Summary

This Guide is intended to facilitate the practical implementation of the *OECD Guidelines on Corporate Governance of State-Owned Enterprises* (the "SOE Guidelines"). It is focused on ensuring a high quality of transparency and accountability, which is the very basis of any sound corporate governance regime. It aims to help evaluate existing practices, identify their strengths and weaknesses and provide examples of successful practices. The Guide provides viable policy options and a "road map" of the practical steps that might be taken to implement the *SOE Guidelines*, pointing at typical difficulties, risks and hurdles that may be encountered during the implementation process. It also provides examples that illustrate the implementation of provisions and can serve as references and inspiration to governments that are confronted with similar challenges.

This Guide has been developed by the OECD Working Group on Privatisation and Corporate Governance of State-Owned Assets. It also strongly benefited from a broad consultation with non-OECD countries, within the framework of the Global Network on Privatisation and Corporate Governance of State-Owned Enterprises.

The Guide covers all relevant accountability and transparency recommendations in the *SOE Guidelines*. These recommendations have been grouped into five broad areas, namely setting objectives, reviewing performance, auditing performance, reporting on performance and disclosure by individual SOEs.

Enhancing transparency and accountability is a central recommendation of the OECD Guidelines: "*The state should act as an informed and active owner … ensuring that the governance of state-owned enterprises is carried out in a transparent and accountable manner, with the necessary degree of professionalism and effectiveness*" (Main Guideline, Chapter 2). It gives substance to shareholders' rights by providing the information essential to their exercise. It is also a remedy of choice for fraud and market manipulation. Finally, it is a prerequisite to, and underpins, public trust. Enhancing transparency and accountability entails complex challenges but is also an efficient entry point for further SOE governance reforms. It is politically feasible, suitable for gradual implementation and effective in mobilizing support for further reform.

This Guide is primarily directed at ministries and other government branches charged with assisting national reform efforts. Other users may include Parliaments as well as independent evaluators that seek a tool to make an assessment of the accountability and transparency framework and practices.

Like the *Guidelines* themselves, the Guide is "outcome-oriented". Rather than being prescriptive in terms of specific provisions, it acknowledges that there may be different ways to achieve the same outcome. The existence of competitors, of minority shareholders, the specific legal status of the SOE concerned, as well as the way the

ownership function is organised within the state administration might all have a non-trivial impact on the way the Guidelines are implemented. There is not a "one size fits all" approach. This Guide, for example, refers to the "ownership entity" to cover different ownership models as identified by the Survey of Corporate Governance of SOEs in OECD countries (OECD, 2005). Most of the recommendations made or policy options described in this Guide concern mainly non-listed SOEs. As soon as SOEs are listed, the state will have to exercise its shareholder rights but will not be more than a significant or controlling shareholder. Market mechanisms then apply, as well as listing regulations. International standards in terms of transparency and accountability do apply in this case; any additional transparency measures that governments apply should complement, and be consistent with, such standards.

Setting objectives

Accountability can be greatly facilitated by a process of performance benchmarking against clearly defined objectives. This requires defining objectives at different levels: firstly, for the state as an owner, with the "ownership policy" for high-level and long-term objectives and then specific yearly targets; secondly, for the SOEs themselves, with their high-level mandates, then their yearly objectives with specific performance indicators.

Since state ownership is often characterised by vague, complex or contradictory objectives, improvement in setting objectives is typically the very first step towards better accountability. At the aggregate level, the government should define its own overall objectives and ownership practices. An effective way of doing so is by developing an **ownership policy for the state shareholder**, as recommended in Guideline II.A (Section 1.2). An ownership policy serves as an effective tool for public communication and provides companies, the market and the general public with a clear understanding of the state's objectives as an owner and of its long-term commitments.

The ownership policy is a short but high-level policy document providing a clear statement of the state's overall objectives as an owner. Such overall objectives could also be defined at a sector level. In addition, it is useful if the ownership policy defines the mandate given to the ownership entity, its main functions and organisation, as well as the main principles followed in exercising the state ownership rights. Finally, it could also provide a summary of the main reference documents that define or frame the exercise of ownership rights by the state.

Developing an ownership policy is often an iterative and inclusive process that may involve several parties and wide consultation. It is based on directions received from the government on its ownership objectives, as well as on an appropriate survey of existing documents and their effective implementation. To improve its relevance, broad understanding and support, the ownership entity might consult with all concerned entities (the relevant parliamentary committees, other concerned ministries, the state audit institution, relevant regulators, etc.). It could also be fruitful to consult broadly with board members and management of SOEs and make appropriate use of public consultation to test the market and political reaction. Once the ownership policy is finalised, it is important to obtain and demonstrate high-level political support to reinforce its credibility. The ownership policy could also be endorsed by relevant public servants, publicly disclosed and widely circulated.

Based on the general objectives that are formulated in the ownership policy, it is useful to identify more specific **targets for the ownership entity** (Section 1.3). Doing this allows communication and evaluation of the ownership entity's performance, as called for in Guideline II.E. Targets could be both quantitative and qualitative, including financial targets covering the whole state portfolio, as well as the combined value of this portfolio. An aggregate **unique target** to increase this value, or a significant portion of the portfolio by a certain per cent over a specified time, is appealing in terms of simplicity. However, it has some inherent limitations and needs to be supplemented by sub-targets for the most important SOEs. Whatever the targets chosen, they will always represent imperfectly the real performance of the ownership entity. An appropriate mix of targets should be selected, with appropriate consideration given to aggregation difficulties. They also need to be discussed widely internally to analyse their practical impact on individual civil servants' motivation and behaviour. When discussing targets, focus should be on their relevance, ensuring that they have a close link with the overall objective of state ownership. They need to effectively reflect the performance of the ownership entity, with due consideration for market and business environment.

The process for formulating targets may vary depending on the institutional setting and the organisation of the ownership function. However, it is essential that all institutions that have a say *ex post* in evaluating the ownership entity's performance be somehow included in discussing its objectives *ex ante*. This may include the Parliament, relevant ministries, state audit agencies, etc. Finally, the overall targets of the ownership entities, as agreed with the government, should be clearly disclosed.

In fully owned companies, it is necessary for the state to **define and review SOEs' mandates** (Guideline V.E.1 and Section 1.4), *i.e.* simple and brief descriptions of the high-level objectives and missions of the individual SOEs in the long run. Clear mandates are necessary to build up appropriate accountability and as a basis for discussing more specific yearly targets. SOE mandates usually define the main lines of business and provide some generic indication regarding the ambition in terms of market leadership, quality of service or innovation and financial sustainability. They quite often show a clear mix of commercial and policy objectives and need to give some clear indication of how to articulate the trade-offs between the two. Mandates are intended to be valid over a long period of time and updated only in the event of fundamental changes. They should be publicly disclosed, posted on the individual SOEs' websites and clearly stated in annual reports.

The process of defining and reviewing SOEs' mandates is carried out by the state, mostly the ownership entity. But the ownership entity, in doing so, should also discuss with SOEs' boards and their chairs, as well as check appropriately existing documents which either define the missions of SOEs or provide the general framework to do so. SOE mandates should be reviewed periodically and systematically to maintain their relevance and consistency with the overall ownership framework and economic environment. Mandate reviews could be done internally, *i.e.* by the SOE and the ownership entity, conducted by independent panels with full public input and contracted experts, or by relevant parliamentary committees. Whatever the process, it needs to be done in a transparent manner and with appropriate consultation of stakeholders concerned.

Based on their overall mandate, and as a preliminary step to setting **specific objectivesand targets at the company's level** (Guideline VI.A), it is necessary to clearly **identify any public services and other special obligations,** decide on their relevance**,**

evaluate their cost and fund them transparently (Section 5). This is essential to ensure a level playing field with the private sector, as their costs might be high and are often hidden or at least not easily identifiable. These "special obligations" usually have a significant impact on SOEs' performance and the risks they face. Clear identification and costing allows an informed public debate about their relevance, their budgetary implications as well as their distributional consequences. It is an important but complex undertaking that requires time, method and a good deal of discussions and negotiations between the ownership entity, the SOEs themselves and in many cases the relevant stakeholders.

After agreeing on a clear definition of what constitutes a "special obligation", which is not trivial, the ownership entity might require SOEs to identify and **map existing** "**special obligations**". SOEs are also required to provide information on their actual cost, based on a consistent methodology in order to reduce inconsistencies among SOEs and make benchmarking easier. This is not a straightforward exercise and will in many cases require discussion as well as trade-offs between precision, time and resources. Once duly identified and costed, these special obligations will have to be reviewed, to ensure their relevance and effectiveness and make them the result of a well thought-out process and explicit political decision. This review would assess to which point these special obligations could be replaced by other mechanisms and how they could be funded in order to achieve the same objectives at a lesser cost, more effectively and/or without having the same impact in terms of market distortion and/or SOE efficiency. The state should also monitor the effective fulfilment by SOEs of their special obligations.

Once the "special obligations" and their costs have been reviewed, it is crucial that the government's expectations of the (fully owned) SOE be formally, clearly and publicly communicated in the form of "objectives documents". These documents might be relatively short and agreed usually on a yearly basis. They clarify high-level expectations and specific objectives agreed upon between the ownership entity and the SOE boards, and must be duly approved by the general shareholder meeting whenever appropriate, for example for partially state-owned enterprises. Objective documents include financial objectives (including sustainable dividend levels) and related performance indicators allowing measurement, following-up and assessment of SOEs' profitability, efficiency and risk level. It is also useful for the objectives document to include, but not necessarily publish, estimation by the boards of the company value, with relevant information on the methodology used and assumptions made. Objectives documents also increasingly include performance indicators for non-financial and public policy objectives, as well as some more "structural" objectives, related, for example, to governance or human resources policy.

The development of an objectives document (Section 1.6) is generally a collaborative process with ongoing communication between the SOE itself (its board and CEO) and the ownership entity. It is useful to formalise this process in order to clarify the requirements in terms of content, time frame and respective responsibilities and powers. Based on communication by the government of its high-level objectives, under the form of "letters of expectations", for example, SOE boards are expected to submit draft objectives documents describing main objectives for the SOE, key performance indicators and specific yearly targets. The informal negotiation of the draft is key to building consensus and ensuring clarity. Formal feedback has to be received from the ownership entities within a defined time limit. The final document should be officially approved, clearly endorsed, in some cases tabled in Parliament and always publicly disclosed.

Developing objectives documents is also a complex task which requires a combination of industry knowledge, financial capability and operational experience. These competencies need to be present in SOE boards and reflected within the ownership entity to allow an informed and balanced dialogue. The whole process also raises important questions about the respective roles of the board and the ownership entities and can be perceived by the boards as a usurpation of their authority. It thus requires a delicate balance that respects the board in the exercise of strategic control.

A central but technical difficulty in this process is to **develop relevant performance indicators** (Section 1.7). Performance indicators, by definition, are not exact measures of performance but "indicate" the level of performance regarding the overall objectives agreed upon. They are practical attempts to improve the quality and consistency of performance measurement by focusing on key synthesis indicators. An extensive literature provides "tips and traps" in developing these indicators. A commonly used "tip" to build-up effective performance indicators is to make sure that they are "SMART", *i.e.* Specific, Measurable, Achievable, Result-oriented and Time-based. Whatever the acronyms used, the quality of the indicators depends on three major characteristics: their relevance, accuracy and reliability. As for the target levels, they have to be challenging but achievable, based on historical performances, benchmarking against peers and an assessment of effective capabilities. Appropriate information systems and structures could be put in place to collect accurate and reliable data necessary for calculating the indicators, possibly extracted directly from the information systems. Actual results need in turn to be duly documented, showing results for previous years accompanied with measures of uncertainty as well as data sources and methodological information, when relevant. Finally, performance indicators should also be audited and reviewed regularly to ensure their reliability and maintain their relevance. Badly chosen performance indicators might bias the incentive structures and consequently have serious perverse effects or unintended consequences.

Reviewing performance

A state's obligation to review the performance of its portfolio companies is central to the OECD Guidelines: "*Its prime responsibilities include setting up reporting systems allowing regular monitoring and assessment of SOE performance*" (Guideline II.F.3). To review performance effectively, the ownership entity must first ensure that it has access to accurate and relevant information on a timely basis, and monitor the performance of portfolio companies both on an ongoing and annual basis.

The system for **ongoing performance review** (Section 2.2) tracks and reviews performance on a regular basis, ensuring early identification of problems and opportunities and allowing prompt reaction to under performance. It typically combines, in accordance with corporate and capital market law, formal and more informal mechanisms, including state representatives on boards, meetings with boards and senior management or more formal reporting processes. Systematic processes might be developed to allow collecting data directly from the SOEs' information systems. "No surprise" or continuous disclosure policies could also be adopted, requiring SOE boards to keep the ownership entity informed in a timely manner about any material or significant events. Complementary information channels might be used, such as dialogue with external auditors, contact points in SOEs and use of external sources such as industry analysts, etc. Whatever the processes in place, they need to be balanced so as not to place

excessive reporting requirements on SOEs or to bypass the board. Ownership entities will also have to develop their own capacity to treat this information. They should seek to provide SOEs with written comments and recommendations when appropriate on current achievements and take actions whenever necessary.

The **annual performance review** (Section 2.3) requires in-depth analysis by the ownership entity of the SOE performance. It might vary significantly in depth and scope but will always include an assessment of financial and non-financial results against key performance indicators, based on information and comments provided by the board. It could also include an assessment of operating results, corporate value and risks, board performance and corporate governance practices. Careful consideration needs to be given to costs and benefits of these information requirements. At the center of the annual performance review is the mostly informal discussion between the board and the ownership entity. Specific mechanisms might be developed within the ownership entity, such as internal panels to allow a broader perspective and fresh views in discussing the evolution of one SOE's performance. A summary document could be developed by the ownership entity, possibly shared with the SOE concerned, and even publicly disclosed. Annual performance reviews are an important tool for identifying actions that need to be taken in relation to underperforming companies and are a natural basis for discussing future objectives. In addition, some more medium- to long-term reviews could be carried out, together with appropriate benchmarking, as the basis for discussing the SOE strategy and assessing the evolution of its value and potential risks.

Ownership entities should also strive to **benchmark SOE performance** (Section 2.4), *i.e.* compare them with relevant peers in the same industry, of similar size and subject to similar complexity and risk, from the private or the public sector, domestic or foreign. The chief purpose is to identify performance gaps and areas of potential improvement, taking into account the impact of market evolution or other "external" factors. The rate of return is often very useful, since it focuses on the cost of capital, which is often underestimated or neglected by SOE management. The use of synthetic financial ratios might also facilitate benchmarking when enterprises are not in the same industry, including different measures of value creation such as EVA (Economic Value Added). Whatever peer is chosen for benchmarking, care is always required in interpreting comparisons of performance and use of relevant industry research is useful.

Auditing performance

Auditing performance provides credibility to the performance indicators and review process, ensuring a solid basis for the overall accountability system. To ensure an overall robust auditing system, it is important to clearly define the respective roles of the three different types of audits, *i.e.* internal, external and state audit, in order to avoid duplication and promote complementarity. The audit committee plays a central role in supporting and overseeing the three types of audit. Appropriate co-ordination and communication has to be ensured among the board, external and internal auditors.

Internal auditors constitute the first level of control (Section 3.2). They can play an important role by scrutinizing and contributing to the improvement of governance practices, reporting routines, risk management and internal control processes. This is becoming critical with the growing deregulation and internationalization of industries in which SOEs often operate. The ownership entities should demand that SOEs have

appropriate procedures for internal auditing, meeting the *International Standards for the Professional Practice of Internal Auditing*, and encourage internal auditors to focus not only on compliance but on risk management. SOEs' financial statements should comprise an internal control report describing the internal control structure and procedures for financial reporting. Internal auditors should have a direct reporting line to the audit committee, which in turns must ensure their independence, support their work and discuss their findings. Finally, periodic audit of internal audit departments could also be required.

The Guidelines also recommend that "*SOEs, especially large ones, should be subject to an annual independent external audit based on international standards*" (Guideline V.C). The annual **external audit** (Section 3.3) shall provide the board and the shareholders with an independent, critical and objective report to ensure that accounts fairly represent the financial position and performance of the company in all material aspects. To improve credibility and comparability, the Guidelines recommended that SOEs be "*subject to the same high-quality (…) auditing standards as listed companies*". Another essential consideration is the effective independence of the external auditors. Criteria for such independence include limits on providing consulting or other non-audit services as well as periodic rotation of audit partners or audit firms. External auditors are accountable to the shareholders via the boards, thus nominated by the AGM (Annual General Meeting) following recommendation of the board audit committee. The audit committee is also responsible for overseeing their work and needs to follow the implementation of the audit findings. Besides that, the ownership entities themselves should "*maintain(s) a continuous dialogue with external auditors*" (Guideline II.F.4) and be able to assess and effectively review regularly the quality of their work. They could provide information both on external auditors and related fees, on their annual reports and websites.

It is often the case that at least large non-listed SOEs are subject to audit by **state audit institutions** (SAIs) (Section 3.4). Their traditional task is to audit the use of public resources, and particularly the legality and regularity of financial management and accounting. SAIs are often powerful tools and information sources for Parliaments. However, the scope of their audits needs to be clearly defined and duplication avoided, with financial audits carried out either by external auditors or by state auditors, depending on the legislation and their respective quality. SAIs could rather focus increasingly on audits of the ownership entities themselves and on performance audits, *i.e.* in-depth reviews of the performance, economy, efficiency and effectiveness of an entity. Ownership entities could put in place specific processes to discuss in a systematic manner the results of state audits with the concerned boards. It is important that they maintain continuous dialogue with SAIs and support their work, ensuring them appropriate access to information, making appropriate use of their audits and taking action based on their findings. Disclosure of audit findings to the public, with due consideration for the protection of commercial, industrial or trade secrets, can also be instrumental in this regard by creating public pressure for action.

Reporting on performance

The Guidelines provide a number of recommendations regarding reporting on performance, covering the publication of aggregate reports, web-based communication and reporting to Parliament.

Aggregate reports (Section 4.2) are short, easy to read and regular reports developed by the ownership entities and providing the general public with value-adding, concise and accessible information about the overall performance of the state sector. They are key communication tools and trust-building instruments directed to the general public, Parliament and the media, and are instrumental in showing that the state is an accountable and predictable owner. The actual process of developing these reports helps clarify policies, make information consistent and improve internal reporting systems. Aggregate reports are also useful for building consensus on specific issues and sensitive policy choices. Their central component is the review of financial performance, including a synthesis presentation of aggregate financial statements with key financial ratios for individual SOEs and the overall state portfolio. Highlights of main events of the year as well as short presentations on the largest SOEs are usually provided, together with essential background information on the framework for exercising state ownership. Aggregate reports could also provide "combined" accounts, giving a clear picture of the whole state sector's financial situation.

Developing aggregate reports entails specific processes within the ownership entity to collect and synthesise information on SOEs. It also involves active consultation and co-ordination among different parts of the ownership entity and with the SOEs and other government departments concerned, which might be time-consuming and not necessarily easy. Clarification of key messages might trigger a lot of internal discussion within the ownership entity. The collection of information both within the ownership entity and from the SOEs themselves is the central stage. The use of specific data sheets, working groups or contact points within SOEs could be helpful, and SOEs need to review the information provided on them. Endorsement of the final draft by the relevant authority gives it more visibility and political weight. Ownership entities could then make active use of aggregate reports, including with the media.

In addition to publishing aggregate reports, **web-based communication** (Section 4.3) is a powerful means of ensuring transparency towards the general public. It provides easy access and timely information about the performance of the state sector, the objectives of state ownership and the way the state exercises its ownership function. Its major advantage is that it can be timely updated. It can be used to provide the latest news and interim reports. It could also be a main channel and support for communicating with the media.

Reporting to Parliament (Section 4.4) is another important element of the overall accountability framework, as Parliaments represent the ultimate owners of SOEs, *i.e.* the general public. It requires a process of compilation, checking, reviewing and questioning that includes a large number of parties. Accountability is achieved through their interaction in what can be viewed as a "disclosure dynamic". There are three types of reporting to Parliament. *Periodic reporting* creates a framework for holding SOEs accountable on a regular basis, but the information is often dated when it reaches the Parliament. *Ad hoc reporting* derives from the capacity of Parliaments to demand information covering a broad range of issues and responding to matters of immediate concern or to important current events. It is sometimes insufficiently structured and subject to political grandstanding. Finally, reporting *for approval* could be discouraged, or at least strictly limited to significant decisions both politically and financially to avoid undue political interference. In practice, the responsibility for reporting to Parliament is usually shared among different ministries and ownership entities. The government's involvement in

transmitting information to the Parliament might be comparatively small, when individual SOE reports are tabled in Parliament after basic due diligence; or very intensive, including evaluation, dialogue with the SOE, analysis and intermediate reviews. In many cases, Parliaments would probably benefit from more concise and relevant information, as well as from better structured debates. It is not easy to find the correct balance between lack of accountability and excessive oversight, which could lead to political interference.

Ownership entities need to clarify the process for reporting to Parliaments. As both line ministries and ownership entities might be involved in reviewing and transmitting documents, active co-operation and co-ordination is necessary to ensure a free flow of information. Specific yet concise documents describing SOE performance, possibly including some form of aggregate data, could be developed to allow a focused discussion by parliamentarians. Appropriate use should also be made of specialised committees to encourage more in-depth and technical discussion and prepare and flag key issues for plenary debates, where a specific and separate discussion on the performance of SOEs could be organised. Ownership entities could also develop long-term performance reporting, allowing for a periodic analysis of the effectiveness of state ownership and a systematic review of SOEs' mandates. Mechanisms have to be developed to limit inappropriate politicisation of debates. Specific procedures need to be developed to deal with confidentiality issues, including confidential or closed meetings, particularly when the SOEs concerned are in competitive sectors. Finally, to facilitate the "disclosure dynamic" referred to above, reports to the Parliament as well as minutes of discussions within the Parliament should be made available to the general public.

The ownership entities are also advised to be pro-active in **communicating with the media**. Having an educated, professional and active press covering SOEs' performance is an instrumental and effective way of ensuring public pressure for performance. The role of the media in exposing, for example, abusive related transactions might be particularly important.

Ensuring adequate disclosure and transparency at the company level

To be transparent as a shareholder, the state must ensure that appropriate information is disclosed at the SOE level. This will allow the state itself to carry out its ownership function, the Parliament to play its oversight role, the media to raise awareness on relevant issues, and the general public to get a clear picture of SOE performance. The Guidelines provide a number of recommendations in this regard, with the underlying objective of ensuring that SOEs are as transparent as publicly traded corporations.

To ensure appropriate disclosure and transparency at the SOE level, the state as an owner needs first to **develop a coherent disclosure policy** (Section 5.2) for its portfolio companies, identifying what information has to be disclosed, how and to whom, and the procedures for ensuring its quality. Developing such a policy would start with an inventory and review of the existing legal and regulatory requirements as well as actual practice at the SOE level. After identifying weaknesses and discrepancies, the framework might be adapted and completed. In doing so, the ownership entity would consult adequately, focus on material information to avoid unnecessary requirements, and make proper use of regulatory impact assessments.

Specific mechanisms could be put in place to **encourage and monitor effective implementation of transparency requirements by SOEs** (Section 5.3). It is necessary for

the ownership entity to develop guidance in sensitive areas, in the form of focused manuals or specific seminars and training. It could also underline boards' responsibilities and the particular role of the audit committee in ensuring appropriate disclosure. Ownership entities need to communicate effectively on the new framework, to ensure that SOEs fully understand their obligations and to raise awareness of the general public and the media. Special initiatives could encourage and support better disclosure, such as holding meetings open to the general public and mimicking AGMs, special transparency awards, etc. SOEs should be encouraged to go beyond requirements and adopt best practices, for example regarding sustainability reporting. The ownership entities have anyhow to measure and assess effective implementation by SOEs and report on it.

The Guidelines highlight the importance for the state as an owner to ensure **equitable treatment of all shareholders** by SOEs (Section 5.4). Building up a reputation of a transparent, predictable and fair owner will have a significant impact on the state's future capacity to attract outside funding as well as on the valuation of SOEs. The state as a shareholder should "tie its own hands" and ensure a clear protection of minority shareholders. An essential prerequisite is to strongly establish and clearly articulate the duty of loyalty of SOE board members towards the SOE itself and to all its shareholders. This policy could then provide a consistent menu of mechanisms, usually adopted to prevent abuse of minority shareholders, with a reasonable balance of *ex ante* and *ex post* mechanisms and taking due consideration of the legal characteristics of the country concerned. This would include pre-emptive rights, qualified majority for certain decisions, capacity for minority shareholders to call for a shareholder meeting, access to redress, etc. The state could also develop nomination processes that are favourable to minority shareholders' representation in boards, such as cumulative voting or participation in nomination committees. Active participation of minority shareholders in general shareholder meetings might also be encouraged by facilitating voting *in absentia* or collection of proxy voting from employee-shareholders. A simple and effective option is to submit all SOEs to the general company law, listing requirements and corporate governance codes applying to private-sector companies. Specific mechanisms and procedures also need to be developed to ensure that ownership entities do not abuse the information they receive as a controlling or significant shareholder.

This policy needs to be actively communicated to all SOEs, the market and stakeholders. The ownership entity should ensure that it is effectively implemented and encourage SOEs **to communicate actively with all shareholders** and adopt good practice in terms of board nomination, participation in general shareholder meetings and disclosure of information to all shareholders.

Abusive related party transactions (Section 5.5) are frequently reported as one of the most serious breaches of good corporate governance around the world. In many jurisdictions, disclosure and approval of related transactions are legal requirements. But implementation and enforcement remains a challenge as detecting a related transaction is difficult and proving abuse even more so. In the case of SOEs, the usual definition of related parties might be considered as too extensive, particularly the case in countries where state ownership is pervasive, as it includes "*entities that control or are under common control with the company, significant shareholders (…) and key management personnel*". This is the reason why the International Accounting Standard (IAS 24) is being modified in the case of state control. Exemptions would be provided for entities controlled or significantly influenced by the state, but the actual exercise of influence would preclude the use of this exemption.

As a significant shareholder and often board member, the state should ensure that SOEs do not undertake abusive related party transactions. To do so, it has firstly to define clearly what should be considered by SOEs as a related party transaction, based on IAS 24. It will then develop a clear policy in this regard, mandating adequate decision processes for approval of these transactions, tough standards regarding their disclosure, as well as outright prohibition of certain types of related transactions. It needs also to provide adequate guidance to SOEs to ensure that they duly identify, decide on and disclose related transactions. This guidance would cover the identification of relevant related parties and related transactions and underline the role of the audit committee in their review and disclosure. Finally, the ownership entity could also encourage gatekeepers and the media to be vigilant in identifying and disclosing abusive transactions.

The Guidelines recommend SOEs to acknowledge the importance of stakeholder relations for building sustainable and financially sound enterprises and fully recognise their rights as established by law or mutual agreement. However, any specific rights granted to stakeholders or influence on the decision-making process should be explicit. Adequate **reporting on stakeholders' relations** (Section 5.6) allows SOEs, particularly listed and large ones, as well as those pursuing important policy objectives, to demonstrate their commitment to co-operation with stakeholders, build up trust and improve their reputation. It is also an important tool for managing risks related to stakeholder expectations.

The state shareholder should thus clearly require and encourage SOEs to follow existing best practices and recently developed guidelines on sustainability reporting, with due consideration for the costs involved. This reporting needs to be independently scrutinised to reinforce its credibility. It might also include information on compliance with internal codes of ethics and mechanisms protecting stakeholders reporting on illegal or unethical conduct by corporate officers, such as confidential access to the board or an ombudsman. SOE boards should also be encouraged to fulfil their responsibility regarding sustainability reporting, and have at least an annual discussion on it.

ANNEX A

Relevant Guidelines and Corresponding Topics Covered in the Guide

	1. Setting objectives	
II.A.	The government should develop and issue an ownership policy that defines the overall objectives of state ownership, the state's role in the corporate governance of SOEs, and how it will implement its ownership policy.	1.2. Developing an ownership policy. 1.3. Setting specific targets for the ownership entity. 1.4. Defining and reviewing SOE mandates. 1.6. Defining SOE objectives and yearly targets. 1.7. Developing relevant performance indicators.
VI.A.	SOE boards should carry out their functions of monitoring of management and strategic guidance, subject to the objectives set by the government and the ownership entity.	
V.E.1.	SOEs should disclose material information on all matters described in the OECD Principles of Corporate Governance and in addition focus on areas of significant concern for the state *as an owner and the general public. Examples of such information include;* A clear statement to the public of the company objectives and their fulfilment.	
I. C.	Any obligations and responsibilities that an SOE is required to undertake in terms of public services beyond the generally accepted norm should be clearly mandated by laws or regulations. Such obligations and responsibilities should also be disclosed to the general public and related costs should be covered in a transparent manner.	1.5. Identifying, costing and funding special obligations.
	2. Reviewing performance	
II.F	The state as an active owner should exercise its ownership rights according to the legal structure of each company. Its prime responsibilities include setting up reporting systems allowing regular monitoring and assessment of SOE performance.	2.2. Ongoing monitoring of performance. 2.3. Annual review of performance. 2.4. Benchmarking performance.
	3. Auditing performance	
V.B.	SOEs should develop efficient internal audit procedures and establish an internal audit function that is monitored by and reports directly to the board and to the audit committee or the equivalent company organ.	3.2. Internal audit.
V.C.	SOEs, especially large ones, should be subject to an annual independent external audit based on international standards. The existence of specific state control procedures does not substitute for an independent external audit.	3.3. External and independent audit.
II.E.	The co-ordinating or ownership entity should be held accountable to representative bodies such as the Parliament and have clearly defined relationships with relevant public bodies, including the state supreme audit institutions.	3.4. State audit.
II.F	The state as an active owner should exercise its ownership rights according to the legal structure of each company. Its prime responsibilities include: When permitted by the legal system and the state's level of ownership, maintaining continuous dialogue with external auditors and specific state control organs.	

	4. Reporting on performance	
V.A.	The co-ordinating or ownership entity should develop consistent and aggregate reporting on state-owned enterprises and publish annually an aggregate report on SOEs.	4.2. Publication by ownership entities of aggregate reports. 4.3. Development and timely update of websites by ownership entities.
II.E.	The co-ordinating or ownership entity should be held accountable to representative bodies such as the Parliament and have clearly defined relationships with relevant public bodies, including the state supreme audit institutions.	4.4. Reporting to parliaments
	5. Ensuring adequate disclosure by SOEs	
V.D.	SOEs should be subject to the same high-quality accounting and auditing standards as listed companies. Large or listed SOEs should disclose financial and non-financial information according to high-quality internationally recognised standards.	5.2. Developing an SOE disclosure and transparency policy. 5.3. Follow up implementation and encourage good practice.
V.E.	SOEs should disclose material information on all matters described in the OECD Principles of Corporate Governance and in addition focus on areas of significant concern for the state as an owner and the general public.	
VI.E.2.	The ownership and voting structure of the company.	
VI.E.3.	Any material risk factors and measures taken to manage such risks.	
IV. B.	Listed or large SOEs, as well as SOEs pursuing important public policy objectives, should report on stakeholder relations.	
VI.E.4.	Any financial assistance, including guarantees, received from the state and commitments made on behalf of the SOE.	
VI.E.5.	Any material transactions with related entities	5.5. Develop appropriate framework to deal with related-party transactions.
III.B.	SOEs should observe a high degree of transparency towards all shareholders.	5.4. Ensure equitable treatment of shareholders by SOEs.
III.C.	SOEs should develop an active policy of communication and consultation with all shareholders.	
IV.B.	Listed or large SOEs, as well as SOEs pursuing important public policy objectives, should report on stakeholder relations.	5.6. Ensure appropriate disclosure on stakeholder relations.

ANNEX B

Participants of the First Meeting of the Global Network on Privatisation and Corporate Governance of SOEs, Paris, March 2008

Country	Participant	Designation
Austria	Mr. Johannes RANFTL	Director Public Investments and Real Estate, Ministry of Finance
Belgium	Mr. Piet RAEPSAET	Directeur de l'Administration de la Trésorerie, SPF Finances
	Mrs. Hilde VAN DEN HOUTEN	Premier attaché, Service Support de la Dette, Service Public Fédéral Finances
Brazil	Mr. Francklin FURTADO	Gestor Governamental – EPPGG, Department of Co-ordination and Control of State-Owned Enterprises, Ministry of Planning Budget and Management
	Ms Luciana PONTES	Co-ordinator, Department of Co-ordination and Control of State-Owned Enterprises, Ministry of Planning Budget and Management
Bulgaria	Mr. Todor NIKOLOV	Executive Director, Privatisation Agency
Canada	Mr. Sebastian BEAULIEU	First Secretary, Permanent Delegation to the OECD
Chile	Ms Leticia Celador IZQUIERDO	Advisor to the Minister, Ministry of Finance
Peoples Republic of China	Ms Jun HAN	Program Co-ordinator, Foreign Affairs Bureau, SASAC
	Mr. Tingyu HUANG	Secretary, Supervisory Committee, China Netcom (Group) Company Ltd.
	Mr. Yongfa QIN	Deputy Head, Board Pilot Project Office, SASAC
	Mr. Guijun WU	Secretary to the Board, Office of Directors, General Dept., China Netcom (Group) Company Ltd..
Croatia	Mr. Ivo RADKOVIC	Advisor, Investment and Export Facilitating Division, Ministry of Economy, Labour and Entrepreneurship
Czech Republic	Mr. Petr MUSIL	Advisor, Ministry of Finance
Egypt	Dr. Ashraf GAMAL EL DIN	Executive Director, Egyptian Institute of Directors
Estonia	Mr. Tarmo PORGAND	Head of Division, Ministry of Finance
Finland	Mr. Arto HONKANIEMI	Senior Financial Counselor, Ownership Steering Department, Government Office
	Mr. Ilkka PUROQ	Senior Financial Counselor, Ownership Steering Department, Prime Minister's Office
France	Ms Lucie MUNIESA	Secretary General, APE (State Participation Agency)
Germany	Dr. Wilhelm WILTING	Referat VIII B 1, Federal Ministry of Finance (BMF)
Greece	Mr. Aimilios STASINAKIS	Special Secretary for Public Enterprises and Entities, Ministry of Economy and Finance
	Ms Dimitra PANAGOPOULOU	Economic Advisor of Special Secretariat for Public Enterprises and Entities, Ministry of Economy and Finance
	Mr. Dimitri ANDREOU	First Secretary, Permanent Delegation to the OECD
India	Mr. Sumant BATRA	Senior Partner, Kesar Dass B and Associates
	Dr. Sikander DEWAN	Director General, Standing Conference of Public Enterprises (SCOPE)
	Mr. K PADMAKUMAR	Secretary, Government of Kerala, Public Sector Restructuring and Internal Audit Board Industries Dept.
	Mr. K D TRIPATHI	Joint Secretary, Department of Public Enterprises, Ministry of Heavy Industries and Public Enterprises
Indonesia	Mr. Mas Achmad DANIRI	Chairman, Indonesia National Committee on Governance
	Mr. Pandu DJAJANTO	Expert Staff in Corporate Governance, State Ministry of State-Owned Enterprises
Israel	Mrs. Avitak BIRGER	Deputy Legal Counsel, Israel Government Companies Authority
Italy	Mr. Giovanni FINO	Director, Direction VII – Office 5, Ministry of Treasury
Japan	Mr. Takashi KAMIYA	First Secretary Finance, Permanent Delegation to the OECD

Country	Participant	Designation
Korea	Mr. Kyung-Ho CHOO	Counsellor for Economics and Finance, Permanent Delegation to the OECD
	Dr. Jiyoung KIM	Visiting Fellow, Korea Institute of Public Finance
	Mr. Heechul MIN	Research Fellow, Korea Institute of Public Finance
Malaysia	Mr. Abdul Wahab JAAFAR SIDEK	CEO, Minority Shareholder Watchdog Group
Morocco	Mr. Abdesselam ABOUDRAR	Président de la Commission Lutte contre la Corruption, CGEM
Mozambique	Mr. Abilio Justino INGUANE	Director-Advisory Staff, State Shares Management Agency, IGEPE
	Mr. Daniel TEMBE	Chairman, IGEPE
	Dr. Maria Iolanda WANE	Executive Director, IGEPE
Norway	Mr. Morten KALLEVIG	Deputy Director General, Ministry of Trade and Industry, Department of Ownership
Pakistan	Mr. Rana Assad AMIN	Joint Secretary Corporate Finance, Ministry of Finance
Peru	Mr. Mario GONZALEZ	Manager Operations, FONAFE
Philippines	Mr. Jonathan Juan MORENO	Vice President, Head of Corporate Governance Division, The Philippine Stock Exchange
	Mr. Jeremius PAUL	Undersecretary, Ministry of Finance
Poland	Mr. Andrzej ZADRUZYNSKI	Counsellor, Permanent Delegation to the OECD
Portugal	Mr. Carlos Lopes PEREIRA	Head of Cabinet, Entrepreneurship, Partnerships and Concessions, Treasury.
Romania	Mr. Valentin MACEC	Director, SME's Ministry
	Ms Mihaela POPESCU	Counsellor OECD Office, Embassy of Romania in Paris
Russian Federation	Ms Elena KURITSINA	Deputy Head, Federal Service for Financial Market (FSFM)
	Mme Tatiana MEDVEDEVA	Senior Legal Expert, Federal Service for Financial Market (FSFM)
	Mr. Ivan OSKOLKOV	Director, Department of Corporate Governance, Ministry of Economy
Singapore	Mr. John LIM	President, Singapore Institute of Directors (SID)
Slovenia	Ms Anka CADEZ	Secretary, Ministry of Finance
	Mr. Leonardo PEKLAR	Chairman, Socius Consulting Inc.
	Ms Nevenka REBRICA	Head of Public Sector Analysis and Evidence, Ministry of Finance
South Africa	Mr. Mohamed ADAM	Corporate Secretary and Legal Counsel, Eskom Holdings Ltd..
	Mr. Bernard MHANGO	Corporate Secretary, Development Bank of Southern Africa
	Mr. Higgo du TOIT	Director Corporate Governance, Assets and Liabilities Management, Public Finance, National Treasury
Spain	Mr. Juan Munuira GONZÁLEZ	Legal Advisor, International Affairs, Commission Nationale du Marché des valeurs (CNMV)
	Mr. Dioniso Usano CRESPO	General Director, FUNEP/SEPI, Ministry of Economy and Finance
	Mrs. Paloma AVILA DE GRADO	Economic and commercial counselor, Permanent Delegation
Sweden	Mr. Lars Erik FREDRIKSSON	Desk Officer, Ministry of Energy and Communications
Switzerland	Mr. Robert MÜLLER	First Secretary, Permanent Delegation to the OECD
Thailand	Dr. Areepong BHOOCHA-OOM	Director General, State Enterprise Policy Office (SEPO)
	Dr. Sathit LIMPONGPAN	Deputy Permanent Secretary, Ministry of Finance
Turkey	Mr. Volkan TASKIN	Chief Economic Counsellor, Permanent Delegation to the OECD
	Mr. Ali Gokhan ASLAN	Expert, Corporate Finance Department, Capital Markets Board of Turkey
	Ms Arzu ATIK	Head of Group, Privatisation Administration
	Mr. Mustafa KORHAN	Member Board, Corporate Finance Department, Capital Markets Board of Turkey
	Mr. Salih KOSE	Head of Department, State Planning Organisation
	Mr. Mehmet Akif KÖSEOGLU	Expert, State Planning Organisation
	Mr. Sefa PAMUKSUZ	Director General, for SEEs, Turkish Treasury
	Ms Filiz Ipek YIKILMAZ	Head of Department, Privatisation Administration
United States	Ms Rebecca FONG	Investment Policy Advisor, Permanent Delegation to the OECD
Vietnam	Ms Thuy TRAN THI PHUONG	Deputy Director, Operating Office, Secretariat Department, State Capital Investment Company (SCIC)
Zambia	Mr. Derrick SIMUKOKO	Senior Economist, Investment and Debt Management Unit, Ministry of Finance and National Planning
	Mrs. Rachel ZYAMBO	Chief Economist, Industry, Investment and Debt Management Unit, Ministry of Finance and National Planning
	Mr. Eugene CHANDI	Director (Non-Executive), Institute of Directors
	Mr. Mumba KAPUMPA	President, Institute of Directors
World Bank	Mr. Philip ARMSTRONG	Head, Global Corporate Governance Forum, IFC/World Bank Corporate Governance Department
	Mr. Sebastian LOPEZ AZUMENDI	Sustainable Development Network, Latin America and the Carribean Region
	Mr. David ROBINETT	Economist, Corporate Governance Unit