

Re: Comments on Draft Revisions to the OECD Guidelines on Corporate Governance of State-Owned Enterprises

Dear Sir/Madam,

We are grateful for the opportunity to provide comments on the Draft Revisions to the OECD Guidelines on Corporate Governance of State-Owned Enterprises.

The European Bank for Reconstruction and Development (“**EBRD**”) is deeply committed to strengthening the corporate governance frameworks of its recipient countries as well as sustainability and governance practices of its clients. Over the years, the EBRD has built considerable experience in improving the governance of state-owned enterprises (“**SOEs**”) and helping governments develop their ownership functions, including high-quality state-ownership policies that are the very basis of any sound corporate governance regime for SOEs and a pre-requisite for instilling the public’s trust in SOEs.

For these reasons, we welcome the efforts to review the OECD Guidelines on Corporate Governance of State-Owned Enterprises, align them with the revised G20/OECD Principles of Corporate Governance, and update them according to the latest developments.

Our comments are annexed to the letter.

Kind regards,

1. Applicability and definitions

Having regard to some additional guidance provided in section V.C with respect to the functions of internal audit, we recommend providing a definition of the internal audit in the “Applicability and definitions” section, given the lack of understanding of what an internal audit function is. Depending on the jurisdiction, it is not uncommon for internal audit in some large SOEs to serve as a narrower “cross checking” function of the accounting department, while in some others SOEs are permitted to outsource internal audit entirely or to do so on an ad-hoc basis for certain audit subjects.

We believe that the definition of Sustainability (“*Sustainability, for the purpose of these Guidelines, refers to the attainment of sustainable development as generally embodied in the United Nations Sustainable Development Goals (SDGs).*”) might be too narrow and does not recognise other important international and domestic regulatory initiatives in this area. Further, this definition may cause confusion with respect to how G20/OECD Principles are to be applied in SOEs as in the Principles, the term “sustainability” is not specifically defined and seems to have a broader meaning. We would therefore advise to expand the definition.

2. II. The state’s role as an owner

In section II.B. we suggest clarifying the final sentence which now suggests that government should avoid redefining SOE objectives only in case of fundamental change (as opposed to redefining objectives in case of fundamental change). We suggesting rephrasing (with the introduction of the underlined wording) as follows: “*The government as a shareholder should avoid redefining SOE objectives in a non-transparent manner and should redefine these objectives only in cases where there has been a fundamental change of mission.*”

3. II. The state’s role as an owner

Coordinating agencies are often tasked merely with co-ordinating the actions and policies undertaken by ownership departments in different ministries under this model rather than carrying out ownership functions directly. In order to reflect this nuance, we suggest phrasing the sentence regarding the exercise of ownership functions with the help of coordinating agencies (underlined) (as opposed to *by* coordinating agencies) in section II.D as follows: “*...relevant ownership functions should be carried out with the assistance of a co-ordinating body*”.

4. II. The state’s role as an owner

Merit-based nomination typically implies assessment of individual’s recognition and perception on a general level. We suggest adding a reference to competences of the candidates (on top of merit of the candidates) in a board nomination process (underlined) in section II.F, since merit-based nomination alone may be insufficient to ensure the board has the skillset and knowledge suitable for a particular job.

“2. *Establishing and safeguarding well-structured, merit and competence-based and transparent board nomination processes, actively participating in the nomination of all SOEs’ boards and contributing to gender and other forms of board diversity*”.

5. III. State-owned enterprises in the marketplace

Regarding section III.A – addition is proposed as underlined to the sentence: “*There should be a clear separation between the state’s ownership function and other state functions that may influence the conditions for state-owned enterprises, particularly with regard to market regulation and policy making. Additionally, to strengthen this separation as well as enhance transparency and create a level playing field between market actors, the establishment of an independent sector regulator should be considered where applicable*”.

Justification: the need for an independent regulator seems implied by the original sentence, yet it remains a frequently overlooked aspect in the context of SOE reform. Having the sentence highlight the need for establishing an independent sector regulator where applicable would address that issue.

6. III. State-owned enterprises in the marketplace

Regarding section III.E.3 – the current sentence is “*SOEs’ economic activities should not receive or provide in-kind inputs (such as goods, energy, water, real estate, data access, land or labour) nor at prices or conditions more favourable than those available to privately owned competitors.*” It seems important to specify this list by considering the addition of terms to this list that would address common infrastructure sector challenges. The proposed additions to the sentences are underlined below:

- (a) add the notion of “right of way”. **Justification:** right-of-way is synonymous of, but still importantly distinct from, receiving land in kind.
- (b) add the notion of “all types of concessions”. **Justification:** although perhaps implied by the current phrasing, it could be useful to mention concessions explicitly in the sentence as they differ from sheer input provision. Concessions are a domain where preferential treatment of SOEs can often arise due to their ownership ties to the public sector. By mentioning concessions explicitly, the guidance would ensure that SOEs and private sector companies can negotiate, and get access to, concessions on equal terms.
- (c) add a parameter “or less” for SOEs. **Justification:** we do see SOEs sometime providing in-kind inputs at conditions less favourable than those for the private sector. Therefore, the guidance should update its wording to reflect the need for a fair and equal treatment of SOEs and private sector entities.

To summarize, the revised sentence we suggest would be: “*SOEs’ economic activities should not receive or provide in-kind inputs (such as goods, energy, water, real estate, data access, land or labour) or arrangements (such as rights-of-way, or concessions), nor at prices or conditions more (or less) favourable than those available to privately owned competitors.*”

7. III. State-owned enterprises in the marketplace

Regarding III.F. - the current sentence is “*When SOEs engage in public procurement, whether as bidder or procurer, the procedures involved should be open, competitive, non-discriminatory, promote supplier diversity and safeguarded by appropriate standards of*

integrity and transparency, ensuring that SOEs and its potential suppliers are not subject to undue advantages or disadvantages". One may consider the proposed underlined additions:

- (a) adding "based on fair and objective selection criteria". **Justification:** this could be implied by other elements in the original sentence but isn't straightforwardly expressed.
- (b) adding "promote optimal risk management". **Justification:** effective risk allocation among entities involved in a project is an important objective, and particularly so for SOEs as they face a distinctive set of risks such as political interference risk. Therefore, the guidance could usefully highlight the need for optimal risk management within projects involving SOEs.

To summarize, the revised sentence we suggest would be: "*When SOEs engage in public procurement, whether as bidder or procurer, the procedures involved should be open, competitive, non-discriminatory, based on fair and objective selection criteria, promote supplier diversity, promote optimal risk management, and safeguarded by appropriate standards of integrity and transparency, ensuring that SOEs and its potential suppliers are not subject to undue advantages or disadvantages*"

8. VI. The responsibility of the boards of SOEs

In spite of national peculiarities, it is very important for some committees (for example and primarily - an audit committee, nomination and remuneration committee and risk committee) to be (i) formed at the board level and (ii) consist of board members, which we suggest stressing in section VI.H by adding a respective reference (underlined).

It is essential that members of board committees (in particular the audit committee) who recommend specific actions to the board follow up on such recommendations and vote for them in their capacity as board members, therefore reinforcing their positions. Further, board members have a full vision of the business of the company, while outside committee members might only have a partial understanding. For the same reason and ideally, we recommend key board committees to be formed of non-executive board members.

"SOE boards should consider setting up specialised board committees, composed of independent and qualified non-executive board members, to support the full board in performing its functions".

9. Annotations to Chapter I: Rationales for state ownership

In the annotation to Chapter I.B: Rationales for state ownership, we suggest spelling out that "*Individual SOE strategies should be linked to a state ownership policy, which would give a clearer and more operational path for their future*", by adding this additional sentence in the text.

10. Annotations to Chapter III: State-owned enterprises in the marketplace

Since SOEs often have a considerable market share, they are uniquely placed to play demonstrative and leading roles in promoting sustainability initiatives and safeguard environmental and social standards in the whole supply chain, by adding certain requirements to their procurement procedures. We suggest using the annotations to Chapter III.4.F: State-

owned enterprises in the marketplace to address the issue of sustainability in the supply chain. This could be added to the new reference on promoting supplier diversity.

11. Annotations to Chapter VI: The composition and responsibilities of the boards of state-owned enterprises

We suggest echoing positive independence requirements for board members mentioned in section V in the annotations to Chapter VI.D: The composition and responsibilities of the boards of state-owned enterprises as follows: “*Independent board members should be in possession of an independent mindset and sufficient competencies to carry out the board duties.*”.