent corporate excesses and political embarrassment from a misuse of public funds. Within the board, a compliance mentality often manifests itself through a preoccupation with the budget setting process and variations from budgets and plans. Often this attention is at the expense of larger issues such as the effectiveness of the overall business strategy. Focusing excessively on conformance can give boards and owners a false sense that they are fulfilling their fiduciary functions.

A visible trend over past decades among both private sector and SOE boards is a greater concern for the drivers of performance. This being said, there are SOEs in both OECD countries and elsewhere where the control environment is still not sufficiently developed for boards to safely shift their focus towards performance issues. Attention to compliance and control is often warranted. The renewed attention to risks and risk management in the wake of the 2008 financial crisis show how important such issues can be. However, concern for a sound control environment is not the same thing as having a conformance mentality. A balance should be struck between focus on performance versus conformance (see related discussion in Chapter 6 on board efficiency).

Adding value

A properly constituted and managed board can "add value" by helping management make better decisions. The characteristics of a value-adding board are: 1) responsiveness to management's need for direction; 2) bringing skills and perspectives that management may be lacking; 3) encouraging the development and examination of a range of options, bearing in mind risks; 4) being objective; 5) encouraging and listening to in-house expertise; 6) looking forward to the future, and taking the long-term view; and 7) thinking strategically. Ultimately, adding value means developing more and better interaction with the executive management, and working in a structured manner with the ownership entity.

One of the most important ways in which boards can add value is to contribute to the strategic orientation of the company. For this, it needs to be adequately empowered by the ownership function to assume its strategic role. Although the ownership function can play a role in encouraging the strategic orientation of the board, it should not impose its views. If for example, the ownership function sets the tone of board discussions, the strategic role of the board may be subjugated (further discussed in Chapter 6 on board efficiency).

Good practice: The State should inform the board of its objectives and priorities through proper channels to ensure the board maximum autonomy and independence.

The State should inform the board of its objectives and priorities through proper channels. Depending on the SOE and country practices, in some cases this is an iterative process in which the SOE and the State, via the ownership function, respond to proposals and jointly develop the strategy. In other cases, high level outcomes or expectations are defined by government, usually the ownership function, and a strategy is developed by the board and management to achieve these outcomes. Regardless of the method, going through proper channels will raise transparency and accountability, and avoid compromising the board's fiduciary duties.

Worst-case examples in this respect arguably involve cases where directly appointed CEOs take instructions directly from political circles, circumventing the board of directors and leads to a significant weakening of corporate (and public) governance. Another case to be avoided, as much as possible, is the appointment of a small number of "directors for the State" who act as custodians of the government interest from within the boardroom. The relevant decisions need to be made by, or communicated to, the board of directors, acting as a unit.

The proper fulfilment of the role of the board *vis-à-vis* the ownership function and executive management is in practice closely linked with the process by which board members are nominated, the profiles of board

members themselves, and board composition. Ensuring strong nomination frameworks will shield the board from political intervention. So too will a board that is comprised of persons who display adequate leadership and the right mix of skills and competencies to ensure strategic guidance. These issues are covered in Chapters 2 and 3, respectively.

Notes

1. "Ownership function" may refer to a centralised ownership agency, a co-ordinating entity and/or responsible ministry(ies) in charge of ownership of individual SOEs.
2. Fiduciary duty is commonly defined as a combination of duties of care and loyalty. According to annotations to the OECD Principles for Corporate Governance, the duty of care requires board members to act on a fully informed basis, in good faith, with due diligence and care. Whereas the duty of loyalty for a board member relates to the company and equitable treatment all its shareholders, remuneration policy for executives and board members, monitoring of related party transactions, etc.
3. This is commonly the case where SOEs are incorporated as joint stock or limited liability companies. However, in some jurisdictions key provisions of company law are effectively countermanded by special SOE legislation, in which case they could arguably no longer be characterised as "fully corporatised".
4. Where companies are listed on the stock exchange this is even more true. Even where the State remains the controlling shareholder, the need to comply with listing and maintenance standards (including disclosure requirements and governance codes) as well as securities laws and regulation, is usually instrumental in empowering boards of directors.

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Chapter 2

Board nomination frameworks and practices

The nomination of SOE directors is one of the primary responsibilities of the state as an active owner. According to ownership structures (centralised, widely dispersed or dual structures involving two ministries) this may remain with individual ministers or involve the entire cabinet and/or executive powers. In exercising these powers, ministers need to be mindful of the fact that they are custodians of the public interest rather than the owners of companies. The process should be rules-based and overseen by a governmental ownership function. Insofar as the ownership function has discretionary powers, it is well-advised to exercise them along similar lines and private sector good practices. This could include relying on external recruitment consultants, building databases with pools of directors and engaging the active involvement of the incumbent boards of directors. Where SOEs have private sector minority investors, processes are usually in place to safeguard the minority representation.

According to the *SOE Guidelines* the starting point for effective SOE boards is to ensure a well-structured and transparent policy nomination framework. This can be ensured by enshrining formal processes that are transparent (and, to the greatest extent possible, predictable), shields the board from ad hoc political intervention, and at the same time assuring an adequate degree of flexibility to ensure the long term success of the board and company. Overseeing the board nomination process is among the primary responsibilities of the ownership function.

However, achieving this in practice is far from uncontroversial. Historically, the nomination of SOE boards has proved to be one of the more contentious policy challenges in SOE reform. Politicisation of the appointment process (e.g. for patronage or to protect special interests served by the SOE's operations) in some jurisdictions, remains an impediment to consistent and transparent process. The formal role of ownership entities has been undermined by different Ministries or interest groups inside and outside the companies.

Political interference in the nomination process has in the past led to inefficient outcomes in the long term, resulting in excessive turnover, a lack of desired profiles on the board, or even stagnation due to lack of fresh faces or innovative persons (Frederick, 2011). Political intervention in the nomination process can undermine competition and the legitimacy of the recruitment process.

SOE Guidelines, Guideline II.F on board nomination processes

According to the *SOE Guidelines*, one of the primary responsibilities of the State as an active owner is to:

II.F.2. Establishing well structured and transparent board nomination processes in fully or majority owned SOEs, and actively participating in the nomination of all SOEs' boards.

Like any private company owner, the State acting in its capacity as shareholder needs to form ideas about whom it wants on the board to act in its own and the company's best interest. However, as mentioned earlier, unlike the private sector Ministers are not the "owners" of SOEs. The challenge is to avoid excessive politicisation and to base decisions on clear rationale and

justification. This can be ensured by putting into place an authority that will formally exercises, oversee or audit the nomination process, and to warrant a formal, competitive and transparent recruitment process that avoids ad hoc interventions or deviations from the (formally) stated procedures. That said, there is probably no way to entirely shield the board form some degree of political overlay.

Good practice: A robust nomination framework is one that clearly specifies the nominating power; is transparent; and is consistent in its application.

The key elements of a robust nomination framework will include clearly specifying the person or body responsible for nominating board members; being transparent about any qualifications that may be required, or guidelines that exist on appointments; and pursuing a consistent approach across all SOEs. Ultimately countries which follow a robust nomination framework report that they have that had the best possible outcomes in terms of finding qualified people for the job.

Robustness and transparency do not necessarily dictate formality. The level of formality will vary according to the level of commercialisation and corporatisation in addition to the stake in ownership (i.e. whole or partial ownership). It will also depend on institutional factors linked to the jurisdiction, in particular as they relate to centralised or decentralised ownership structures. The remainder of this chapter explores these issues starting from country practices concerning who formally exercises the nomination power. It examines the role of the ownership function, and contestability in the nomination process. It examines the tools that are used by ownership functions to identify suitable candidates, and the roles of the board and shareholders in nomination processes.

Exercising the nomination and appointment powers

According to the *SOE Guidelines* one of the primary responsibilities of the State acting as an owner is to participate actively in the nomination process. However, practices differ radically across jurisdictions. The right of nomination is almost invariably exercised by the relevant minister, or through some form of inter-ministerial process. Ministerial/Executive involvement in the appointment process is usually a requirement of the legal structure. It has the advantage of providing political legitimacy to the appointment process. The exact format that the Minister/Executive carries out this function is largely dependent upon the ownership model adopted (i.e. centralised or decentralised), and depending on the level of the State's stake in the company.

Good practice: Ministerial or Executive powers normally have the ultimate responsibility for nominations. This brings legitimacy to the process, but it should not undermine the role of the ownership function.

There is a fairly clear distinction between those jurisdictions that have centralised ownership, for instance through an ownership agency, and those that do not. In the former, one minister usually is in charge of the ownership function, and in the case of highly commercial SOEs usually is in charge of board nominations. Where SOEs are subject to sector interest (and sector regulation) it is more likely for the nomination process to be co-ordinated across government. In some cases, wider vetting by a group of ministers, the Cabinet, or Head of state to confirm the nomination decision is required in a consensus-based nomination process. In other cases, there may be an actual carve-up of the right to make board nomination across the Cabinet.

The latter system operates in both Braziland Turkey, where the central minister nominates one member, with the rest nominated by the sector Minister. In Estonia, the sector minister is responsible for half of the appointments to the Board, with the remainder appointed by the Ministry of Finance. Involving different ministries in the appointment process may lead to more diverse Boards, with a variety of skills and experience. However, the key risk with having the power of appointment between ministries is that it can lead to representative Boards, i.e. where board members see their principal role as being to represent their appointing ministry and their respective political interests, rather than owing their duties to the company as a whole.

A more unusual form of centralisation of the ownership function is found in a few jurisdictions, where the power of nominations has been formally devolved to the ownership entity (Chile and Slovenia). However, recent experience indicates that this legal construct may in practice not be sufficient to shield the nomination process from political interventions, which – if confirmed by fact – could lead to a loss of transparency rather than a gain in board independence.

Where ownership is vested with individual ministries (which in countries with strongly corporatised SOE sectors applies mostly to companies with strong non-commercial orientations) the relevant ministers are usually solely responsible for nominations, though parts of general government responsible for public finance may sometimes retain the right to appoint a representative to the board. In the case of dual ownership models, line Ministries share the appointment powers with a central ministry (typically the Ministry of Finance). In actual practice, this may take either of the following forms: *i*) each Ministry is attributed the powers for nominating a certain number of directors; *ii*) each director has to be nominated by consensus between the involved ministries. Where consensus is called for, co-ordinating agencies (such as COMU of New Zealand – see below) may play a central role in the process.

Good practices suggest that ministerial decisions concerning nominations should be subject to some form of consensus by a wider group of ministers, the Cabinet or Head of State, regardless of the formal appointment process. One proponent of this is Sweden, which considers this to be a key feature of their system as it provides for a consistent and widely-supported approach to board appointments: "Each nomination for a state owned company is made in agreement with all four governing parties. A decision by the Government Offices, formally made by the ministry responsible for the governance of the company, and then confirms the nomination decision."

Good practice: Where feasible, board appointments should be subject to co-ordination or consensus on a whole-of-government basis.

Where government is the sole shareholder, nomination and appointment process tends to be one in the same thing, since the government, as shareholder in most cases, will have sole rights to appoint the board (subject to any employee representatives on the board). Ultimately, the power of appointment rests with the Annual General Meeting (AGM) of shareholders. The actual voting of shares in this case is usually undertaken by the relevant entity having the ownership role (i.e. either the central ownership unit, or a sector Ministry, depending on the ownership model adopted) in a minority of cases by an independent body invested with the ownership function. In the case of 100% state ownership, there is a risk that AGMs become considered by the involved government officials as purely a "matter of form". However, where the SOEs operate according to company law (including the filing of AGM minutes with company registries) this is an important source of transparency – including concerning board appointments.

Good practice: Board appointments, even in wholly-owned SOEs, should be entrusted to the annual general meeting of shareholders.

Ministerial involvement in the board nomination process, whilst politically necessary, does potentially weaken a key ownership role from the entity exercising the ownership function and, in doing so, could weaken the direct accountability of board members toward the ownership function. Partly for this reason, a large number of national administrations have put into place methods to reinforce the role of the ownership function in the Ministerial nomination process and to improve the overall transparency. This is considered in the below sub-section.

Identification and selection of board members

Although the legal responsibility for exercising the nomination power usually lies with a Minister, good practice dictates that independent bodies weigh in on the appointment process.[1] The annotations to the *SOE Guidelines* highlight the role of independent bodies can have an impact on depoliticising

board appointments, noting that "even though such commissions or public boards might have only recommendation powers, they could have a strong influence in practice on increasing the independence and professionalism of SOE boards." The actual job of helping identify and select board members is a priority for the ownership function. The ownership function can help to address challenges include being transparent about any qualifications that may be required; developing guidelines on appointments; and pursuing a consistent approach across all comparable SOEs.

Good practice: Establishing a transparent and consistent method to identify applicants from a wider pool of talent will improve board composition and bring uniformity in the assessment process.

When comparing the practices in OECD and other countries, two basic distinctions offer themselves. First, one needs to consider what precise role is assigned to the ownership function to assist (or, as the case may be, check) Ministerial powers in the nomination process. Secondly, ownership functions may use different tools and methods in exercising such discretionary or advisory powers as each of them have. On the first of these issues, national practices can be summarised as follows:

- *Pre-declaration of formal qualification requirements*. A relatively small number of countries have stipulated in law minimum formal qualifications that individuals must possess to be eligible for board nomination. Where such exist they are usually backed by some form of accreditation mechanism attached to the ownership function. In Israel, sector ministers and the Minister of Finance are usually responsible for initiating nominations, but the Government Companies Authority (GCA), nevertheless plays a central role in managing the process. Board appointments are subject to an approval of a special Appointments Examination Committee that confirms that the educational qualifications and further criteria prescribed by the Government Companies Law are met. Similarly, Portugal has recently passed legislation instituting a system of non-binding recommendations by a Committee on Recruitment and Selection for Public Administration.
- *Informal processes to vet or advice on ministerial appointees*. In some countries, a vetting process occurs on a more informal basis. In Australia, the co-ordination agency GBPFAU plays an informal role in advising the Minister on possible board candidates. In the United Kingdom, advice and recommendations are submitted by the Shareholder Executive or sponsoring Department following an open competitive process of selection. All appointments are then made by the relevant Secretary of State based on these recommendations. The arguably most sophisticated model of advice, vetting and ministerial interaction is found in New Zealand. This example described in detail below.

- *Formal or informal nomination committees*. Large SOEs – following a practice also used by a number of listed companies – sometimes have external nomination committees attached to their AGMs. These committees may contain both civil servants and private sector representatives and (in case of mixed ownership) they can be elected by to the AGM. An informal similar structure is found in Sweden, where the board nomination process relies on informal working groups. A working group is set up for each company analysing the current need of expertise on the basis of the company's operations, current situation and future challenges as well as the board's composition. Recruitment needs are then established, after which requirement profiles are produced and the work of recruitment starts with looking for suitable candidates. Preparatory work is then done on these candidates and the acceptance of the government needs to be obtained. As mentioned, the unique approach followed by Sweden is that government decisions are taken on a consensus-based approach to ensuring that the decision reflects a collective government decision.

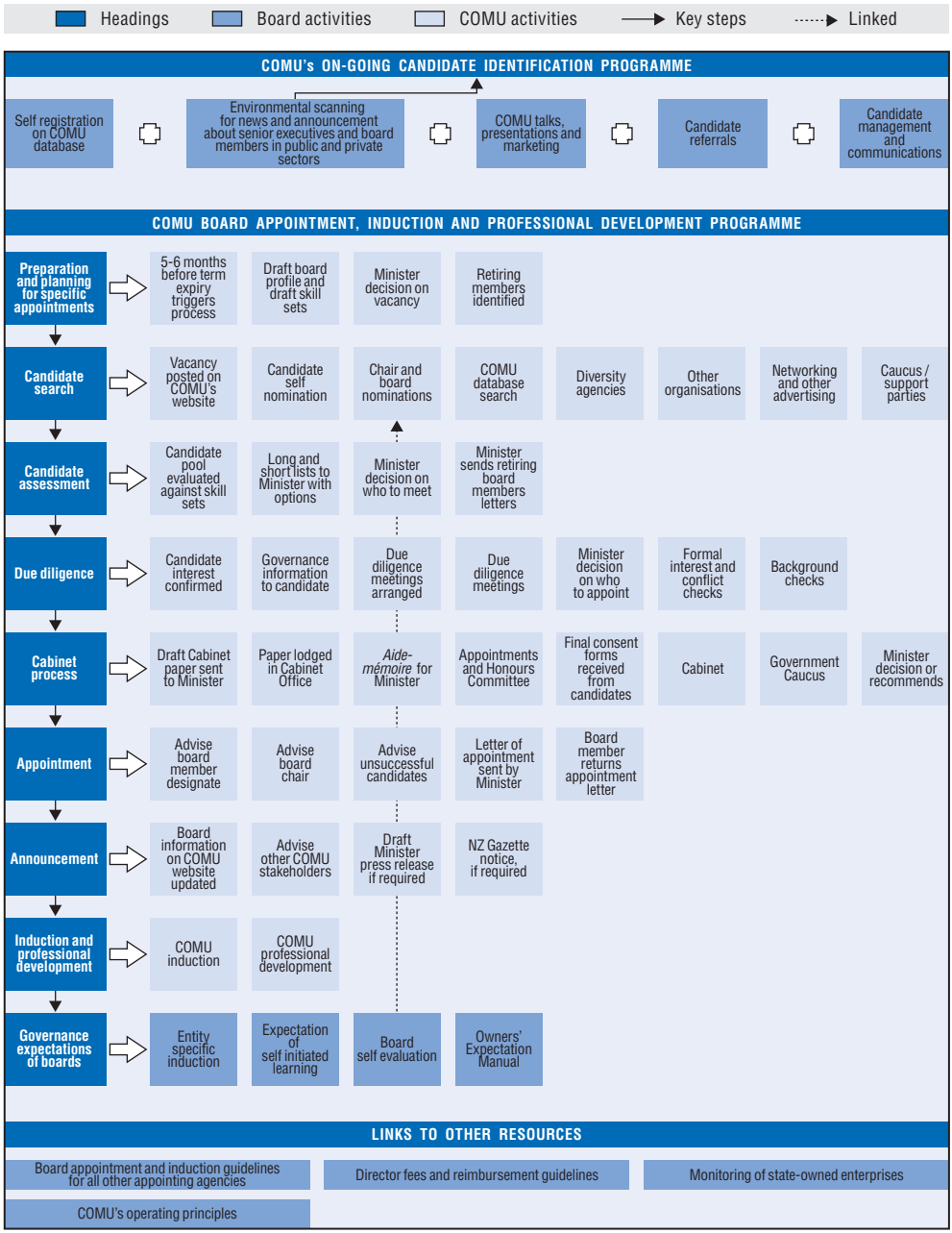
Good practice: A specialised body in charge of advising or accrediting the nominations can bring further objectivity and transparency to the nomination process.

New Zealand operates a dual ownership model but with a centralised ownership support unit, the Crown Ownership Monitoring Unit (COMU). It has adopted a comprehensive approach to board appointments, from soliciting, vetting and recommending candidates through to conducting induction training after an appointment has been made (Figure 2.1). COMU manages this process by advising the bodies responsible for appointment (i.e. the Minister after approval by a Cabinet Appointments and Honours Committee, and confirmation by Cabinet). It is responsible for developing a long and short list of candidates (with options) for consideration by the minister; conducting due diligence on preferred candidates (including conflict of interest clearance, background checks); managing the cabinet approval process; and managing the formal appointment process.

"Tools" available to the ownership function

As mentioned, different ownership functions have varying degrees of influence on the board nomination processes. Within such discretion, they employ a wide variety of tools to identify potential board members. Some jurisdictions have adopted gatekeeper arrangements to provide a clearing house for applications, enabling applicants to be considered from a wide variety of sources but nevertheless subject to a uniform assessment process. Where a centralised ownership unit has been established, it is common for the unit to have responsibility for soliciting/receiving applications and then vetting these applications against any pre-determined qualification criteria.

Figure 2.1. **New Zealand board appointment process**



The methods employed usually aim to improve the processes used to ensure that the nominating body had access to a wide pool of available talent; facilitate open access by prospective applicants to the nomination process; bolster the role of the board in advising on potential nominees or on skills needs of the board; and reinforce the role of the ownership function in the process. The methods applied in different countries include:

- *Pools of directors.* The establishment of a pre-qualification mechanism for SOE board members based on a formal evaluation of interested candidates. Such systems can be based on a mechanism for self-nomination by persons interested in serving on SOE boards. In some countries this has been formalised in the form of a "directors' pool" from which new external directors to SOEs are drawn. In France, this pool is managed by the ownership function; whereas in Malaysia pools of candidates are held managed by the private institute of directors.
- *Recruitment professionals.* Reliance on head-hunters and other management recruitment consultants to identify suitable SOE directors among individuals who might not themselves have taken the initiative. The recruitment consultant's role is generally limited to the identification and pre-screening of candidates, as an adjunct to the usual nomination processes. For example in Chile, head-hunters are commonly used to fill Chairmen roles in large SOEs or those facing particular challenges.
- *Reliance of the incumbent board.* Nominations of individual directors are usually based on a "needs analysis" aimed at identifying qualifications that may be in short supply in the incumbent board. The board itself, and in particular its Chair, can play an essential role in this process. This is discussed in Chapter 3.

Finland apparently stands out in regards of modernising its selection procedures. The ownership agency outsources the development and maintenance of a database of pre-qualified candidates to a recruitment consulting firm. The outsourced contract is subject to competitive tender every four years. This arrangement would appear to offer some advantages over maintaining an internal database: it provides access to the networks and resources of the recruiting firm, who have specialist skills in sourcing candidates for private sector boards, especially international candidates; it reduces the risk of political involvement in the selection process; and it provides for a cost-effective, transparent and consistent process for dealing with applications received from a wide variety of sources. A solidly structured process which is applied on a consistent basis has proved to be beneficial in avoiding a number of political sensitivities. (Box 2.1)

Box 2.1. **Reliance on recruitment management consultants in Finland**

A bidding contest

A bidding contest is arranged to hire a suitable executive search company, on the basis of four year consultancy contracts, in order to identify additional candidates. The justification of going with executive search companies is their profound database with suitable profiles. The bidding contest is run in the same way as any small public procurement, invitations are sent to five or six consultants and the most appropriate offer is selected. The contract is based on a fixed annual fee.

Resource bank

The consultancy is responsible for developing a Resource Bank, with suitable candidates are added to a pool of candidates based on the criteria set by the Ownership Steering Department (e.g. professional distinction, etc.). New candidates are added to the pool on a regular basis. The Ownership Steering Department also reserves the right to propose candidates whereby they are included according to the same systematic scrutiny applied by candidates identified by the consultancy. To complete the selection process, personal interviews may be conducted.

Selection from the pool of candidates

The Ownership Steering Department, based on its portfolio of companies, identifies a list of positions for which new candidates are needed. It also defines the particular qualities required from candidates for each position. These requirements are communicated to the consultant. Following this meeting, the consultancy will present a short list of candidates for each position. A company-by-company sorting process occurs, until two or three candidates are identified for each position taking into account the background, qualities and the capabilities as well as potential conflicts of interest of each candidate. A decision is made on the short list by the Ownership Steering Department following a proposal made to the AGM of each company.

Source: Finnish authorities' response to OECD questionnaire.

The role of the board in nomination

According to the annotations to the *SOE Guidelines*, the board should be able to make recommendations to the ownership entity concerning board recruitment. The *Guidelines* further suggest board nomination committees as a means to better identify candidates.

Listed SOEs have to follow listing and maintenance requirements, which in many countries include corporate governance stipulations requiring that the

SOE Guidelines, Annotations to Guideline II.F.2 on the board nomination process

Annotations to Guideline II.F.2: "SOE boards should also be able to make recommendations to the ownership entity based on the approved board member profiles, skill requirements and board member evaluations. Setting up nomination committees may be useful, helping to focus the search for good candidates and in structuring further the nomination process."

board makes the nomination decisions. The benefits to including the board in the decision making process is that the board knows the type of profile and talent it needs to complete the team. Internal board nomination committees help to filter candidates with final approval with the full board. This would arguably constitute a good practice for SOEs in general – whether listed or not. Currently, however, the use of board nomination committees and the formal involvement of the board is not common practice. Nevertheless, a number of countries have put into place processes that follow good practice supported the by the *SOE Guidelines,* some of which are summarised in this chapter.

In Canada, there is a formal process requiring Boards to establish and maintain board profiles, a process that seems to align practices with the recommendations of the *SOE Guidelines*. When a vacancy arises, the responsible minister for nominating a candidate (and his or her staff, with the support of his or her department) will be guided by the board profile developed by the board of directors to identify potential directors for appointment. The use of board profiles in Canada is described in more detail in Box 2.2.

The United Kingdom also has a process which formally involves the board of the SOE in the recruitment and selection process at various stages. The Shareholder Executive (the government's co-ordination entity) and the SOE Chair agree on the mix of skills and experience required on the board leading to agreement on a strategic plan of public appointments. A timetable for recruitment is then agreed between the SOE, the lead Director in the Shareholder Executive. For specific appointments, a draft specification setting out the role and requirements for the board appointment is drafted and agreed with the SOE. When interview panels are convened, they will include the Chair (Box 2.3).

Good practice: The board should be involved in the nomination process in an advisory capacity

More commonly the board is involved through informal consultations between the board, or its Chair, and the ownership unit. For instance, in Finland the ownership unit, OSD, consults with the Chair on the board's performance and the skills and attributes required, well in advance of the

Box 2.2. **The use of board profiles in Canada**

The Board of Directors liaises with the responsible minister's office and the portfolio department on all appointment-related issues, including advising the government on selection criteria for Chairpersons, as well as developing competency profiles and future needs for directors to fill upcoming vacancies.

Crown corporations are asked to develop and maintain a Board profile to ensure responsible ministers and their departments have a thorough understanding of the competencies required by the Board as a whole and to identify any gaps in those competencies.

A board profile describes the experience, attributes and skills that should be possessed by the board as a whole. While it may be essential for all directors to possess certain attributes and skills, other specialized skills may be required for one or two directors only. A director profile, therefore, is a subset of the board profile which provides a concise description of a position that contains all the information necessary to fill a vacancy on the board. Board profiles for all Crown corporations are publicly available on the Governor in Council Appointments website (*www.appointments-nominations.gc.ca*).

The responsible minister and his or her department will use the board profile and the director profile to guide them in identifying suitable candidates for consideration for appointment to a board of directors.

Source: Canadian authorities' response to OECD questionnaire.

AGM when appointments are made. Estonia similarly states that there is no formal rule to consult the Chair of the board on the vacant positions, but informal discussions may be held to choose the best possible candidate. In Norway, the board evaluates its composition and functioning, both individually and as a group. These assessments are made available to the nomination committee, to use as one of several sources to identify board's needs/characteristics.

In Denmark (Box 2.4), the nomination of new directors involves the Chair of the Board at all stages in the process. Approximately six months prior to the AGM (which appoints new directors) there is normally a discussion between the Minister/Ministry and the Chair about possible needs to change the board composition. Change may be triggered by resignations, a need to strengthen the board, or to ensure staggered board renewal. The Chair will work with the Minister/Ministry to form a common view on which qualifications and experiences of potential candidates that could strengthen the board's composition (with the aim developing a written profile of the desired competencies of any board of state-owned companies). The Chair of the Board may then propose a

Box 2.3. **Board appointment process in the United Kingdom**

The general Office of Commissioner of Public Appointments (OCPA) recruitment process is as follows (although this may vary slightly depending on the size of the SOE and the specific requirements of the post):

- The central ownership advisory unit, the Shareholder Executive (ShEx) and the SOE Chair agree on the mix of skills and experience required on the Board leading to agreement on a strategic plan of public appointments. A timetable for recruitment is then agreed between the SOE, the lead Director in ShEx and an Independent Assessor (IA).
- A draft specification setting out the role and requirements for the Board appointment is drafted and agreed with HR and the SOE. The role and person specification is then agreed with the body or Minister making the final decision.
- A candidate search is undertaken with the vacant position being publicly announced (i.e. advertised) and often involving the use of recruitment agencies to ensure a more thorough search of potential candidates.
- On the basis of applications received a long list of potential candidates is produced. An initial sift involving ShEx, the IA and the SOE is conducted to produce a short list of candidates to interview.
- An interview panel is established comprising a the lead ShEx policy official, the IA and the Chair of the SOE.
- The panel will then reaches agreement on the preferred candidate and submit a panel report with recommendations to Departmental Ministers.
- Once Ministers have agreed the recommendation the appointment can be made.
- An appointment is normally for a fixed period of 3 years at which point the position is subject to re-election.
- The remuneration of the successful candidate, if over £142k, needs to be agreed with the Chief Secretary to the Treasury.

Where the post is not OCPA regulated, the SOE runs the process but follows the OCPA guidelines in most instances. ShEx is closely involved if the post is important (e.g. CEO or Finance Director) in the process. For example, ShEx will be a member of the interview panel. In this way, ShEx is able to make suitable recommendations to give consent for appointments.

Source: British authorities' response to OECD questionnaire.

number of candidates to the ministry, but candidates may also be sought from other sources.

Box 2.4. **Identifying potential board members in Denmark**

The process to identify board members in Denmark is as follows:

- The starting point for board nomination is normally a discussion between the Minister/the Ministry and the Chair of the board about the need to change the board composition at the next annual general meeting. A need for change can arise because current board members will like to resign, a preference for strengthening the board, a preference for ensuring that board compositions are changed gradually to secure "new blood" and continuity, etc. The initial discussion ideally takes place in the autumn, as the Annual General Meetings takes place in March and April.
- Given a common view of the need to change the composition of a board, the next step is to form a view on which qualifications and experiences of potential candidates that could strengthen the board's composition. Although not fully established yet, it is the aim to develop a written profile of the desired competencies of any board of state-owned companies.
- Based on a joint view on desired competencies, the next step is to identify potential candidates, and – depending on the specific circumstances – it will often be the Chair of the board that proposes a number of candidates to the Ministry, but candidates may also be proposed by the Minister/the Ministry. Recruitment firms may be involved in this process, but it is not typical.
- Based on the actual composition of the boards of SOEs, the vast majority of board members are drawn from the private sector. Some have in the past been either employed in the public sector or been politicians (minister/member of parliament), but all have worked in the private sector at managerial level since resigning from public service.
- Based on the short list, which is presented to the minister, the most suitable candidates (normally 2-3) to a given board post are identified.
- The minister then presents these proposals for the Government's Appointment and Organisation Committee, who agree on which candidate to approach. The approach to candidates is made either by the Ministry or the Board Chair, and it is typical that the Chair interviews the candidate to make sure that expectations between the candidate and the company are aligned. Of course, if a new Chair is to be elected, it is the ministry that may interview the candidate (in particular if the candidate for the chairmanship is not already on the board, and therefore know to the ministry).
- If the candidate accepts the nomination, the Minister then presents a final proposal to the Government's Appointment and Organisation Committee, and if approved can then elect the candidate at the next general meeting.

Source: Danish authorities' response to OECD questionnaire.

In Switzerland, the board has the legal role of proposing the final candidate(s) to the AGM for appointment. For fully-owned SOEs, the Federal Council (executive authority), as the sole shareholder, decides on the nominees. Nevertheless, the board has a strong role in identifying potential nominees. When vacancies arise, the Chair and/or a board committee develop a requirements profile for board members and specifically define the board's needs in new appointments. The board then works with the ownership unit to identify and (pre)evaluate potential candidates. Out of this larger pool a short-list is established in a multistage procedure, commonly supported by an external consultant (head-hunter) and in close contact with the heads of the ownership units.

The relationship with non-state shareholders

The *SOE Guidelines* emphasises the involvement of non-state shareholders' participation in the election of the board. The focus of the Guidelines in this respect is more on preserving the rights of minority shareholders, rather than the more complicated question of how interactions between Government and non-Government shareholders might impact on the quality of boards. On the positive side, the participation of non-state elected representatives might be expected to bring relevant expertise to the board. The need for consensus might also act as a discipline on the quality of Government nominated candidates. Conversely, the processes and mechanisms that moderate the relationship between the shareholders might lead to boards that are factional or representative of particular shareholder interests.

SOE Guidelines, Annotations to Guideline III.D on preserving the rights of minority shareholders

Guideline III.D provides that "the participation of minority shareholders' in shareholder meetings should be facilitated in order to allow them to take part in fundamental corporate decisions such as board election." The Annotations go on to note that "to participate in general shareholder meetings is a fundamental shareholder right. To encourage minority shareholders to actively participate in SOEs general shareholder meetings and to facilitate the exercise of their rights specific mechanisms could be adopted by SOEs […]. These could include […] the possibility to use special election rules, such as cumulative voting."

Good practice: Mechanisms should exist to facilitate non-government shareholders participation in the board nomination process.

The formal mechanisms through which minority shareholders can be guaranteed a board representation differ across countries. In order from general to specific they include: legal provisions in general company law or specific SOE legislation; stipulations in the bylaws of individual state-owned enterprises; and shareholder agreements between the state and the minority investors. They are discussed briefly below.

- *Legal provisions*. At the most primary level, the relevant company laws often provide a voting framework or protections to ensure adequate representation of shareholders. Voting procedures at the AGM provide an opportunity for informal discussions amongst the shareholders to attempt to obtain consensus on board appointments (Slovenia and Poland, for example). In Poland's case, the strong rights afforded to minority shareholders to appoint representatives (by group voting of shareholders cumulatively having minimum 20% of voting rights) seems to be the key factor in promoting dialogue between the shareholders. This, however, seems to be rather an exception: few OECD countries systematically apply cumulative voting rules to their SOEs.) Norway has one of the more structured processes for involving non-governmental shareholders: "The preparatory work for the nomination of board members in listed companies is carried out through separate nomination committees, where the State, in conjunction with representatives of the other shareholders, seeks to achieve the best possible composition of the companies' governing bodies." Further, Norway has a Code requirement that at least two of the members of the board elected by shareholders should be independent of the company's main shareholder.[2]
- *Bylaws and articles of association*. The company bylaws in some countries contain voting procedures that enshrine the rights of the various shareholders and, in doing so, promote a degree of co-ordination between the various shareholders. For example, in Italy, the bylaws of some non-listed SOE's impose a "listing vote system", a form of cumulative voting that ensures that minority shareholders are always represented in the board. Brazil also adopts various voting procedures through the SOE bylaws that guarantee representation for minority shareholders, such as a guarantee of board representation for any shareholder holding greater than 15% of the voting stock. In Turkey, non-Government shareholders have a right to board representation where their holdings are greater than 20%.
- *Shareholder agreements*. The shareholder agreement model is in practice only feasible when the minority shareholders are themselves block-holders, as for example in the case where the government owns and enterprise jointly with a "strategic partner". It is extensively used in countries such as

Denmark, Finland and Sweden where shareholder agreements guarantee each shareholder a right to appoint a certain number of representatives in several SOEs.

Finally, an important point is the question of whether the CEO should be on the board. Under a two tier system the question is moot, but many OECD countries have unified boards. In a unified board, the separation of the role of chair and CEO is viewed as necessary to underscore the separation of oversight and executive functions, but views differ regarding whether this also implies that the CEO should be excluded from the board of directors. Although this falls beyond the scope of this report, it is an important consideration to be made concerning board composition which is covered in Chapter 3.

Notes

1. This chapter does not look at the nomination practices for employee representatives on the board which may be appointed using a different procedure than those prescribed for "independent" or state board members.
2. Where the state is a significant minority shareholder (as noted *inter alia* by Norway and Slovenia) a consensus approach with other shareholders is usually required to get a cohesive and functioning board.

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Chapter 3

Board composition: Constraints and guidelines

A central recommendation of the SOE Guidelines *is that boards should be composed to exercise "independent and objective judgment". In most countries SOE boards are composed of a mix of civil servants, other individuals tasked with pursuing the public interest and "independent" directors. The trend, fuelled by a growing commercialisation of SOEs, is toward a greater reliance on independent board members – or persons with relevant commercial experience. Ensuring the recruitment of suitable board members can be based on formal eligibility rules, processes to advice or vet ministerial candidates for board appointment or actual or* de facto *nomination committees proposing candidates of the ultimate decision of ministers. Board composition can be further influenced by limitations on the number of board positions and/or affirmative action targeting gender and minority groups. Employee representation on boards generally follows private sector practices, but can differ for some SOEs (especially in the context of privatisation).*

> "Companies [...] should seek directors who are committed to improving the system and who can push for the changes that may be required to enhance the company's competitiveness in international markets – they should be people of integrity who are willing to make a difference. Companies can determine whether a person may be suitable by looking at his or her track record and reputation in the business community" (OECD, 2008).

Board composition is evidently important to a board's functioning and its performance. SOE directors should have the right skills and experience to contribute effectively to deliberations and respond to the needs of the SOE. In principle, the best boards are those made up of the individuals who are capable of exercising the qualities of a "good director". Concrete skills, such as technical knowledge and business experience are obviously important – even if some of them may arguably be learnt on the job. A good director also needs to possess more tacit qualities like interpersonal and communication skills in order to work in a team, as well as personal integrity. The board is a collegial body and therefore nominating qualified individual for board memberships is normally not sufficient; thought must also be given to the subsequent working of the board as an entity (OECD, 2010) (this is further discussed in Chapter 6). Accordingly, many countries have established minimum requirements for SOE board members which often require a mix of tangible and intangible skills/experiences.

Recognising that country practices vary, the *SOE Guidelines* do not spell out requirements as to board composition. They recommend that the boards of SOEs "should be composed so that they can exercise objective and independent judgement" (see below). The annotations to the Guidelines further posit that they should be "protected from undue and direct political interference". General consensus among OECD economies is that SOE directors cannot be directly linked with the executive power (e.g. ministers and their close associates); however civil servants and employee representatives can serve on boards depending on the country tradition and legal requirements.

SOE *Guidelines*, Guideline VI.C on board composition

The boards of SOEs should be composed so that they can exercise objective and independent judgment. Good practice calls for the Chair to be separate from the CEO.

Most OECD countries have a mix of directors for the state and "independent" directors on the boards of SOEs. Some also have a legal requirement, or tradition, for employee representatives on the board of some or all SOEs. This is consistent with the annotations of the Guidelines which propose that a sufficient number of the non-executive SOE directors be recruited from the non-State (and preferably private) sector – especially where the SOEs concerned operate in a commercial environment. As country practices indicate, in most SOEs it is nowadays uncommon to have boards that are made up by a majority of public sector representatives.

Many governments, either through law, subordinate regulation or circulars from the ownership function, establish certain constraints exist on who is eligible for nomination as a director. Such rules or guidance may relate to the behavioral characteristics of the person in question (i.e. integrity, honesty); educational or professional qualifications; and any other demonstrated qualities that are valued on the board (i.e. team player). But they also may be related to specific guidelines or constraints concerning quotas for gender, diversity, and representation of employee, state or other stakeholders on the board. Constraints concerning board size are also important but are dealt with in Chapter 6 of this report on board efficiency.[1]

Defining guidelines for board composition is ensures that boards are objective and independent. Importantly, board "independence" should not be confused with "independent" directors. An independent and objective board is one that operates under a legal framework, which is subject to public governance and that is designed based on board profiles. Independent directors (subject to national definitions) are individuals who are not directly representing any particular stakeholder interest in the company, but who are sought to bring certain skills and competencies to the board. The precise meaning of "independent" in the latter context is usually spelt out in national legislation – or reliance on national corporate governance codes and not limited to SOEs.

Although various board composition requirements may exist in a number of countries, all directors, in principle, should have the same responsibilities and be required to act in the best interests of the owner and/or the SOE. The various representatives on the board, especially if required by law or mandated by quotas, should not be seen as competing factions representing different interests. The best interests of the State should be weighed with that of the company (and in accordance with the high level objectives set by the ownership entity) (OECD, 2008).

The remainder of this chapter examines country practices with regard to board composition. It focuses on the question of board objectivity and independence by exploring the issue of public versus "independent" representatives on the board. It also looks at country practices concerning

employee representatives on the board. The remaining sub-section then focuses on board nomination eligibility requirements, including qualification requirements, and quotas/objectives terms of board size and composition.

Maintaining board objectivity and independence

One of the unusual characteristics of SOE boards, as compared with private sector boards, is the tradition in most countries (and sometimes legal requirement) to have direct representatives of the owner (public sector) representatives on the board. The question of how public and private representatives are combined on the board is central. Also, unlike in many private companies, the division is not merely between independent directors and "the rest". Figure 3.1 suggests a continuum of dependency on the ownership function including:

- Direct representatives (in some jurisdiction termed "controllers") from the ownership function.
- Other directors for the state, who by law or statutes are tasked with representing the governmental interest. In some countries these can be picked from the private sector or academia and "tasked" to act in the interest of the state, but in most cases they are civil servants.
- Directors that are picked at the discretion of the nominating minister or the ownership function, but not specifically tasked with representing the state. (In some countries these may include representatives of political communities.)
- Independent directors, picked according to national or SOE specific definitions of "independent".

Figure 3.1. **A continuum of board "independence"**

Some specific mechanisms may be set up in order to reinforce the independence of SOE boards. In many countries directors may, for example, have set terms (usually from three to five years) and can only be dismissed for a cause. In the most extreme cases, even the nomination of independent representatives will result from bargaining among ministries concerned, possibly involving specific committees or organs.

In line with the *SOE Guidelines*, many countries have made it obligatory for the SOEs to have independent directors on SOE boards. The presence of independent board members varies a lot from one country to the other, as well as the understanding about what is meant by independence. Ultimately, the degree of independence of SOE boards also depends partially on the size and makeup of the board (i.e. mix of private, state and employee representatives).

SOE Guidelines, Annotations to Guideline VI.C on objective, independent boards

The Annotations to the Guidelines, in contrast, highlight the benefits of sourcing non-executive directors from the private sector: "A central requirement to enhance the objectivity of SOE boards is to nominate a sufficient number of competent non-executive board members who are capable of independent judgment. These board members should have the relevant competence and experience and it is advisable that they be recruited from the private sector. It will help in making boards more business-oriented, particularly for SOEs that operate in competitive markets."

Public versus private

Overall, a large number of countries draw a broadly equal number of directors from both spheres. Nominees can include a combination of academics, private and public sector representatives (Korea). Only in a small minority of jurisdictions (Brazil, Mexico and Turkey) is there a clear preference that board members are sourced from the public sector.

The justification for public sector representatives on boards is probably stronger when the non-commercial objectives of the enterprise are prominent. For example, Sweden highlights that "Companies with specially adopted public service obligations generally have a higher degree of directors from the public sector due to the fact that a good understanding for government processes and decision making is vital in these companies."[2] However, where State representation boards is stipulated by law or made as formal selection criteria, special attention should be paid as to how candidates are selected (see chapter on Board nomination) and their duty towards the SOE.

That said, there is growing recognition that certain public sector representatives are not acceptable as SOE board members under any circumstance. OECD consensus holds that neither ministers, state secretaries nor other direct representatives of, nor parties closely related to the executive powers should be represented on SOE boards.[3]

This exemption could arguably be broadened to also cover high-level civil servants who work directly with representatives of the executive. Nordic countries have gone further than most jurisdictions to formally limit the weight of politicians and bureaucrats in SOE boards. For example, active politicians, including members of parliament, ministers, state secretaries, as well as civil servants who within their remit exert regulatory or controlling authority over the company or deal with matters of substantial importance for the company, cannot be elected to the board of directors in Norway. Similar rules are in place in Germany, except regarding State Secretaries who can be appointed in SOE boards if they are not members of the Parliament. New Zealand (which also has an express process for vetting conflict of interest) has gone farthest in instituting an absolute ban on any serving politicians or civil servants sitting on SOE boards

Good practice: Persons directly linked with the executive powers should not sit on SOE boards. Other State representatives should be nominated based on qualifications, subject to specific vetting mechanisms.

Moreover, many countries have restrictions concerning the nomination of civil servants as board members. In Finland, for instance, only one civil servant from the ownership function (and in some cases another from a relevant administration) can serve on an SOE board but potential conflict issues are avoided by generally not allowing the politically-appointed civil servants to serve on boards. A similar approach has been adopted by Australia where appointment of departmental officers to GBE Boards could only be considered in exceptional circumstances, having regard to their ability to represent the interests of the government, their possession of the business skills, and to any potential conflicts of interest that might arise.

In Israel, persons with personal, business or political connection to one of the Ministers are not barred from becoming directors in SOEs, but a significantly more demanding set of qualifications is applied in this case. A control mechanism has been established in the form of a public Appointments Examination Committee, which must approve the appropriateness of appointees (board members, chairmen of the board and CEOs), subject to a set of required qualifications established by law. The Committee needs to assure itself of the political independence of the proposed candidate (OECD, 2011).

The use of independent directors

As already mentioned, in SOEs as well as in private companies the trend is clearly toward a greater reliance on independent directors – reflecting, among other things, the stronger corporatisation of SOEs in a number of countries. In some jurisdictions, large and/or commercially operating SOEs are even requested to follow the best practice as set up by country codes, laws or

regulation regarding the corporate governance of listed companies. This is the case in the United Kingdom, where the Combined Code on Corporate Governance is used as a benchmark for SOEs. This Combined Code requires a majority of independent directors on boards of large companies.

Good practice: Independent directors should be independent from management, government and business relationships. Specific safeguards should be established to verify that nominees comply with requirements.

"Independent" is taken to imply independence both from the ownership, the management and from business relationships with the SOE (as defined by company law). In Scandinavian countries as well as the Austria, Germany, Netherlands and New Zealand, most SOE board members (apart from employee or stakeholder representatives) come from the private sector and are categorised as independent directors. These countries appear to define independence more strictly than average. They also follow the *SOE Guidelines* in that the role of Chair of the board is separate from the CEO. The board is tasked with appointing the CEO, although responsible Ministers are, as a rule, consulted as part of the process.

Australia and Norway arguably go further in requiring that independent directors from the private sector not only do not have any business relations with the SOE but that they are also not engaged in competing business. In Greece, independent board members should not be an executive or the Chair of the board, have business or other professional relationship with the company, and not be a first or second relation of or be married to an executive member of the board, a senior executive, or a shareholder owning a majority stake.

Somewhat beyond the scope of this report, in some countries the listing of minority stakes of SOEs in the stock markets has served as a "backdoor" to making boards more independent. The companies and securities laws of most countries establish a required minimum number of independent directors. An example of the latter is Brazil where only listed SOEs are required to have independent board members. At least 20% of the board members have to be independent if an SOE is listed in the "Novo Mercado" or "Nivel 2" segments of the Brazilian Stock Exchange Market.

Employee representatives on the board

A major difference in the composition of SOE boards across countries is the presence and number of employee representatives. The underlying rationale for having employee representatives on boards in SOEs is the same as for listed companies' boards (even though many more countries mandate participation in SOEs than for private enterprises): to increase accountability towards employees as stakeholders and reap the benefits of specific knowledge of the enterprise. Specifically, employee representation on the board can have the informational advantages of having a direct employee input to board discussions.

Employees as stakeholders can benefit by providing an opportunity to discuss and negotiate alternative strategies while keeping in mind the overall financial and service obligation objectives. Employee representatives on the board can facilitate awareness of employment and social aspects of the SOE's strategy. Board decisions can be brought down to the workplace quickly and smoothly. Last but not least, employee representation may be a primary source of information that is independent from senior management regarding the situation within the SOE. In some country experiences, lack of employee involvement in board decisions has resulted in tension when decisions were brought to the workplace (OECD, 2008).

Overall most countries report that employee representation on boards contributes to improved company performance Special care, however, needs to be exercised to ensure that employee representatives are sufficiently well qualified to play an equal role with other directors and to prevent their "capture" by stakeholder interests.

Good practice: Employee representatives can enrich board discussion; the appointment process should ensure that such persons are qualified, as well as representative of the SOE's staff.

The *SOE Guidelines* recommend that where it is mandated it be done in a way so as to guarantee that it "contributes to the enhancement of the board skills, information and independence," employee representation however "should not in itself be considered as a threat to board independence". In terms of board nomination this implies that the employee representatives should be selected through transparent and democratic processes involving all company employees. Regardless of the appointment process, qualities such as competence and independence of employee representatives and their respect of confidentiality obligations should be sought.

As mentioned, in many cases presence of employee representatives on SOE boards derives from usual corporate practice in the countries concerned such as in Austria, the Czech Republic, Finland, Norway, Denmark and Germany. In slightly less frequent cases, employee representation on SOE boards is determined through legal statute requiring a definite number or percentage of employee representatives, such as in France (where it varies between two individuals and one third of the board), Greece, Israel,[4] Spain, Sweden, and Switzerland. In other cases, privatisation laws stipulate the inclusion of employee representatives on the boards of companies from which the State plans to divest.[5]

Eligibility requirements

Skill-based qualifications

Structured and skills -based processes are at the heart of successful board nomination. Across OECD economies, ownership functions have in place recruitment processes that establish minimum criteria and ensure the right mix of skills and talent. These may be largely informal, but there are some countries that have formalised the eligibility requirements in the form of guidelines, and others have included stipulations in company bylaws. Regardless of the level of formalisation, there is a growing tendency for countries to rely less on quantitative requirements (education and professional background), and more on qualitative characteristics to describe appropriate board members. An outcomes-oriented approach can help to seek board members that have the right balance between skills, qualifications and personality characteristics.

In fact, some countries largely eschew formal requirements, preferring instead to rely on a case-by-case approach tailored to the board vacancies that are to be filled. As a general rule, formal eligibility criteria are prevalent in the case of boards with a predominance of State representatives. More "professional" boards where the majority of members are independent and/or from the private sector, the general preference is for ad hoc application of eligibility criteria.

Good practice: Certain eligibility requirements may be needed, but good practice increasingly relies on tailored approaches to identify the right mix between skills, experience and personal characteristics.

Australia has pioneered processes to develop specific eligibility guidelines. These include nominating individuals with an appropriate balance of relevant skills (such as commerce, finance, accounting, law, marketing, workplace relations and management) and contribute to the achievement of the GBE's objectives. Similarly, using the good governance recommendations provided by the New Zealand Securities Commission (NZSC), the Crown Ownership Monitoring Unit (COMU) provided guidelines for the public sector corporate entities. The guidelines from New Zealand place greater emphasis on potential board members' personal qualities.

In Italy, the company bylaws of unlisted SOEs were recently modified to introduce respectability and professional requirements among the criteria for nominating board members. A limit was also introduced to the number of board positions (executive as well as non-executive) that any individual may hold at the same time (OECD, 2011).

For those mandating minimum requirements, the most common provisions related to a minimum level of educational qualification, usually a degree, but in some jurisdictions this extended to a PhD level qualification. For example, Israelhas adopted a prescriptive system for mandating minimum

qualifications. It has established a system of mandatory qualifications for all boards that requires both high level academic qualifications and minimum five years senior experience. For large SOEs, the Government Companies Authority (GCA) has established additional proficiency and suitability requirements that are established for each board on a case by case basis. The GCA has prescribed for each company the specific expertise required of each director to ensure that the board has the appropriate mix of skills and experience. In a small number of cases, the requirements included the type of education required, such as law, accounting or economics. The other quantifiable measure related to threshold levels of experience, for instance in Greece the requirement is for five years of high-level or executive experience in the public or private sectors.

Those jurisdictions that do not mandate threshold education/experience requirements mostly rely instead on more holistic descriptions of the qualities needed to serve as a board member. The advantage of this approach is that it can more flexibly accommodate board members whose profile might not meet standard criteria but who, nevertheless through their business experience might bring valuable skills to the board. Sweden describes its process thus: "The starting point for all board nominations is the need of expertise. The composition of the board shall ensure that the board always has knowledge of the industry and other relevant expertise for the company. To be considered for election to the board, a high level of expertise is required in corporate governance, business operations, business development, industry knowledge, financial issues or other relevant areas. Furthermore, integrity and the ability to see to the company's best interests are required. The composition of the board shall also ensure that a balance is achieved between background, area of expertise, experience and gender."

Good practice: For all other than direct ownership representatives, relevant commercial or financial expertise is viewed as essential qualifications.

Relevant commercial and financial expertise is normally viewed as essential. Candidates who have worked as executives in a large or listed company, or have previously served on private sector boards, are usually sought after. Attracting executives from private sector companies can in practice be quite a challenge, given the increasing time commitment that is required of board members. This has in some countries led to an increasing reliance on professional board members (who devote themselves full time to board duties), many of whom may be retired corporate executives. This development is understandable, and perhaps unavoidable, but it needs to be counterbalanced by a stepped-up effort to recruit directors with recent hands-on experience. It also bears mentioning that, depending on the objectives of some SOEs with non-commercial orientation, relevant public sector

experience is still sought in some cases, and is sometimes preferred over commercial and financial expertise.

Maximum number of board appointments

Good practice: Reasonable limits on maximum number of board appointments are important to ensure that directors have sufficient time to carry out their duties.

In terms of improving the quality of boards, imposing hard constraints on the number of board memberships an individual can hold is a difficult issue, but it is growing in importance when identifying suitable candidates. Board members should have sufficient time and resources to devote themselves to their duty, which implies a natural limit to the number of directorships they can reasonably hold. However, excessive limits will reduce the capacity for a professional board membership to develop and may unnecessarily limit access to talent, particularly in smaller jurisdictions. Whether or not this is expressed formally differs between jurisdictions. For example in Austria, a maximum number of appointments is 10, whereas in Estonia the number of appointments to a board is usually less than four (an individual assessment of the extent of workload is, however, involved). In Greece only one remunerated directorship is allowed at any given time.

The number of board nominations per individual is linked organically with the size of SOE boards discussed in Chapter 6. Particularly large SOE boards (which are not recommended, for reasons discussed below) imply less time commitment from each director. Where such are common, the limitations on number of board appointments are usually less strict.

Gender, diversity and nationality/residency quotas

Judging from current debates about listed companies, there is mixed evidence and continuous discussion concerning the outcomes board diversity practices. Proponents of board diversity argue that it helps to intensify discussion, the exchange of ideas, and group performance. As a result, diversity has been supported as an instrument to improve organisational value and financial performance by providing a board with new insights and perspectives. Opponents have argued that the inclusion of eligibility criteria other than formal qualifications in the nomination process is liable to limit the pool of candidates, which can potentially impact the quality of SOE boards.[6]

Good practice: Diversity preferences may add value to Boards, but should not rise to the level where the ability to attract candidates with the right skills and capabilities is imperilled.

A number of European jurisdictions have introduced gender preference in their board nomination process. Countries with hard quotas include:

Austria has a minimum quota of 25% of female representation by the end of 2013; Belgium requires a one-third quota; and Finland has a minimum requirement of 40% for both genders.[7] Sweden and Norway have both expressed formaltargets for gender representation, although not as quotas: in Sweden's case it is 40% representation of both genders, and in Norway it is equal gender representation.[8]

Other European countries have expressed a preference, but no quota; for example in Denmark equal gender balance is encouraged "as far as possible." While in others, gender quotas are only applicable to state-appointees to boards (Greece, Slovenia). The European Commission has proposed legislation on a 40% target for the "underrepresented" gender on boards starting with large listed state-owned enterprises (i.e. public undertakings) but extending the requirement to large private companies (European Commission, 2012). If passed, this legislation would presumably affect national targets among EU membership where applicable.

Other jurisdictions have gender or other preferences, but no particular targets. New Zealand and Israel implement their diversity preferences by actively preferring suitably qualified people in under-represented groups. One mechanism used in New Zealand is to seek nominations from Ministries with a role in promoting the interests of diversity and equity.

Some other countries, one example being Canada, have additional affirmative action requirements, for example in terms of geographic origins or in terms of minority representation. While favouring an enlargement of the pool of candidates, such a policy may also put too much emphasis on the diversity of SOE boards to the detriment of their skills and capabilities. This has been criticised in Canada where Crown Company Boards have a high ratio of women, a good geographic balance, but lack in some cases critical skill and capabilities.

Good practice: Restricting board membership to nationals should be limited to cases where there is a demonstrated need for such rules, considering that it can act as a barrier to attract the right talent.

For certain SOEs operating in sensitive areas (i.e. national security or strategic sectors) restricting membership to country nationals (or residents) is preferred in some jurisdictions, but such limitations raise potential barrier to boards recruiting the best expertise and experience. It is unclear the extent to which jurisdictions are actively seeking foreign expertise in identifying potential board candidates. A small number of jurisdictions have nationality requirements of SOE board members. Turkey has a requirement that all board members must be Turkish nationals. Brazil also stated that the company by-laws often included a requirement that members be Brazilian nationals. Belgium, Latvia, and Switzerland have no nationality constraints, but express preference for members to speak the local language(s).

Notes

1. Although outside the scope of this report, it should be noted that limits in board size is relevant in the context of SOEs with strong State representation as a means to balance board composition, especially where historically public sector representatives outnumbered "independent" directors.
2. However, they go on to point out that more 90% of their nominees come from the private sector, suggesting that public sector experience may be relevant in a limited number of circumstances.
3. This consensus was enshrined during the process leading to the accession of Chile, Estonia, Israel and Slovenia to the OECD during which member countries concluded that the presence of Ministers, or persons closely affiliated with them, or other parties closely affiliated with the executive power, on SOE boards would preclude these boards from being capable of independent and objective judgement.
4. For companies with over 100 employees, the appointment of two employee representatives to the board is mandatory.
5. A recent survey of European economies suggests that board level employee representation is more widespread in terms of legal rights. According to the survey this is not only the case in SOEs but also private companies alike (14 economies fall into this category). Key differences among countries can be explained by the extent of their rights and appointment processes, which are determined as a function of the characteristics of the company, its board, and how legal provisions are implemented. See Conchon (2011).
6. The question of gender balance on boards has been considered by a recent OECD report; see Chapter 3.5 of OECD (2012).
7. In Finland, the quota is not a legal requirement, but subject to a government rule that applies to SOEs only. The rule may not be applicable where the government is not the full owner.
8. However, in the case of publicly listed companies in Norway (including SOEs) a minimum 40% representation of each gender is stipulated by law; whereas in Sweden, this is part of a voluntary goal of parity for listed companies.

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Chapter 4

Board training and induction

The SOE Guidelines *recommend engaging in human capital building among SOE board members to inform them of their responsibilities and liabilities. How much and what kind depends on the company and context. In all countries board induction is provided to new directors, in some cases mandated (and even arranged) by the ownership function, in other cases organised informally by the SOEs. Education and continuous training of board members is considered good practice in countries whose SOE boards contain mostly public officials. Countries that have commercialised SOEs and professionalised their boards mostly nominate directors who are in little need of further training. Where training is offered it is mostly provided "off the shelf" by professional bodies such as institutes of directors and often not materially different from what is found in private enterprises.*

Once a board of directors is in place, in many countries it is considered good practice to provide two specific kinds of human-capital building: *i)* board induction; and *ii)* continued training/professional development. Annotations to the *SOE Guidelines* suggest that training should be required, at a minimum, in order to inform SOE board members of their responsibilities and liabilities. This is essentially a limited form of induction, and indeed the need to provide new directors with an introduction is commonly acknowledged.

SOE *Guidelines*, Annotations to Guideline VI.A on training and induction

Annotations to Guideline VI.A: Training should be required in order to inform SOE board members of their responsibilities and liabilities.

As for actual training, in a number of economies there is apparently limited need. As discussed in previous chapters, the rules and procedures for board nomination are such that persons with proven qualifications and track records are recruited. For this reason, board members in many countries tend to attribute little significance to training aside from the induction programmes. However, where civil servants, public figures or employee representatives are asked to sit on boards, these persons might not be recruited specifically due to their corporate experience. Thus the assistance provided further to the appointment of new board members can be seen as useful.

In some economies the use of board training and induction goes further with the aim of developing already well-qualified SOE boards' competencies. Professional bodies and "centers of excellence" (such as institutes of directors) play a role in offering adequate and specific training to SOE boards. Such training covers their roles and responsibilities, as well as specific training on relevant technical aspects, related for example to financial and non-financial disclosure.

The remainder of this chapter examines country practices with regard to induction for new board members, and whether specific training is common to encourage on-going professional development. It finally examines the role of "off the shelf" training programmes and their role in supplying training to SOE board nominees.

Induction for new board members

Induction serves as useful reference point before taking up duties. Once directors are made aware of their duties, and any important rules and regulations (this is especially true in countries with relatively new director independence requirements) they can fulfill their roles more effectively and furthermore help to ensure smooth integration to the board (OECD, 2008). Induction is further aimed at introducing the company and its activities to the board member.

Good practice: Induction programmes should match the needs of each board. They should serve as a way to improve effectiveness of board members.

Board induction is a common practice across most OECD countries, although the format and organisation differ among countries and depending on the company, and even individual that is hired. A position held by most countries is that induction programmes should match the needs of each board and requirements will vary, (even if induction is a requirement).

An induction session is most effective if taken place within the first month of appointment, and always before the first board meeting. The induction session can be run by the Chair and/or Chief Executive. If possible, existing board members should also attend to pass on their experience. Some other members of the senior management team may also be required, including the board secretary. In smaller SOEs a discussion with the Chair, backed up with relevant documents could be considered sufficient. Larger SOEs are likely to require a more systematic induction programme including: formal meetings; courses or other development events; meetings with executive staff and other board members; a programme of visits; and more comprehensive reading material such as the ones on the list below.

Induction sessions normally cover three main areas: strategic, organisational and individual. The induction process should be tailored to the needs of new members. A less experienced board member, for example, may require support in more basic skills such as reading accounts. The induction session should explore these development needs and agree a plan to address them. Some countries have taken concrete measures to reach this objective. The government of New Zealand stands out thanks to its desire to appoint first-time directors and its regard for comprehensive induction programmes to achieve this goal. COMU organises inductions for both new and recurrent directors. It also sees the induction process as a networking opportunity (Box 4.1).

In a number of other countries, including Australia, Chile, and Germany mandatory formal induction within the individual SOEs is common practice. In Germany, for example, this is conducted through a two-week induction aimed at providing board members with up-to-date knowledge required to perform their duties as members of the supervisory board.

Box 4.1. **Formal induction in New Zealand**

Comprehensive induction is seen as very important to ensure that new Crown directors fully understand their responsibilities both to the SOE to which they are appointed and to the Crown and public. Specific induction to the SOE (its operations, personnel, strategies, markets, etc.) is conducted by the SOE under the supervision of the Chair, and according to the method determined as most appropriate by the SOE. The Crown Ownership Monitoring Unit (COMU) organises a separate one-day induction programme for all new Crown directors covering:

- The duties and responsibilities of Crown directors.
- The expectations of ministers.
- Relationships with key stakeholders (e.g. other parts of the Crown).
- An opportunity to meet with other new Crown directors to establish networks.

All new Crown directors are strongly expected to attend this programme within about six months of appointment, however this is not mandatory. An example of an agenda for a Crown Induction Programme is appended. COMU funds all venue and presenter costs, and the SOE funds any travel costs associated with attendance by new directors.

COMU is currently reviewing its full suite of development activities for Crown directors. In terms of induction, it is expected that face to face programmes will continue (to enable networking and other relationship-building to take place), and this will be supplemented by web-based materials and fora.

Source: New Zealander authorities' response to OECD questionnaire.

In other jurisdictions, induction is either mandated, or may be carried out at the level of the ownership function. For example, one may invite newly appointment board members to participate in a type of "orientation" as in the case of Israel. In most other cases the preferred form of induction consists of a one-on-one meeting with the CEO in addition to on-site visits (e.g. Finland and Sweden).

Specific training aimed at SOEs

As mentioned, in many jurisdictions even if on-going professional development may be a priority general board training is not mandatory nor, in most cases, common practice. Rather, the trend is to focus on thematic training in areas where supplementary training is needed on an individual or board basis, for example on accounting standards, tax codes/legislation, or laws, regulations and other areas of relevance to the function of the board.

Thematic training can also target technical committees where specific aspects of board competence are needed; for example, it is common in most countries to organise specific training for audit committees.

Good practice: General training for boards of directors should not be a formal requirement; however, on-going professional development should be encouraged and supported.

Where training is provided, the preference tends to be for workshop style meetings where good practices can be shared and exchanged with members of the board. Interestingly, in Japan, workshops are held for non-standing directors where reforms of public institutions are introduced. This practice apparently serves to inform board members of government objectives rather than equip them to fulfil their ordinary board functions. Other jurisdictions report that they encourage professional development by enabling payment by the SOE for training where necessary or requested by individual board members, although training is usually provided by in the form of an "off the shelf" training (Israel).

It is not common practice for SOEs to offer specific training for employee representatives on the board. In jurisdictions where employees serve on boards, training may be received through their own constituencies (e.g. trade unions). This is the case in Sweden, Germany and (on an informal basis) Finland.

"Off the Shelf" director training programmes

As mentioned, in some countries professional bodies and centres of excellence (such as institutes of directors) play an important role in providing training to boards. In most jurisdictions, these "off the shelf" trainings are oriented towards board members in general (regardless of public or private sector status). In other jurisdictions, especially outside the OECD area, specific courses may be provided for boards of public sector companies.

Interesting examples from outside the OECD areas comes, *inter alia*, from India where the a government sponsored Directors' Certification programme is in place for Directors and Senior Executives of large SOEs, including independent directors and government nominee directors, all of whom have to take a three hour examination before certification. A similar approach has also been adopted by the government of Malaysia in order to improve the efficiency of SOE boards. The training focuses on:

- facilitating and encouraging sharing of learning through forums, linkages and databases of best practices;
- conducting research and developing Malaysian-related case studies to assist directors in building knowledge on how to handle specific situations;

- organising "on-the-job" learning and coaching which will be customised to an individual director's needs; and
- increasing the quality of existing training and development programmes to meet the needs of directors.

The pervasiveness (or benefit) of "off the shelf" training for SOE board members are less well documented in the case of OECD economies. Most countries report that it is not clear whether such training actually improves the chances of getting nominated, or improves the performance of individual board members who have undergone formal certification or accreditation programmes. Clearly, many informal learning opportunities for learning exist including, for example, interactions with inside outside experts (such as board evaluation consultants), site visits, meetings with executives, etc. Memberships on other boards also provide excellent opportunities to learn from case experience. Even very technical issues such as accounting or financial instruments are learned on the job in meetings with SOE auditors rather than in formal outside venues. Despite the overall trend, the role of the State in encouraging on-going professional development especially where technical training may be necessary should be considered.

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Chapter 5

Board remuneration

The SOE Guidelines *recommend that remuneration schemes for SOE boards foster the long term interest of the company and attract qualified professionals. In most countries, the remuneration of board members falls below market levels. Remuneration and incentives are often regulated and limited for both executives and board members. Some countries have policies to align pay with market rates, but not be market leading; others are considerably more restrictive. The models most commonly used are* i) *limiting remuneration to an attendance fee per board meeting;* ii) *capping directors' remuneration at a multiple of average salaries in the SOE or the national economy; and* iii) *developing a "fee policy" taking into account factors such as the size of SOEs, time requirements and director qualifications. Attracting talent may be a challenge due to low remuneration; but other non-pecuniary benefits such as prestige, opportunities to build experience and networking attract talent to boards.*

The *SOE Guidelines* indicate that a prime responsibility of the State as an active owner is to ensure that remuneration schemes serve the long term interest of the company and attract the right people. The annotations further refer towards the need to look at private sector remuneration practices.

> **_SOE Guidelines_, Guideline II.F on remuneration**
>
> In setting remuneration, Guideline II.F recommends that "the state as an active owner should [… ensure] that remuneration schemes for SOE board members foster the long term interest of the company and can attract and SOE motivate qualified professionals."

In practice, in a majority of OECD countries, remuneration fall below market levels for the competencies and experience required, as well as for responsibilities involved. As a general rule, governments tend to regulate and limit the remuneration and incentive awards of both executives and board members of SOEs. Some countries have policies that seek to align pay with market rates but not be market leading. Others prescribe maximum remuneration levels. These prescriptions may be supplemented by prohibitions on share options, or restrictions on bonuses.

The remainder of this chapter examines board remuneration practices and considers the question of adequacy of remuneration *vis-à-vis* private sector companies. It also looks at the role boards have in setting.

Practices and trends

The state's concern with pay issues is largely political in nature. The general public expects remunerations paid by the government to be "fair", but there is no commonly shared definition of fairness. One of the goals of government is to create a "level playing field", i.e. fairness of opportunity within society. But another goal may be to encourage fairness in outcomes, and money is a clear indicator of outcomes. In the first view of the world it would be perceived as unfair to differentiate between public and private employees; in the second it might be seen as unfair to remunerate State employees more generously than the earnings of members of the general

public. Faced with this choice, governments generally wish to avoid public controversy over excessive pay in the public sector.

Remuneration criteria are determined by a variety of factors and are very often related to the size of the SOE, work load, risk level, wage indices in the sector or company, as well as usual practice in the sector concerned. In establishing remuneration, the observed low levels probably reflects concerns regarding board remuneration generally, but may also reflect the fact that there are significant non-monetary rewards from accepting an SOE board position. For example, association with an SOE may bring a director reputational benefits and/or create longer-term opportunities that go beyond immediate financial gains. Due to these advantages, the prevailing view in most, but not all, governments is that remuneration does not currently affect the recruitment of candidates for serving on SOE boards.

Where civil servants sit on boards, the most common approach is for them to receive no remuneration in addition to their civil service salaries. While this may be necessary to avoid controversy, given their existing remuneration from the state, the risk with such a policy is that it creates a perception of these directors' activities as guardian of the public interest, rather than in the interests of the company. It may also dis-incentivise the most qualified civil servants from accepting such assignments.

Good practice: Board remuneration should reflect the market conditions to the extent that this is necessary to attract and retain highly qualified directors.

Ongoing efforts, discussed elsewhere in this report, to enhance board professionalism and performance are unlikely to be successful unless board remuneration allows SOEs to attract and retain directors with the required expertise and experience. However, a distinction needs to be drawn between SOEs operating in a competitive environment which, by extension, conditions offered to the board also need to be competitive, and SOEs with largely sector policy priorities whose board members are likely to have significantly different professional profiles. As a point of illustration (refer to the tables in Annex A) countries that practice centralised models of ownership generally have the most market-consistent board remunerations, largely because they also tend to be the ones that have gone the furthest in commercialising their SOEs (characteristically, one of the few "dispersed" systems with broadly market consistent board remuneration is found in the United Kingdom, a country with a well documented commercial approach to state-owned enterprises).

This is an area which has attracted recent attention. A stocktaking of SOE reform in OECD countries found that three Nordic countries (Finland, Norway and Sweden) as well as the Czech Republic have in the past few years issued policies or guidelines aimed at imposing some limits and restrictions on the

remuneration and employment conditions of SOE directors and executives (OECD, 2011). Still, national practices differ. Governments that limit, or at any rate regulate, board remuneration do so in a number of different way, that can be clustered into the following three categories (broadly, in increasing order of "generosity" of remuneration):

- *Attendance allowances*. In a few countries SOE board members are not remunerated except for a certain allowance per board meeting attended. Obviously, the ultimate remuneration for board work then depends on the generosity of the allowance, but the tendency is (fuelled by a public perception of a board attendance being just "a few hours of somebody's time") to keep attendance allowances low. Countries practicing this system include Greece, Spain and Slovenia. In the latter country, low levels of remuneration have been frequently cited as an impediment to attracting private sector expertise to SOE boards.
- *Caps or limits*. Other jurisdictions have capped SOE remuneration at certain maximum levels. The maximums may be fixed, or they can be set according to a percentage of the respective SOEs' employee or managers salaries (as in Brazil, Hungary, Latvia, Poland,* and Portugal). For example, in Brazil the cap is 10% of the median manager's salary. In Hungary and Poland it is set by reference to a multiple of employee wages, and in Portugal the limit is struck by reference to the pay of executive directors. Latvia expresses Board member remuneration in relation to the CEO salary. At the same time, it is also the only country reviewed in this report to mandate a minimum (based on the national minimum wage). In some countries maximum limits are subject to a degree of flexibility, such as Poland which allows a possible exception for very important SOEs where remuneration can be 50% higher than otherwise stipulated. In the Slovak Republic, the board remuneration is capped at five times the national average wage salary.
- *An overall remuneration structure*. Some countries have developed more elaborate structures for differentiated board remuneration according to enterprises size and other indicators of workload. This is for example the case in Canada, Estonia, Israel, New Zealand and Sweden, which grade each SOE according to a ranking system and let remuneration levels depend on the rankings. However, the overall finding remains that, notwithstanding these more sophisticated methods of differentiation, board remuneration generally remains below the levels of comparable private enterprises.

A particularly flexible system is applied in New Zealand, where a lump sum is approved for each board, based on COMU's methodology which places SOEs into one of six remuneration bands (based on size and complexity). The

* Remuneration levels are currently under review in Poland.

lump sum covers directors' fees for all normal duties (including board sub-committee attendance). The board chair and deputy chair receiving a higher proportion of the distributed amount given the weight of their responsibilities.

Good practice: Remuneration policies of civil servants serving on SOE boards should be carefully considered to ensure the right incentives.

The role of boards in setting remuneration

It is very uncommon among SOE boards in OECD economies to have a role setting their own remuneration. The exceptions include Italy and Lithuania, where the board has a formal role in remuneration which in both cases this basically consists of making recommendations to the AGM. In Denmark, the Chair would have an informal discussion on remuneration with the Minister, prior to the AGM where remuneration would be set. Although the board may be conflicted in setting its own compensation, it is difficult for the State to be position to determine this amount; for this reason it is common place that the boards are consulted. Regardless, the decision should be made as transparent as possible and benchmarked according to practices in similar companies (including in the private sector). Pay should be within reason and in line with what the company can afford in addition to the remuneration philosophy applied at the executive management level (OECD, 2008).

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Chapter 6

Boardroom efficiency

As SOE boards become more "professional", the issue of boardroom efficiency moves to the forefront. A well-functioning board takes responsibility for setting strategy and creating value, acting as a collegial entity with a shared responsibility. One implication is that it has become more important to identify directors that answer concrete demands for skills and competencies in individual boards. In the course of the process of professionalisation, therefore, the size of boards has generally shrunk to more manageable size, the role of directors as "team players" has grown and, partly related to the previous point, the role of the Chair as a convener and co-ordinator has been strengthened, so too has the role of board committees. However, it has also led to an increase in the workload and time commitment of directors, which has in some cases created problems for board recruitment and potential remuneration.

Although the *SOE Guidelines* do not deal explicitly with the issue of boardroom efficiency, it does pronounce itself on a number of key issues that fit into the broader issue of efficiency. Moreover, boardroom efficiency is unsurprisingly gaining importance among SOE owners. SOE board should consider is whether it makes an effective and efficient contribution to the function of the enterprise and to the fulfilment of the objectives that the State owner has communicated. This starts with defining the role of the board and its composition (as covered in previous chapters), but it also involves other aspects such as team dynamics, workload, size and structure (role of the Chair and respective committees) which are covered by the remainder of this chapter.

Team dynamics

Team dynamics of a board is an important aspect in improving board efficiency. On the one hand behavioural characteristics of individuals contribute to boardroom efficiency (as suggested by the quote cited in Box 6.1), on the other it is the working environment created by the team dynamic created by a group of members together. This is not only influenced by the perception of its board members as to their role, but also in terms of what their added value is. In order to contribute to the efficiency of the board, it follows that employee representatives should act as part of the board team, as opposed to the

Box 6.1. **Perspectives on boardroom efficiency**

"Boards often resemble families with each person appearing to have a particular role. Some boards also have director 'cliques.' Upon joining a board, directors should think about their role on the board and where they fit. New directors should work to establish themselves by leading with their unique skills. For example, a director with a strategic background could ask questions about how well the company analyses what its competitors are doing and how it's operating structure compares to theirs. It can be difficult for new directors – particularly those in the minority – to find their voice on a board. New directors should strive to bring a different perspective to build credibility and avoid "add-on' comments. Directors may need to work extra hard to make their mark and avoid exclusion from debates on issues that do not directly relate to their minority status."

Source: OECD (2008), *Using the OECD Principles of Corporate Governance: A Boardroom Perspective*, OECD Publishing, Paris, *www.oecd.org/daf/ca/corporategovernanceprinciples/40823806.pdf*.

representatives of the constituencies which appointed them. These factors will influence whether the board, acting as team can have an impact on the performance of the company.

A typology for SOE boards suggested by an earlier OECD study reflects all these different factors which influence the team dynamic and can determine whether a board can be effective (Table 6.1). The team dynamics of a board can be broadly classified in four categories: *i)* the conduit board, which runs the SOE as an extension of a government department and relays directions given by ministers; *ii)* the subjugated board which is dominated by a powerful CEO/Chair; *iii)* the effective board; and *iv)* the symbolic board which is circumvented and uninvolved (adapted from Frederick, 2011).

Table 6.1. **Team dynamics on SOE boards**

Type/function	The conduit board	The subjugated board	The effective board	The symbolic board
Decision-making powers	Board functions as an extension of a governmental department	Approves without contest or consideration Does not consider alternatives	Board makes performance-related decisions	Circumvented and powerless Not consulted on decisions by either management or owners
State vs. Company orientation	Focus on state expectations versus needs of the SOE	Limited strategic focus Relies on information fed by executives	Strategic focus	Unable to influence orientation
Relationship with executive management	Limited role of non-executive board members Relays directions given by Ministers	Limited role of non-executive board members Dominated by executives	Board is actively overseeing management Significant role for non-executive directors	Not privy to key discussions between owners and management with all decisions taken by owners
Value adding	Compliance/ conformance checking	Does not see its role as adding value	Value adding with visible board influence and presence	Lack of recognition, influence and impact

Source: Adapted from Frederick, W. (2011), "Enhancing the Role of the Boards of Directors of State-Owned Enterprises", *OECD Corporate Governance Working Papers*, No. 2, OECD Publishing, *http://dx.doi.org/10.1787/5kg9xfg6n4wj-en*.

Workload

As in the private sector, the expectations of SOE boards seem to grow inexorably. The most visible manifestation is the increase in the workload and the time commitment that board members face. The workload of a board member is a reflection of both the number and complexity of issues that it needs to consider. Today, boards must consider increasingly difficult technical issues including risk and risk management, financial instruments, financial reporting, systems of control, etc. Other issues may be less technical but challenging from a conceptual perspective such as corporate social responsibility. Furthermore, boards are increasingly expected to look to the future and anticipate events.

Board members can now expect to work from 10 to 25 days per year, and the expectations of board chairs are much higher. Depending on the size of the company, a chair can expect his/her time commitment to run from 40 to 90 days of service per year (OECD, 2008), and where special circumstances (such as a crisis) exist this may be even more. Only a few countries have developed or are developing specific guidelines for how the work of SOE boards should be conducted. The only requirement usually established by the Company Law or in specific SOE related legislation, concerns the obligation for minutes of board meetings and the number of meetings to be held per month or year, which varies from twice a month in Turkey to once a year in Austria.

The level of organisation of the board will also affect work load and therefore efficiency. As such an important aspect in keeping the work load reasonable is to ensure that board meetings are set well in advance, with a clear agenda and with set dates (much of this relies on the Chair of the board as discussed below) (OECD, 2008). Boardroom efficiency is also reflected in the level of preparedness of directors. For example the board can contribute their perspectives to the discussion base on their experiences, but this should also be coupled with adequate knowledge of the company's business and the conditions in which it operations. The workload expectations for board members should also factor in time invested in researching the industry of the company, how it operates, how it makes money, any specific non-commercial objectives that it be required to undertaking, in addition to understanding its competitors (OECD, 2008).

Size limits

Determining the right size of the board is an important issue with respect to promoting board efficiency. It is not possible, nor is it appropriate, to recommend a one size fits all approach when looking at board size in the public sector. However, size does matter as is supported by the *SOE Guidelines*. Large boards can result in unwieldy processes and lack clear direction (as is the case for SOEs in some jurisdictions), whereas boards which are too small may not fully reflect the needs of the company. In other jurisdictions, such as Portugal and Hungary cost savings are a key motivator in reducing the size of boards; whereas, in Switzerland, board size is identified in one of its Corporate Governance Principles requiring slender structures for governing bodies.

As a general rule, board size should be developed taking into consideration factors such as an entity's size, complexity, risk of operations and the needs of the board. Furthermore, over time the optimal board size may vary in line with changes in its functions or the needs of the board. Nevertheless, there does appear to be consensus in the approach of jurisdictions to the optimum board

SOE Guidelines, Annotations to the Guideline VI on board size

To encourage board responsibility and in order for boards to function effectively, they should follow best practices adhered to in the private sector and be limited in size. Experience indicates that smaller boards allow for real strategic discussion and are less prone to become rubberstamping entities.

size: a large number of OECD economies identify the optimum board size as somewhere between five and eight members (see Table 6.2).

Table 6.2. **Maximum board size**

	Maximum size	Minimum
Austria	20	–
Belgium	–	12
Brazil	6	–
Canada	12 (maximum)	9
Chile	7	3
Denmark	–	3
Finland	10	3
France	18	9
Germany[1]	n.a.	n.a.
Greece	7	–
Hungary[1]	7	3
Israel	12	–
Italy	5	3
Korea	15 (informal)	–
Latvia	3	–
Lithuania	15	3
Mexico[1]	n.a.	n.a.
New Zealand	9	2
Norway	–	3
Poland	–	3
Portugal[1]	–	–
Slovenia	–	3
Sweden	9	3
Switzerland	10	5
Turkey	–	6
United Kingdom[1]	–	–

1. Depending on the company.
Source: Country submissions to OECD questionnaire.

The role of the Chair

The crucial element in promoting board efficiency and creating an effective board is the chair of the board. It is the chair's task to build an effective team out of a group of individuals. This requires specific skills, including leadership, the capacity to build and motivate teams, the ability to understand different perspectives and approaches, the capacity to diffuse conflicts, diplomacy and personal effectiveness. The chair of the SOE must also interface between the State, the board, and the executive. Its role in liaising with the ownership function is seen as an important channel of communication. Finally the chair must understand the business and ensure compliance with all legal and statutory obligations.

Good practice: The key to the board efficiency is a Chair who can build an effective team by exercising leadership, diplomacy and a deep understanding of the business.

Some jurisdictions highlight the importance of the Chair in board functioning. These are usually reflected in their board guides covering not only the SOE sector but the broader public sector. Depending on the jurisdiction the Chair will fulfill more or less functions. At minimum, the following roles should be assumed by the Chair:

- setting the board agenda;
- facilitating the flow of information and discussion;
- conducting board meetings and other business;
- ensuring the board operates effectively;
- liaising with and reporting to the minister or ownership function;
- reviewing board and organisational performance; and
- induction and supporting of board members.

SOE chairs are contributing in new and evolving ways, for instance in enhancing the board composition and selection procedures. *First*, in some countries chairs are involved in conducting gap analyses of boards (i.e. in determining what board member profiles are required to strengthen the board), and in interviewing candidates to help assess personal and behavioral characteristics. *Second*, in other cases chairs have the capacity to express reservations regarding nominees and override government proposals based upon an expression of justified concerns.

A final observation is that the role of chair requires a significantly greater contribution in time than that of other board members. Workload needs to be taken into account when considering the accumulation of board roles and in remuneration.

The use of board committees

The *SOE Guidelines* posit that when necessary, SOE boards should set up specialised committees to support the full board in performing its functions. Annotations to the Guidelines further indicate that the setting up of specialised board committees could be instrumental in reinforcing the competency of SOE boards and in underpinning their critical responsibility in matters such as risk management and audit. They may be also effective in changing the board culture and reinforcing its independence and legitimacy in areas where there is a potential for conflicts of interests, such as with regards to procurement, related party transactions and remuneration issues.

SOE Guidelines, Guideline VI.E on board committees

"When necessary, SOE boards should set up specialised committees to support the full board in performing its functions, particularly in respect to audit, risk management and remuneration."

The use of specialised board committees in SOEs has increased, in line with practices in the private sector. The type of special committees that boards make use of can vary between companies and industries and includes: audit committees, remuneration committees, nomination committees,* strategy committees, ethics committees, and in some cases risk and procurement committees. Even in countries where audit committees are not commonly used other board-linked bodies may in practice perform a similar function.

Good practice: Specialised committees can contribute to the efficiency of the board, but should not detract from the responsibility of the full board.

The existence of specialised committees should not deprive the full board of its responsibilities in the matters concerned; however, it can contribute to the efficiency of the board by ensuring that technical issues are dealt with by members who are adequately independent, trained or informed. When setting up board committees, general practice would suggest that they are chaired by a nonexecutive and include a sufficient number of independent members. The proportion of independent members as well as the type of independence required (e.g. from management or from the main owner) depends on the type of committee, the sensitivity of the issue to conflicts of interests, and the SOE sector. The audit committee, for example, should be composed of only independent and financially literate board members.

* The prevalence of nomination committees is briefly discussed in Chapter 2.

Good practice: Board committees should be made up of independent and technically literate board members to ensure efficiency.

In most jurisdictions board committees are not mandatory; boards are free to set up such committees, based on the Company Law and according to their governance needs. Where they exist, the composition and duties of committees are defined by the board, and are published in Annual Reports (OECD, 2005). Though not prescribed by concrete reform measures, the ownership agency in France has actively encouraged government-invested companies to establish audit, strategy and remuneration committees. Finland, too, does not require committees, but it has recently (since 2007) has encouraged the establishment of remuneration committees, with the purpose of ensuring competitive and incentive-consistent remunerations in SOEs. In Korea, however, board audit committees are required by law for commercial SOEs (OECD, 2011).

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Chapter 7

Board evaluations

The systematic evaluation of SOE board increases professionalism and is commonly considered good practice. They serve directors (not least the Chair) as a vehicle for assessing and improving the board's modus operandi, *and they provide the ownership function with valuable information concerning possible changes to board composition. Administrations that run their SOEs relatively close to general government tend to rely on top-down approaches through which the ownership function evaluates the board in light of corporate objectives. In more commercial SOEs the trend is to rely largely on board self-evaluations. All such evaluations assess the workings of the board as a whole; some extend to an assessment of individuals. Self-evaluations are often assisted by external evaluators from private companies, or in some cases from within the general government sector. An evolving consensus is to create strong feedback links from the board (self) evaluations to the board nomination process.*

Board evaluation, which has long been commonplace in large private sector companies, is becoming increasingly widespread in state-owned enterprises as well. Board evaluations are being encouraged by governments as a way of maximising board performance and minimising risk. Government interest in evaluations is also heightened as a result of increasing board autonomy, which has reduced the role of what we previously a process of monitoring from inside the board room.

Board evaluations are commonly recognised to be an important tool in promoting an effective functioning board. The *SOE Guidelines* suggest that SOE boards should conduct a yearly evaluation to assess their performance. Systematic evaluation is a crucial tool in improving SOE board professionalism, since it underlines the responsibilities of the board and the duties of its members. It is also helpful in recognising necessary competencies and board member profiles. From the perspective of the board they allow an assessment of the functioning of the board to improve the board's operating procedures and practices.

SOE Guidelines, Annotation to Guideline VI.F on board evaluation

The Annotations to the Guidelines make clear that a systematic evaluation process is a necessary tool in enhancing SOE board professionalism, since it highlights the responsibilities of the board and the duties of its members ... [and] it is a useful incentive for individual board members to devote sufficient time and effort to their duties as board members.

From the perspective of the ownership function, board evaluations can also serve a purpose in allowing those responsible for board nominations to assess the composition and functioning of the board on a holistic basis. Even where the nomination process is rigorous and well structured, the nomination of individual board members may be done as a succession of discrete decisions, with the risk that it neglects a consideration the overall needs of the board in terms of the balance of skills and experiences. Utilising the board evaluation processes as an input into nomination decisions provides a mechanism to make important decisions about board succession, director

development activities, and actions to address any skills gaps in the boards (e.g. through subsequent appointments).

To be effective in achieving these goals, board reviews should be performance based, rather than simply focusing on mechanistic elements such as attendance levels and number of interventions. Involving the board in the review (even where an external review is conducted) is more likely to lead to substantive performance issues being addressed. Most countries adopt one of two approaches: either the ownership entity conducts an external review of board performance which they use to assess the functioning of the board or, alternatively, the board is tasked with reviewing its own performance. The challenge is to ensure that performance evaluations are conducted in a way to improve performance and inform the nomination process.

As illustrated below, in most countries evaluation ranges from informal evaluations by the Chair to more formal self-evaluations, to formal evaluations conducted by external experts and facilitators. Countries and companies also differ in respect of whether they merely evaluate the board as a whole or meter out individual evaluations of each board member and the chair. The remainder of this chapter looks at the role the ownership function, the board itself and external evaluators play in board evaluation. Finally it considers the extent to which board evaluations feed back into the board nomination process.

Evaluation by the ownership function

Board evaluations can be done at the ownership level as a form of top down review, and in a minority of jurisdictions this is the principal means by which board performance is assessed. Where this approach is chosen the board evaluation is usually linked to the fulfilment of overall corporate objectives: boards are monitored against their ability to agreed objectives and corporate strategies. In fact, this is an oft-overlooked aspect of top-down board evaluation: it cannot be performed in a meaningful way unless the State communicates non-commercial (as well as commercial) objectives that an SOE is expected to pursue in a transparent manner (OECD, 2008 and as discussed in Chapter 1). A board of directors "is not better than its objectives" and absent this condition it is not clear against what benchmark the board is being evaluated.

National approaches differ, however, in respect to whether the ownership function limits itself to this performance review, or goes beyond it to try to assess the board functioning as an entity and/or including the efforts of individual directors. Whether this is done by outsourcing evaluations or supported by the involvement of external/internal audit bodies differs. Some national approaches are described below.

In Chile (Box 7.1), the ownership agency, SEP, co-ordinates performance reviews for all SOEs, but outsources a large amount of the work to external

Box 7.1. **Chile's board evaluation process**

SEP conducts an annual evaluation of all SOEs board members. The evaluation focuses on the board as a whole, but the Chair´s role and impact on the performance of the board is a specific aspect evaluated.

The evaluations are conducted by nationally known Corporate Governance Centres; specialised companies; or auditors. The external facilitators are responsible for the preparation of the evaluation, getting the information and answers and its analysis.

The questionnaire is prepared by the specialised external facilitators and reviewed by SEP, in order to assure its results are comparable to past results. The survey is sent to board members and the results are analysed by the external facilitators.

Apart from the external review, a series of other aspects are evaluated, this time only by SEP. This includes: performance of the board, attendance of board members; fulfilment of goals proposed by SEP, and performance of the SOE.

The establishment of the criteria used to measure the board's performance contains both mechanical aspects as well as performance-based measures. For instance, the evaluation focuses on: the collaboration of the board (teamwork); the flow of information; performance of the board; mechanistic elements (attendance), fulfilment of goals proposed by SEP as shareholder (for SOEs not created by law) or representative of the State (for SOEs created by law), and, performance of the SOE.

At the end of the process, the results are provided to the board, through the chair, and also relayed to the relevant share ownership entity. A report is prepared for the SEP Council and also sent to relevant Authorities.

The results of the evaluation are used for determining the future composition of the board and the continuity or change of boards.

Source: Chilean authorities' response to OECD questionnaire.

corporate governance centres, and reserving for itself an overview role. The reviews are based primarily on questionnaires sent to board members. At the end of the process, the board (through the Chair) are debriefed on the outcomes of the review.

In Mexico, a hybrid form of review is conducted. All SOEs are audited by an internal unit, called the Internal Monitoring Body. But the Monitoring Body itself is appointed by the Secretariat of Civil Service. In some cases, the internal reviews are supplemented by additional reviews by the Supreme Audit Office. The Monitoring Body has the responsibility of evaluating the overall performance of the SOE including the board's performance. The board

is evaluated according to the objectives stipulated in the Sector Program by the relevant Ministry.

In Poland, the Ministry of Treasury undertakes periodic evaluation of the operations of supervisory boards in companies with State Treasury shareholdings. These reviews are prepared on the basis of the documentation sent to the Ministry by the supervisory boards as well as through personal contacts with the companies. The review covers mechanistic elements (compliance with binding laws; timeliness of reporting and informational duties; frequency of meetings and attendance of individual supervisory board members; the completeness of documentation, etc.), but are also performance focused. For instance, the review examines the theme of the meetings and the scope of issues covered by the supervision and control, and initiatives of individual board members with regard to putting forward motions aimed at improving company efficiency.

SOE board performance in Switzerland is measured by its fulfilment of the strategic goals generally set for a period of four years. The assessment is exercised on the basis of annual reporting to the ownership units and the Federal Council, who in turn evaluate company achievements and give feedback to the Chair. The board is assessed as a whole. In case of under-fulfilment/mismanagement, the Federal Council is entitled to adopt pre-defined measures (including the dismissal of board members/the Chair).

Board self reviews

In many countries SOE boards are required to carry out self evaluations. The outcomes of the appraisal are generally communicated to the ownership entities, and in some cases also board nomination committees. The use of self reviews may co-exist with evaluations by the ownership function, but it is more common where no top-down reviews are in place. The degree to which the ownership function is involved in co-ordinating or participating in the review, and in receiving the results of the review varies quite markedly among jurisdictions. The board evaluation serves primarily the board itself particularly through the round up discussion, teaching the members to cooperate more efficiently and to perform better during the following fiscal year. Some examples of national practices are provided below.

A number of countries mandate an annual self-evaluation but leave the format of the evaluation up to the board. They perceive self-evaluations essentially as an internal board issue for the board – a collegial process focused on improving the workings and processes of the board. For example, in New Zealand the State requires each board to undertake periodic evaluation (at least annually) of the performance of individual directors, the chair and the board as a whole.

In Denmark self-evaluations are carried in different ways. In some boards, the Chair carries out a formal self-evaluation based on a standard questionnaire, while a more informal process is applied by other. For those boards that use questionnaires, the topics covered are typically the board's competencies (do the board think it is appropriately composed) and functioning as collective decision making entity (are they focusing on the right issues, is there an open debate at board meetings, do all members participate and are prepared), the Chair's performance, co-operation with management.

In other countries the ownership function provides general guidelines for the form that the self evaluations must take. For instance, in Brazil the Ministry of Planning has only recently introduced a process of systematic annual self-reviews to be conducted by SOE boards. The ministry has developed a detailed questionnaire and it is expected that the reviews will be based on this. The ministry will receive a copy of the outcomes of the review and may utilise this in assessing future board needs. At a minimum, the ministry will utilise the review to inform the annual process of fixing their remuneration, and will tie board member variable remuneration to the outcomes of the review.

In Slovenia, the ownership entity mandates that the self evaluation must be conducted according to a manual for self evaluation of boards, issued by Slovenian Directors' Association. The analysis is performed by evaluating a questionnaire is filled in by each member of the board. The analysis is discussed in special session of the board and action plan for improvement of boards' work is adopted in that session. The Chair of the Board is responsible for implementing the action plan. Boards can hire independent external professionals to assist them in the process of evaluation. In Latvia and Estonia, self-evaluation is a requirement of commercial law and forms part of the report presented annually to the shareholders meeting.

Good practice: Board evaluations should favour focus on performance of the board as an entity. They should not be limited to "box-ticking" exercises.

Role of external evaluators

Where reviews are conducted or co-ordinated by the board external facilitators is not un-common. External advisers rather than acting like an evaluator generally assume the role of facilitating the discussions on board performance by the use of various interview and questionnaire techniques. Many jurisdictions report a widespread use of external facilitators, but in most cases this is a decision left to the board rather than mandated by the ownership function. In Finland and Sweden, for example, boards are free to choose the method of evaluation used as long as it does not deviate much from best business practices. As noted above, Chile outsources the core work of the

review to recognised Corporate Governance Centres that have experience in conducting such reviews.

Good practice: The use of external facilitators can be useful to structure the discussion of board performance.

In some cases, the reviews are conducted with the participation of the external auditors or the state audit authority. In the Czech Republic, self-reviews by the board and augmented by external reviews, where auditors are engaged to conduct reviews of Supervisory Board performance on an ad hoc basis.

Feedback into nomination process

As noted above, one of the key benefits of board evaluation processes is that they can help form a view on the overall functioning of the board, the desirable attributes that the board should possess and, in doing so, help identify any needs that could be addressed through future nominations. In order for this to occur requires both that the evaluation is directed to addressing these sorts of issues (that is, they go to the heart of board performance), and that there is a process by which the people or entities responsible for board nominations are provided with feedback on the outcomes of the evaluation process.

A non-trivial number of jurisdictions utilise board evaluations as an input into the nomination process, but the degree of formality of the process varies considerably. As a general rule, mandatory requirements for evaluation tend coincide with a more structured process for utilising evaluations as part of the nomination process. Some national examples are provided below.

Chile, with its quite structured reviews, reports that it uses the outcomes of these reviews specifically as an input into the nomination process, together with interviews with the chair and certain directors, an evaluation of the performance of the business and the fulfilment of its goals. In Sweden, board evaluation is addressed through the Corporate Governance Code which allows the results of board evaluations to be made available to the nominating body. In others the practices may not be formalised but are intended to inform the ownership entity on the future shape and membership of the board.

In Denmark, where formal self-evaluations are performed, they normally (in their entirety or as headlines) enter into the process of deciding on the optimal board composition and the identification of new board members, subject to discussions between the ownership Ministry and the Chair. Similarly, in Finland, board evaluations are not normally communicated to the ownership agency but "in the process preparing for the AGM the Chair discusses confidentially with the Director General of the OSD the performance of the Board as well as the additional skills needed, if any [...]. In this

discussion, the Chair might find it helpful to take advantage of the results of the evaluation process."

Good practice: Well structured board evaluations can act as a helpful tool informing the nomination process.

Notwithstanding the above examples, there are surprisingly few jurisdictions which formalise feedback loops (whether or not including actual communication of the outcomes of board evaluations) to the authorities responsible for the nomination process. Further, where results are made available, they tend to be used in an ad hoc fashion, rather than a systematic component of the nomination process. Many jurisdictions see the evaluation process as serving primarily for the improvement of the extant board and not necessarily as means to enhance the board composition.

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ANNEX A

*National board practices comparative tables**

* The Tables featured in this Annex describe the *status quo vis-à-vis* national policies and practices for the first half of 2012.

Table A.1. **Nomination framework**

	Responsibility for nomination	Required qualifications	Guidelines/constraints on member characteristics	Public, private and independent
Austria	The power of appointment is generally exercised by the ultimate owner, i.e. the ministry which administers the SOE. An exception is the special purpose privatisation agency where the board itself nominates and appoints new members.	Members of the supervisory board must have the "necessary qualifications and skills."	There is a quota for female representation – a minimum of 25% by the end of 2013 and then a minimum of 35% by the end of 2018. In general, board members shall not have more than ten appointments.	Both public and independent representatives. There are no regulatory/ policy limits.
Belgium	Appointment by Royal Decree following consultation amongst the council of ministers.	No formal requirements.	Board members are limited in the number of directorships they can hold. One third of the Board must be of the opposite sex. French and Dutch speakers should be equally represented.	Both public and independent representatives.
Brazil	One member nominated by the ministry of Planning, Budget and Management. Remaining members and Chairman nominated by the relevant sector ministry. All nominations require Presidential approval.	University degree required. Further qualifications are often set out in company by-laws e.g. "board members will be Brazilians with reputed knowledge and experience and high moral character".	Usually restricted to Brazilian nationals in the by-laws. Board members are not limited in the number of SOE appointments, but can only receive remuneration for a maximum of two.	Generally from the public sector.
Canada	For Crown Corporations (statutory) appointments are made by the Governor in Council on the advice of the relevant minister. For Corporations Law companies, appointments are nominated by the minister.	No formal qualifications.	No formal guidelines. Ministers are responsible for recommending candidates that reflect Canada's diversity (linguistic, regional and employment equity representation).	Almost exclusively independent.
Chile	Appointments are made by the Sistema de Empresas ("SEP") the centralised ownership function, according to a formalised procedure.	Qualifications are determined on a case by case basis, depending on the SOE.	Maximum number of SOE board appointments for an individual director is five.	Independent.

Table A.1. **Nomination framework** *(cont.)*

	Responsibility for nomination	Required qualifications	Guidelines/constraints on member characteristics	Public, private and independent
Czech Republic	Relevant shareholding Minister nominates members (based on Ministry advice) after consultation with Prime Minister.	Requirements include: professionally qualifications; experience in corporate governance; knowledge of economics and financial statements; knowledge of the Commercial Code.	Commercial Code requirements only, e.g. reasonable, educated, experienced and careful person.	No data.
Denmark	Board appointment by the AGM (per Companies Law). Board nomination formally rests with the relevant minister, but must be approved by an Appointment and Organisation Committee (comprising the Prime Minister and other key Ministers).	No formal qualifications.	State nominated board members must not be employees of the company, or civil servants. Increasing female representation is a goal, but there are no formal targets.	Vast majority of members are independent.
Estonia	Relevant shareholding Minister nominates members, with certain nomination rights reserved for the Minister of finance.	No formal qualifications.	Commercial code requirements, plus additional negative requirements to prevent potential conflicts of interest.	Informal rule is that the board members should be drawn 50% from the public sector and 50% from independent (private sector). In larger SOEs, the proportion of independent representatives is usually higher.
Finland	Board appointments made by the AGM (per Companies Act). State shares can be voted by the Minister (seldom), the Director General of the ownership function, OSD or his appointed representative.	No formal qualifications.	Ministers, Parliamentary Members and Senior Civil Servants should not be appointed as board members. Minimum 40% of either gender. No limit on the number of appointments, but this is taken into account when judging suitability of candidates. Members can serve for a maximum of 7 years.	One board member from the public sector to represent the state's strategic interests. The remainder are independent.

Table A.1. **Nomination framework** *(cont.)*

	Responsibility for nomination	Required qualifications	Guidelines/constraints on member characteristics	Public, private and independent
France	For Companies subject to the DSP Law (majority owned), board appointments are made by ministerial order. For partly owned companies, the appointment formally made by the ordinary general meeting. Nomination of government representatives is formally the responsibility of the Minister.	The legislation provides for certain qualified persons to fill the role of board member.	Laws introduced in 2011 require balanced gender representation.	Board members representing the Government must come from the public sector, or from majority public owned enterprises.
Germany	General assembly of shareholders elects board members. In SOEs where the State has a right to nominate members to the supervisory board, power of appointment is with responsible minister.	Knowledge, experience and expertise are required.	For large companies (> 500) employees have the right to appoint members to the supervisory board. In larger companies (500 to 2000) employee representatives elect ⅓ of non-executive directors. For the largest companies (> 2 000) ½ of supervisory board members are elected by employees (State and private enterprises are treated the same). Gender balance is required. Members of the board cannot have conflict of interest or more than 3 appointments at the same time, or cannot be appointed if to be imminently withdrawn from public service or office.	The state as a shareholder in some cases can appoint 1-2 members of the supervisory board. Generally a mix between public, employee and independent.

Table A.1. **Nomination framework** *(cont.)*

	Responsibility for nomination	Required qualifications	Guidelines/constraints on member characteristics	Public, private and independent
Greece	Board members are proposed by the relevant sector Minister and approved by inter-ministerial decision. In certain SOEs, parliamentary approval is also required.	Minimum requirements include a university degree and 5 years high-level executive experience.	Members of a board cannot be a member of another board, unless they receive no remuneration for the second position. One-third of state-appointees to boards must be from each gender.	n.a.
Hungary	Board nomination is formally responsibility of the Minister for National Development, but exercised by the Hungarian State Holding Company (HSHC).	No formal requirements. HSHC imposes a minimum requirement of a degree in law, economics or finance for Supervisory Board members.	No requirements.	Both public and independent representatives are utilised. There is no policy preference.
Israel	Appointments made jointly by the Minister of Finance and the Sector Minister. An Appointments Examination Committee vets all appointments to ensure that mandatory qualification requirements are met.	For all SOEs minimum academic and experience qualifications. For large SOEs, the Government Companies Authority establishes more detailed mandatory proficiency and suitability requirements for various types of board member.	Civil servants can be board members up to a maximum of ⅔ of the board (actual levels are much lower). Affirmative action provisions are in place for both gender and Arab representation on boards, but with no mandatory minimum requirements.	Civil servants cannot be more than two thirds of the board. Currently 22% of board members on SOEs are civil servants.
Italy	Board nomination and voting is exercised by the Ministry of Economy and Finance. In some SOEs this is done in cooperation with the relevant sector Ministry.	The company by-laws can establish specific qualifications regarding skill, independence and probity.	Board members of SOEs can sit on a maximum of five boards. One-third quota for women by 2015.	n.a.
Korea	Boards are divided into standing (executive) and non-standing (non-executive) board members. For the latter, the appointments are made by the Ministry of Finance and Strategy.	Formal qualifications are stipulated in the Act on the Public Institutions Management.	No formal requirements. Factors such as vocation, sex and native hometown are all considered to achieve balance.	No preference. Nominations made from candidates in various fields – academia, private and the government – is encouraged.

Table A.1. **Nomination framework** *(cont.)*

	Responsibility for nomination	Required qualifications	Guidelines/constraints on member characteristics	Public, private and independent
Latvia	There is no common approach to the responsibility for nomination.	Law requires that Supervisory Board members are persons who are fluent in national language, and have the experience, education and qualifications to perform their functions in a professional manner.	Board members can sit on a maximum of 3 SOE boards.	No data.
Lithuania	Boards of Directors are nominated by the relevant sector Ministry. For limited liability companies (LLC), an inter-ministerial selection committee recommends candidates to be approved by the Annual General Meeting. The concerned sector minister has veto rights. Candidates are suggested by the Governance Coordination Centre (ownership agency).	Qualification requirements are set by an inter-ministerial Selection Committee for LLCs. Specific qualifications may be required by the ownership Ministry on a case-by-case basis. General criteria are to be met (i.e. education, no conflict of interest, no prohibitions by law for candidature). The overall board should have a mix of finance, strategic management and specific industry knowledge.	Management cannot serve on the Supervisory Board, as per Company Law. Board members should not be regulators or policy maker in the same sector as the SOE. Employees cannot constitute board majority. CEO cannot be board chairperson.	For LLC, one-third of board members are to be independent.
Malaysia	"State leadership" is responsible, non-listed SOEs directors are appointed according to SOEs' articles of association. Vetting of independent director appointment rests with nomination committees of boards.	Leadership experience, national and regional background.	Encouraging board diversity, but also requirement to have mix of state, ex-officio, civil servants and employee representatives on boards.	Balance of independent and public directors desired, with mix of various stakeholders represented.
Mexico	Board composition is established by Company by-laws, and usually includes representation of relevant Ministries, appointed by the Head of each Ministry represented.	There are no formal qualification requirements, beyond "acknowledged honesty, prestige and experience in the activities performed by the enterprise". Individual SOEs may establish more detailed qualifications in their by-laws.	There are no limits on the kind of person nominated to the board. In practice, a majority of the board are public servants. The Chairman is usually Head of the Ministry in charge of the public programs related to the SOE.	n.a.

Table A.1. **Nomination framework** *(cont.)*

	Responsibility for nomination	Required qualifications	Guidelines/constraints on member characteristics	Public, private and independent
New Zealand	Directors are appointed by the Shareholding Minister following Cabinet approval. The central ownership unit (Crown Ownership Monitoring Unit) provides advice on skill requirements and potential nominees.	No formal qualifications.	Certain people are disqualified (i.e. current members of Parliament; current civil servants). There is an active effort to increase board diversity, but no targets or limits.	All independent representatives.
Norway	Board members are appointed at the shareholders meeting. Nominations are formally made by the Minister.	No formal qualifications. Emphasis placed on appointing representatives with broad experience of business and industry, and with specific expertise in defined categories.	State aims as far as possible, equal gender representation. Geographic, cultural and social diversity is also emphasised.	No data.
Pakistan	Generally, federal government and respective ministries appoint directors. According to SOEs' articles of association. For financial institutions, directors appointed from relevant ministry.	No requirements. Draft regulations considering requirements based independence, and diversity. And skill/ competence based. For financial companies persons must be "fit and proper".	Strategic SOEs must have board with a mix of 20 % government, 20% executive and 60% private members.	Balance desired but not required for non-listed companies.
Poland	Members are nominated by the State Treasury. Detailed formal policy on nomination and selection requirements.	A qualifying examination; minimum education and experience requirements.	Civil servants can be members on a maximum of two boards. Other persons are limited to board membership of one SOE.	No data.
Portugal	Decision is made by the Council of Ministers, or in some cases, by the Minister of Finance and the sectoral Minister. The decision is based on an opinion report issued prior to each nomination by the Committee on Recruitment and Selection for Public Administration for each appointee (newly established in 2012).	The Committee on Recruitment and Selection for Public Administration defines the applicable criteria in evaluating board candidates. Candidates must have integrity, professional merit, skills and management experience. A Bachelor degree is required.	Detailed conflict of interest provisions.	Currently about 25% are independent representatives.

Table A.1. **Nomination framework** *(cont.)*

	Responsibility for nomination	Required qualifications	Guidelines/constraints on member characteristics	Public, private and independent
Slovenia	Board nominations are made by the central ownership unit (AUKN).	Formalised policy on determining suitable candidates. Requirements include minimum education levels, 10 years relevant experience, references and a range of qualitative requirements.	Conflict of interest requirements. Members can sit on a maximum of three boards Gender quota of 40% for state-appointees on boards.	The Accreditation rules provide that civil servants and politicians are not to be considered for Supervisory Board membership.
Sweden	Board nomination is formally a decision of the ownership Ministry, but is a collective decision by the Government Offices.	No formal qualification requirements. Nominees chosen on a range of qualitative characteristics.	Gender target of 40%.	Companies with public service obligations tend to have a higher level of public sector directors. Nevertheless more than 90% of directors are from the independent.
Switzerland	Appointments are formally made by the General Assembly. For fully-owned SOEs, the Federal Council, as the sole shareholder ultimately makes the nomination.	Qualifications sought are fixed in a standard requirements profile and divided in three categories: a) for the board as a whole (e.g. team functions, strategic skills, relevant market and professional knowledge); b) for the single member (e.g. integrity, independence, professional and social skills); c) for the chair (specific leadership-skills).	There are no firm constraints or limits. Adequate representation with regard to gender and language minorities is stipulated in the principles on corporate governance.	Mainly independent, but for some companies, the nature of their operations (e.g. Swiss Post) means public sector experience is considered an important attribute.

Table A.1. **Nomination framework** *(cont.)*

	Responsibility for nomination	Required qualifications	Guidelines/constraints on member characteristics	Public, private and independent
Turkey	Directors are nominated by the relevant line Minister, with one member nominated by the Treasurer. All nominees are appointed by joint decree of the nominating Minister, Prime Minister and President. For companies in the Privatisation Portfolio, all members appointed by the Prime Minister.	University degree and adequate experience.	All appointees must be Turkish nationals.	Predominantly public sector, but independent representatives are possible.
United Kingdom	Power of appointment rests with the Secretary of State of the Ministry sponsoring the SOE.	No formal qualifications established. Appointments are based on the experience of the Board member, their knowledge of the sector in which the SOE operates, and the relevance of these skills to the company.	No formal constraints apply. All appointments should be available on fair and equal access to ensure that all sectors of society are represented.	Overwhelming majority is independent. Shareholder Executive representatives can sit on Boards where there is a need for a public presence.

Table A.2. **Selection and appointment processes**

	Vetting, identification or accreditation processes	Role of the board in identifying candidates	Role of non-government shareholders
Austria	In general, the directors are proposed by the ownership unit and approved by the corresponding minister. Directors are nominated due to their qualifications and skills by the ownership unit. In exceptional cases, head-hunters are used.	None.	Non-government shareholders can nominate candidates in proportion to their shareholding.
Belgium	Appointees are chosen according to their capacities in specific fields (such as accounting, legal financial or investment experience).	n.a.	Certain director positions are reserved for appointment by general meeting of shareholders on the proposal of an external jury.
Brazil	Ministers are free to define the process for choosing board representatives. It is common for ministers to propose board members directly, and equally common for the ownership unit or relevant Ministry to have lead responsibility.	n.a.	Various voting procedures for board members (such as guarantee of board members for 15% voting capital) guarantees Minority shareholder board representation.
Canada	There is no formal oversight mechanism for vetting or proposing names of potential directors. In some cases, the establishing legislation provides for the creation of nomination committees.	Formal board profiles are established and maintained by the Board which guide future government decisions on possible nominations.	n.a.
Chile	A pool of candidates is maintained from past appointments. When a vacancy arises, potential applicants can be drawn from the pool; from a Pension Fund list of independent candidates; from new applications; recommendations from SEP staff; or via the use of head-hunters. Head hunters are commonly used, particularly for Chairmen roles in large SOEs or for SOEs facing particular challenges.	SEP's board evaluation is used to identify skill gaps or compositional weaknesses. Board itself does not have a role in the nomination process.	Minority shareholders can nominate directors at the AGM.
Czech Republic	The relevant shareholding Ministry proposes candidates which must be approved by the Prime Minister.	None.	Minority shareholders have the rights according to the company statutes and the Commercial Code.

Table A.2. **Selection and appointment processes** *(cont.)*

	Vetting, identification or accreditation processes	Role of the board in identifying candidates	Role of non-government shareholders
Denmark	The minister/ministry and chairman jointly address board nominations; formulate required skills/experience; identify potential candidates; and prepare a shortlist. Minister presents the proposed nominees for approval to an Appointment and Organisation Committee. Finally, the chosen candidates are approached and typically interviewed by the Chairman.	The Chairman is involved at all stages of the process.	Where there are shareholder agreements, these usually preserve a right to appoint an agreed number of members. In dispersed shareholding companies, either nomination committees have been established, or informal contacts with other large shareholders may take place.
Estonia	The processes adopted are informal. There is no public advertisement and proposals are made by the senior executives of the ministry.	No formal role. The Chair may be consulted informally.	All board members are appointed by the shareholders meeting. The Articles of Association may contain provisions to guarantee proportional representation.
Finland	A Directors' Pool is maintained by an external recruitment consultant (procured through a competitive process). The recruitment consultant identifies potential candidates, and any applications received by Government are conveyed to the consultant.	The Chairman is consulted by OSD on the board's performance and the skills/attributes required well in advance of the AGM.	Where there are a limited number of shareholders, then shareholder agreements specify board representation. Shareholder nominations committees are used in listed companies and in one SOE with a wide shareholder base.
France	Directors that are appointed by decree or order are first proposed by the Agency for State Holdings (APE). APE maintains a pool of administrators filling the professional profile required of potential directors.	n.a.	Voting rights are exercised according to the company's law.
Germany	For direct appointments, directors proposed by the ownership unit subject to approval by minister. There are no committees or pools. Outsiders may not apply.	n.a.	For joint stock companies: Minority shareholders propose candidates. Proportional allocation may be considered, but no cumulative voting rights.
Greece	All vacancies are advertised. Potential candidates are screened by the relevant line Ministry according to the qualification criteria (i.e. education, experience). The Minister's preferred candidate(s) are subject to inter-Ministerial approval.	n.a.	Voting rights are exercised according to the companies' law.

Table A.2. **Selection and appointment processes** *(cont.)*

	Vetting, identification or accreditation processes	Role of the board in identifying candidates	Role of non-government shareholders
Hungary	The HSHC either approaches potential candidates directly or uses publicly distributed job vacancies. Ministers have no role in the selection process.	The Chairman (and potentially other board members) is consulted during the selection process. Board evaluations (which are compulsory) are also used in the selection process.	Non-government shareholders are consulted through the nomination process, and appointments are made at the AGM. Minority shareholders have the capacity to nominate board members.
Israel	Candidates are proposed by the relevant Minister and Minister of Finance. There is no formal procedure, although candidates have to meet the qualifying criteria. To do this, candidates must complete a detailed questionnaire which is provided by the Ministers to the GCA and Appointments Examination Committee. GCA provides an opinion on the candidates; Committee uses this information and the questionnaire to determine whether the candidate has the required qualifications.	None.	Rights of non-Government shareholders set in the Companies Law and the Articles. Nominations are not subject to the Governmental procedures.
Italy	The Ministry of Economy and Finance co-ordinates all nominations.	n.a.	Board representation for Non-government shareholders is facilitated through cumulative voting arrangements.
Korea	No consistent process. In general the Executive Nomination Committee proposes a long list to the Public Institutions Management Committee (centralised ownership unit), who prepares a short list for the ultimate decision maker.	Executive Nomination Committee develops the "long list" which is referred to the Public Institutions Management Committee.	n.a.
Latvia	Currently there are is no common practice. Methods used include: open competition; and use of recruitment consultants.	None.	The Commercial Code allows any shareholder with 5% voting rights to nominate board members.

Table A.2. **Selection and appointment processes** *(cont.)*

	Vetting, identification or accreditation processes	Role of the board in identifying candidates	Role of non-government shareholders
Lithuania	A database of candidates has recently been established by the Governance Coordination Centre. Although sector ministries and the Selection Committee are not obliged to consult it, the database is expected to be used more regularly in the future of identification of independent board members. Potential applicants may submit their names for consideration; relevant ministries may also submit candidates. For LLC companies, the sector Minister has a veto right to reject candidates approved by the inter-ministerial Selection Committee.	None.	As per the rights contained in the Companies Law.
Malaysia	Potential directors identified by investment corporations (Khazanah or Permodalan). Independent generally drawn from pool set up by corporate governance institutions.	Board nomination committees vet appointments.	n.a.
Mexico	Generally the board opening must be filled by a specific civil servant appointed by the head of the respective Ministry.	None.	As per the Companies Law.
New Zealand	Candidates for vacancies sought from a wide variety of sources, including advertisement/database/ Chair or board nomination/ diversity agencies. COMU prepares lists for Minister's consideration. Due diligence conducted. Minister consults with Cabinet and decides.	Chair input sought for new appointments.	n.a. (all companies 100% owned).
Norway	The preparatory work for the nomination of board members in non-listed companies is carried out by the ownership department itself. The process is not contestable; board vacancies are not advertised.	The board of directors' evaluates its composition and functioning, both individually and as a group. These reports are available to the nomination committee, to use as one of several sources to identify board's needs/characteristics.	The preparatory work for the nomination of board members in listed companies is carried out through separate nomination committees, involving all shareholders. At least two of the members of the board elected by shareholders should be independent of the company's main shareholder.

Table A.2. **Selection and appointment processes** *(cont.)*

	Vetting, identification or accreditation processes	Role of the board in identifying candidates	Role of non-government shareholders
Pakistan	Federal government selects from a pool of candidates. For independent directors of financial companies, appointments are to be made from a pool of professional directors maintained by respective ministries. Names can also be provided by the Chief executive.	Independent directors elected by directors in general meetings.	For listed companies: Cumulative voting system. Where government is less than majority shareholder, consults with non-government shareholders and nominates one representative to board.
Poland	The State Treasury can appoint civil servants to be a board member in SOE or start the open competition process. During the competition regarding companies of key importance, recruitment consultants can be utilised to "search and verify candidates meeting requirements and criteria specified for the proceedings, to receive the required documents from them and accept their statements."	None.	The Commercial Code provides rights for minority shareholder to appoint board members (by group voting of shareholders cumulatively having minimum 20% of voting rights). In some cases, the State Treasury has co-ordinated with other shareholders to agree a candidate.
Portugal	Vetting and accreditation will be performed by a newly created Recruitment and Selection Committee according to yet to be published criteria.	Not yet defined.	Not yet defined.
Slovenia[1]	An Accreditation Committee of the ownership entity (AUKN) maintains a pool of accredited candidates and then selects a number of potential candidates for each board opening.	AUKN meets quarterly with the Supervisory Boards of SOEs. Boards can communicate the skills/characteristics they consider are required.	Informal negotiations usually take place between the major shareholders. Directors are usually nominated according to respective shareholdings.
Sweden	Working group analyses the current skills needs of the board and its composition. Recruitment profiles are developed and used to identify possible candidates.	Chairman provides feedback on the board evaluation process.	In listed companies, state representatives sit on the nomination committee. In non-listed companies there are usually shareholder agreements setting out appointment rights.
Switzerland	Ownership unit works with the board (either a committee or the chairman) to identify needs and evaluate potential candidates based on the standard requirements profile. Short listing of candidates occurs with external consultants. There is no pool of candidates or advertising, but process is basically open.	Board works through a committee or chair in concern with the ownership unit.	All fully state owned.

Table A.2. **Selection and appointment processes** *(cont.)*

	Vetting, identification or accreditation processes	Role of the board in identifying candidates	Role of non-government shareholders
Turkey	Candidates are identified internally, and are not contestable or advertised.	None.	Private shareholders can nominate one member for each 20% shareholding.
United Kingdom	Positions are advertised, and often recruitment firms are used. Shareholder Executive and the SOE develop a shortlist for interview. Preferred candidates are recommended to the Minister.	The SOE is involved in developing the specification for the position, identifying and interviewing the shortlist.	As per their voting rights or, where they exist, the shareholders' agreement.

1. At the time of producing the present report, a major legal overhaul of the Slovenian SOE sector was underway. However, the said policy documents were still in force.

Table A.3. **Remuneration of board members**

	Remuneration limits	Remuneration levels impacting candidate quality	Role of the board
Austria	No specific limits. The remuneration for SB members of Austrian companies is generally low.	No.	None. Remuneration is decided by the AGM.
Belgium	Remuneration set by the general meeting of shareholders.	n.a.	Remuneration committee makes a recommendation to the shareholders meeting.
Brazil	10% of median managers salary.	No.	No.
Canada	Fixed fees based on a ten level remuneration structure.	No.	None.
Chile	No limits, but in practice SOE board members are less well remunerated than the private sector.	No data, but current candidates are very highly qualified.	No.
Czech Republic	Set according to 2009 Principles for Remuneration of Management and Board members of Corporations with State Shareholding above 33%	For managerial positions.	Supervisory Board sets Management Board remuneration.
Denmark	Remuneration should be competitive. In practice it is below the private sector.	Possibly, but no evidence.	Minister and Chairman discuss prior to the AGM, which sets policy.
Estonia	Remuneration levels are set according to Ministry of Finance regulation.	No data.	No.
Finland	No express limits. Set by reference to the size and complexity of the business. Lower than private sector equivalents.	Sometimes argued by Chairmen, but not supported by evidence.	No.
France	Non-executive directors receive a fixed annual sum. There is no government legislative limit.	n.a.	The Board sets individual remuneration within the envelope set by the shareholders meeting.
Germany	Fully-owned SOE, no remuneration for board members, except reimbursement of expenditures. Other companies, as stipulated in companies act.	No.	Board can present proposals to shareholders' meeting.
Greece	EUR 300 per month for members. EUR 400 per month for President, plus an additional fee depending on size and nature of the SOE.	Possibly.	No.
Hungary	HSHC Guidelines: Chairman salary limit to 5 times the minimum wage, and members limited to 3 times the minimum wage.	No.	No.
Israel	Fixed sum per meeting set by regulation according to the company ranking. Civil servant directors receive no remuneration.	No data.	No. Board could lobby to change company ranking to improve remuneration.

Table A.3. **Remuneration of board members** *(cont.)*

	Remuneration limits	Remuneration levels impacting candidate quality	Role of the board
Italy	Minister of Economy and Finance establishes minimum and maximum remuneration levels.	No data.	Remuneration Committee of the board establishes remuneration subject to constraints set by AGM and the Minister.
Korea	No statutory limits or policy on remuneration.	No data.	Board sets remuneration in accordance with the establishment laws or by-laws.
Latvia	Fixed percentage of CEO salary (20% for Chairman; 15% for members), subject to not being less than the minimum national wage.	No.	None.
Lithuania	Ownership guidelines recommend that remuneration of supervisory board members does not exceed ¼ of CEO remuneration; chairman's remuneration should not exceed ⅓ of CEO remuneration.	No data.	Board makes a recommendation to the AGM.
Malaysia	No limits, in accordance with industry practices and linked to performance and responsibilities. Based on shareholders' vote.	n.a.	Remuneration committees submit proposals as stipulated under terms of reference.
Mexico	Civil servants receive no remuneration. Independent members' remuneration set according to Government guidelines.	No.	No.
New Zealand	Board fees set by the Minister of SOEs according to a Cabinet approved COMU fees framework that ranks SOEs according to bands. Rates benchmarked to private sector but in practice below private sector levels.	No.	No.
Norway	No formal limits. The objective is that remuneration should be moderate compared to private sector companies.	No.	No.
Pakistan	No limits, amount should not compromise independence.	n.a.	Board determines scale of remuneration for non-executive directors.
Poland	For fully owned SOEs, set by the Law on Remuneration of Persons Managing Certain Legal Entities (2000). For minority owned SOEs, set by the AGM. In both cases must be not more than agreed multiple of average salary.	No data.	No.

Table A.3. **Remuneration of board members** *(cont.)*

	Remuneration limits	Remuneration levels impacting candidate quality	Role of the board
Portugal	Maximum of one quarter of executive directors, or one third if represented on board committees.	No.	No.
Slovenia	Limits set in Criteria for Remuneration of Members of Supervisory Boards of Companies with State Capital Investments, established by AUKN. Members receive sitting fees and an annual payment.	Recent increases in fees have helped attract better candidates.	Boards can make a proposal on the amount of yearly payment.
Sweden	AGM votes on board fees. Fees should be competitive but not market leading. Analysis suggests that SOE board fees are less than 50% of market. Civil servant members receive no remuneration.	In some cases, the low level of board fees has made it hard to attract candidates.	No.
Switzerland	Federal Council issues principles of remuneration. There are no limits in these principles, with a focus on transparency and coherence. As the sole (or majority responsible) shareholder, the Federal Council has established remuneration levels for SOE board members and chair persons by specific provision.	Remuneration is lower but non-monetary benefits potentially compensate.	The board proposes remuneration to the General Assembly according to the parameters established by the Federal Council.
Turkey	Determined annually by the Supreme Planning Council, which is composed of various Ministers and chaired by the Prime Minister.	No data, but remuneration is usually lower than the private sector.	No.
United Kingdom	Remuneration for Board appointments relating to appointments onto the Boards of those businesses which are the responsibility of the Dept for Business (BIS) are required to be approved through the Senior Remuneration Oversight Committee (SROC). Any remuneration package that exceeds the salary of the Prime Minister (currently GBP 142 000 pa) requires the additional approval of the Chief Secretary to the Treasury.	Yes. Public interest in ensuring senior remuneration packages are at a level acceptable to the public during difficult economic times, has made it increasingly difficult to secure the right people for the role.	Yes. It is usual for the Remuneration Committee (or if there isn't one the Company Secretary) to prepare proposals for a "remuneration framework" which informs the discussion about the remuneration of individual appointments.

Table A.4. **Board evaluation processes**

	Ownership entity evaluation	Board self evaluation	Feedback into nomination process
Austria	None to date.	No data.	No data.
Belgium	n.a.	The independent directors draw up a yearly report for shareholder review.	No data.
Brazil	No. Receives a copy of the board self-evaluation.	Annual self-evaluation, as a group and individually, according to a detailed questionnaire.	Process has just commenced. In future may feed into nomination process.
Canada	No formal reviews. Performance audits and ad hoc reviews do sometimes address board performance in crown corporations.	Not mandatory, but these are encouraged. The Treasury Board Secretariat has established a set of non-binding guidelines on the conduct of such reviews.	Chairpersons are required to communicate the findings of their self-assessment to the relevant Minister. Assessments are not used systematically to feedback into the nomination process, but this does happen on an informal basis.
Chile	Annual evaluation by SEP, conducted by external specialists (e.g. Corporate Governance Centres). Focuses on the board as a whole, and includes both mechanistic elements and performance.	Boards participate in the SEP review, via completion of a survey.	The evaluation process forms part of the inputs into the nomination process, together with interviews with the chair and certain directors, an evaluation of the performance of the business and the fulfilment of its goals.
Czech Republic	External advisers (auditors) are engaged to conduct reviews of Supervisory Board performance on an ad hoc basis. Assessments are performance based.	Supervisory Boards are required to complete a report on activities at least annually. Completed self evaluations are discussed with the shareholder.	Both the external audits of performance and the self reviews are used as an input into the board composition, particularly at the expiry of the Supervisory Board's mandate.
Denmark	No top-down evaluations.	Annual self-evaluations are recommended and commonly conducted. These can be formal survey based evaluations or more informal. They are generally performance-based reviews.	Formal self-evaluations will normally enter into the process for deciding future board composition, in the discussions between the Minister and the Chair.
Estonia	No formal process. Informal reviews are conducted through SOE monitoring.	Formal reviews are conducted as per the Companies Law and reported to shareholders annually.	Informal review of performance is part of the renewal process for Board members.
Finland	No ownership initiated evaluations.	Boards undertake annual evaluations with flexibility as to the approach adopted. Questionnaire based exercises and the use of external facilitators is common.	The self evaluations are not normally communicated to the ownership entity, OSD – they are focused on assisting the board improve its performance. The Chairman nevertheless will discuss the performance of the board with OSD prior to the AGM.
Germany	No data.	No data.	No data.

Table A.4. **Board evaluation processes** *(cont.)*

	Ownership entity evaluation	Board self evaluation	Feedback into nomination process
Greece	No specific processes.	The Audit Committee is responsible for evaluating the performance of executive board members.	No specific processes.
Hungary	Quarterly ownership assessment meetings where state ownership is greater than 50%. Board members are invited to attend.	The Supervisory Board can conduct a review of the performance of the executive officers.	Evaluations are used to frame future nominations.
Israel	No formal process. An evaluation of a director will take place at the time of re-nomination.	No formal processes.	At the time of re-nomination of a director, the GCA will assess a director's contribution to the board's work.
Italy	No data.	No data.	No data.
Korea	The ownership agency does not conduct evaluations, but the Ministry of Finance and Strategy conducts annual evaluations of performance of SOEs, including board performance.	No data.	Performance evaluations are used as a basis for considering appointment for a further term.
Latvia	No.	Yes, as part of the annual report to Shareholders.	Not specifically, but implicitly because it feeds into shareholder decision making on board nominations.
Lithuania	Governance Coordination Centre monitors implementation of Ownership Guidelines according to objectives, strategic plans, financial reports and suitability of legal form.	The board evaluates its own performance at the end of the financial year (or when board term ends).	Self-evaluation is submitted to ownership entity and Governance ation Centre. If a competency is needed/lacking the Governance Coordination Centre proposes to replace or appointment new members.
Malaysia	Top down evaluation of each board for listed companies annually or biennium.	Recommended in the form of peer assessment of by the Chairman. Chairman evaluated by the board as a whole. Based on performance measures and assessment of the boards collective performance.	Generally encouraged.
Mexico	Board performance is evaluated by an Internal Monitoring Body appointed by the Secretariat of the Civil Service. Reviews are performance based.	No.	No.
New Zealand	No. COMU does not receive copies of board evaluations but receives high level feedback on board performance.	Each board must undertake an evaluation at least annually of the performance of individual directors, the chair and the board as a whole. No prescribed processes.	Feedback from the evaluation process feeds into decisions regarding board succession, director development, and board composition.

Table A.4. **Board evaluation processes** *(cont.)*

	Ownership entity evaluation	Board self evaluation	Feedback into nomination process
Norway	No.	The board of directors does an evaluation of its own performance including an evaluation of the composition of the board and the manner in which its members function, both individually and as a group.	The board evaluation is provided to the nomination committee as an input into its work.
Pakistan	No formal process, but controlling ministry reviews company and CEO performance. Draft regulation underway recommends formal board evaluation.	n.a.	n.a.
Poland	Periodic evaluations covering both performance of the board and mechanistic elements.	No.	Negative evaluations of board members can lead to motions for changes to the board at the AGM. If the board member is not given endorsement at the AGM (with the consent of State Treasury),s/he is in effect removed from the board and cannot represent the State Treasury on a board for the next 3 years, but this does not hold s/he from being private shareholder representative.
Portugal	As shareholder, receive annual self evaluation from the board and vote on it at the AGM.	Annual self-assessments of performance based on fulfilment of the defined company objectives.	Via the AGM.
Slovenia	No independent evaluation. Receives the board evaluation reports, and votes on these at the AGM.	Annual self-evaluation according to a manual on self evaluation for boards prepared by the Slovenian Directors Association.	AUKN will utilise the evaluation reports in the nomination process for candidates (2011 is the first year of operation).
Sweden	Receives a report from the Chair on the annual evaluations. Conducts their own evaluations for the purposes of board nominations.	Board self-evaluation must occur annually. This covers qualitative and quantitative criteria. Facilitators are often used.	The Government Offices use both the self-evaluations and their own evaluations to inform the nomination process.
Switzerland	Board performance is reviewed on a regular basis against strategic goals: annual reporting of performance; chairman reporting 4 to 6 times per year. Board performance is assessed as a whole.	Not required, but does occur for the board's own purposes.	No institutionalized process. Evaluations can influence future (re-)elections.

Table A.4. **Board evaluation processes** *(cont.)*

	Ownership entity evaluation	Board self evaluation	Feedback into nomination process
Turkey	No.	No.	No.
United Kingdom	Shareholder Executive will appraise the performance of individual Board members on an ad hoc basis. At a minimum, this would be part of an annual Investment Review of each business. There is also a regular review of Board performance and composition (internal annual review by the Company and, in some cases, a full review every 3 years by ShEx).	There is an expectation that the Chair of the SOE will perform an internal annual review of Board performance. These could be self evaluations or using external facilitators depending on the issues prevalent at the time. It is more often the case that the performance of the Board is evaluated as a whole rather than at an individual level.	The Board self-evaluation informs the ongoing discussions between the Chairman and Shareholder Executive about the future shape and membership of the Board.

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Corporate Governance

Boards of Directors of State-Owned Enterprises

AN OVERVIEW OF NATIONAL PRACTICES

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