

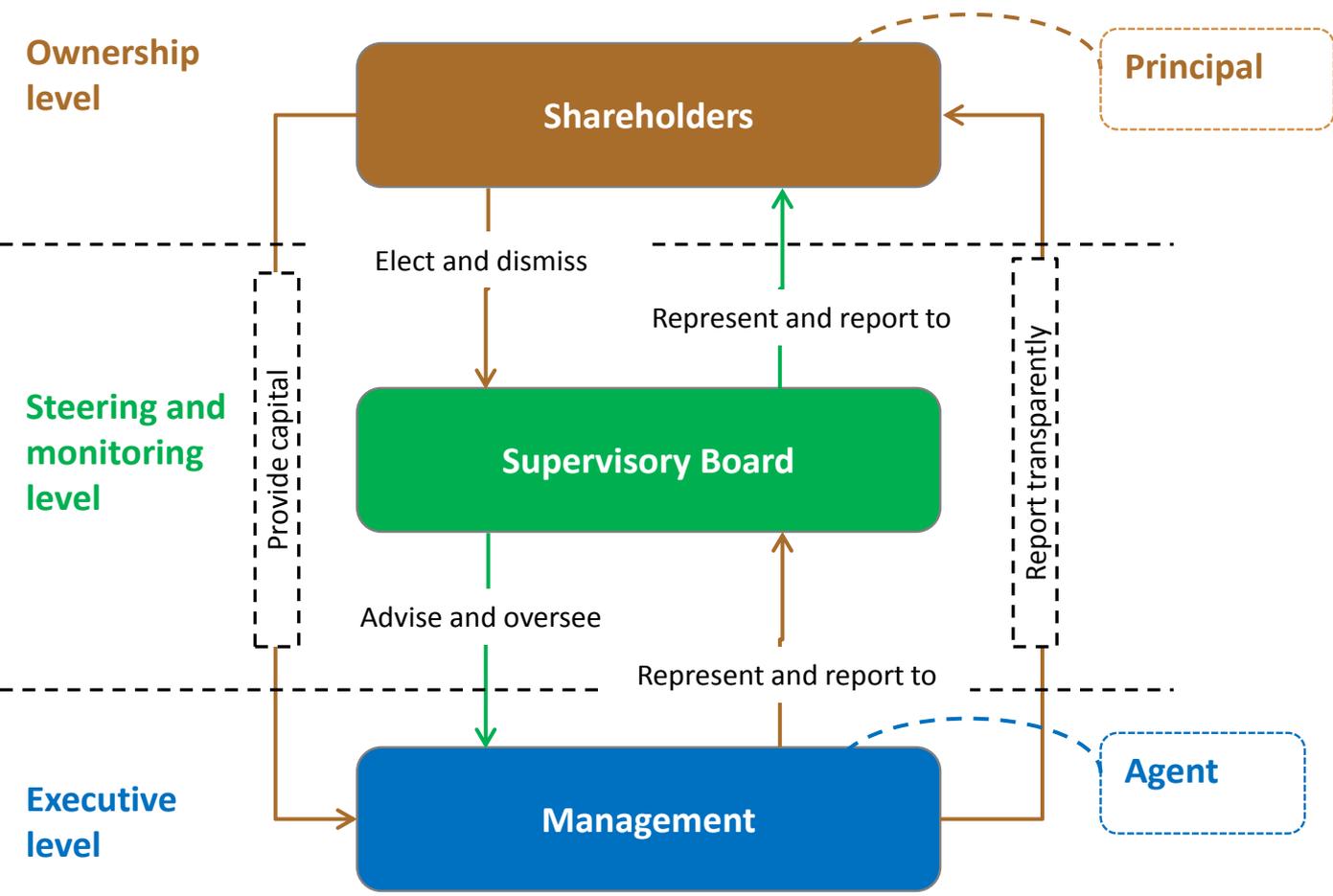
# OECD Guidelines on Corporate Governance for SOEs: Implementation in Ukraine

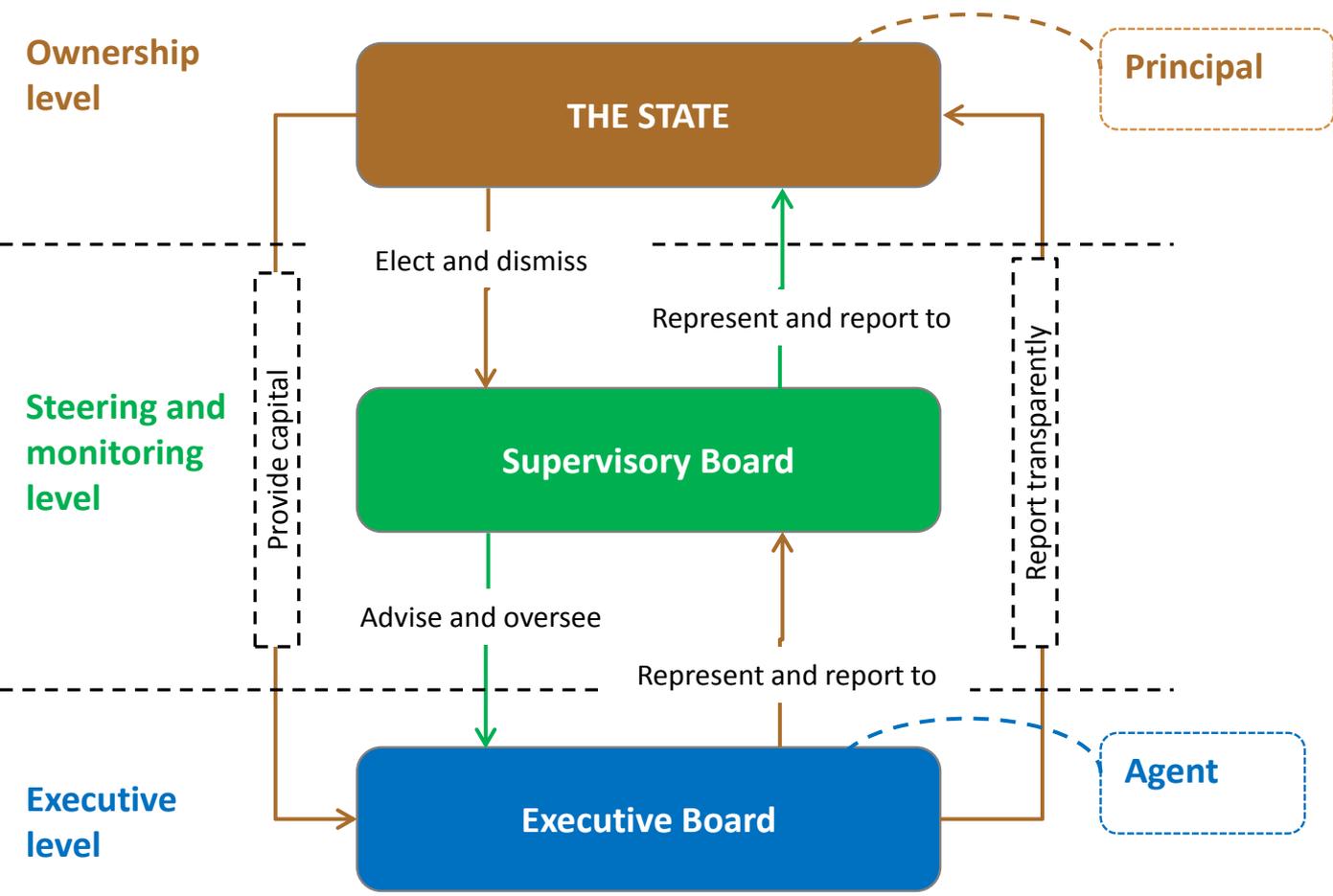


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KYIV, 29 SEPTEMBER 2016**





**Ownership level**

**The people of Ukraine**

Appoint and dismiss  
(through Parliament)

Represent and answer to

**CMU ("founder") and Ministry of Energy ("shareholder")**

Elect and dismiss

Represent and report to

**Supervisory Board**

Advise and oversee

Represent and report to

**Executive Board**

**Steering and monitoring level**

Provide capital

Report transparently

**Executive level**

**Nearly no incentives to protect own shareholder interest:**

- Cannot vote with their **hands** (no actual shares (measurable value) in Naftogaz)
- Cannot vote with their **feet** (no mechanism to participate in decision-making, e.g., no GSM)
- Little interpretable information

**Decision-making politicised:**

- Separation of powers/responsibilities unclear
- Roles of founder and shareholder conflicting
- Commercial interest in Naftogaz conflicts with the State's social policy and regulatory functions
- Intervention in day-to-day management possible

**De facto, no board:**

- 2014: no actual board
- All board decisions made by the Ministry (= GSM)
- Previously, all board members were selected among government officials
- All board members must act (vote) within the CMU's directives (= no independent decision-making)
- None of board members remunerated for their work

**Poor incentives for top management:**

- Very low compensation, compared to market
- High responsibility (incl. criminal responsibility)
- Currently, no liability insurance in Ukraine
- Little autonomy

# Framework of reference: OECD standards



- **OECD standards:**
  - OECD Principles of Corporate Governance
  - OECD Guidelines on Corporate Governance for SOEs
- Understandable to outsiders (EU, int'l community)
  - Need not reinvent the wheel
  - Are very concrete, when applied (substance over form)
- **External reference**
  - Formal requirement (Coalition Agreement)
- **Clear guidelines minimising discretion**
  - Minimises the possibility for vested interests to “imitate” a reform and bend the rules in the favour

# OECD Guidelines on CG for SOEs



- Rationale for state ownership
- The state's role as an owner
- SOEs in the marketplace
- The responsibilities of the boards of SOEs

# Rationales for state ownership



- The state exercises the ownership of SOEs in the interest of the general public
- What value to maximise (for society)?
  - Ownership function (shareholder value)
  - Social policy
  - Regulatory
- Public policy objectives mandated and disclosed
- Rationale for an individual SOE
  - Clarity for the board/people
  - E.g., energy independence or maximum returns?
- No justification → privatise

# The state's role as an owner



- Informed and active owner
  - Refrain from intervening in SOEs management
  - Avoid redefining SOE objectives in a non-transparent manner
  - Let SOE boards exercise their responsibilities and respect their independence
- Centralised ownership entity (if not possible, a co-ordinating body)
- Complex legal forms
- Corporate norms different than those commonly accepted
- Little operational autonomy
  - Appointment
  - Financial plans
  - Dividends
- Recent Naftogaz situation
  - Can happen in any other SOE or state-owned bank
- Ministries → National Wealth Fund
  - Political insulation
  - Professional management

# SOEs in the marketplace



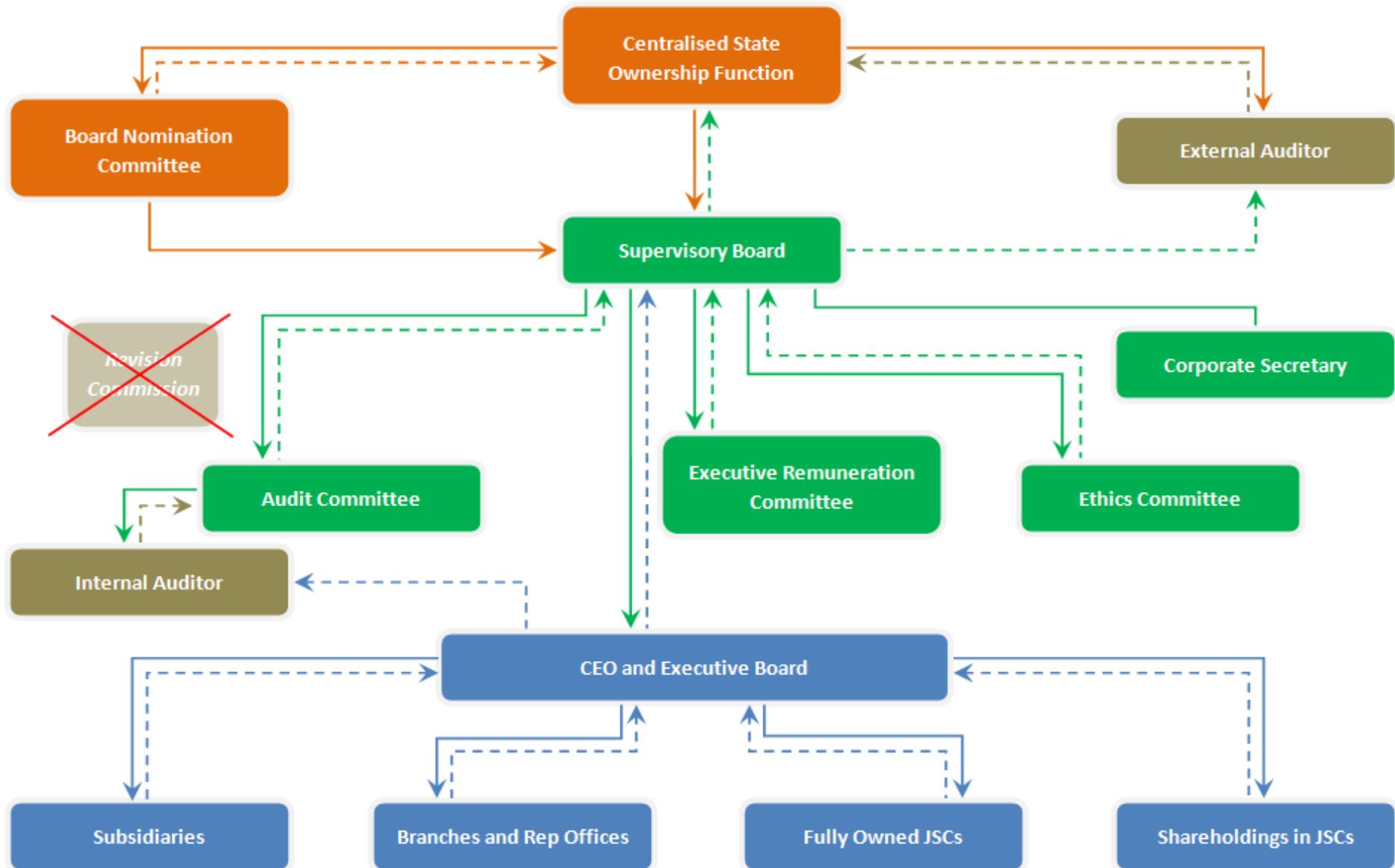
- Level playing field
- Fair competition
- Laws and regulations discriminate between SOEs and their market competitors:
  - Entities of private law vs. entities of public law
  - “State sector of the economy”
    - Appointments
    - Financial plans
    - Dividends
- Little separation between the state’s ownership function and other state functions that may influence the conditions for state-owned enterprises
  - implicit policy objectives
  - subsidies

# Responsibilities of the boards of SOEs



OECD	Ukraine
Accountability	No boards
Strategy	Not approved by the board Financial plan approved by Ministry
Supervising management	CEOs appointed by Ministries Remunerations set by the state
Composition	Government officials Diversity? State representatives?
Equivalent legal responsibilities	Voting instructions <i>State representatives</i>
Committees	???
Evaluation	???
Audit	???

# Corporate governance target structure



# Context: Ukrainian law, two-tier board



- Clear distinction between the one-tier and two-tier systems in OECD standards
  - Focus on Supervisory Board (not Board of Directors)
  - Independent board members (no “non-executive” directors)
- Challenges to implementing corporate governance principles under Ukrainian law
  - Legal transplantation impossible
  - Concept + local lawyers
- Active legal reforms mode, although competitive among various ministries and donors and not always well-coordinated
- State’s fear of losing ministerial control over SOEs to private control

# Challenges



- **Ownership policy**
  - Clarity for the ultimate shareholders (the people of Ukraine)
  - Clarity for the Supervisory Board
- **Board composition**
  - Must reflect the ownership policy (competent and diverse)
- **Strategy**
  - Clarity on strategic objectives
- **Evaluation → clarity for ultimate owners/board on:**
  - performance indicators and incentives
  - responsibilities (e.g., Naftogaz subsidiaries)

→ Who is accountable?

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