Consultation with the
OECD Corporate Governance Committee

Paris, 27 November 2012

BIAC Comments

Corporate Governance, Value Creation and Economic Growth

BIAC welcomes the initiative to connect corporate governance, value creation and growth. As recognized by the OECD Corporate Governance Principles, the corporate governance framework should be developed with a view to its impact on overall economic performance. BIAC strongly supports the recommendation to bear in mind, when discussing policy changes or corporate governance rules, the overall objective of creating growth, value and jobs, recognizing that corporate governance affects every step of the investment process. Corporate governance practices are not a goal in themselves, but should enable business to take risk to grow and create value, which requires access to and effective allocation of capital.

In view of the withdrawal of more and more companies from the public markets over recent years, the question remains how companies can be assured of continued access to sufficient capital to grow and drive growth in both innovation and employment. The findings of the OECD project can make an important contribution by informing both policy makers and business of the key changes in equity markets. It can also contribute to shedding further light on the ability of equity markets to serve the long-term needs of the real economy and the role of effective corporate governance to help channel savings to corporations that need capital for innovation, job creation and growth. The project will be particularly important in providing fact-based analysis on global trends and the changes we have been experiencing which will be indispensable to inform discussions on the forthcoming update of the OECD Corporate Governance Principles.

Whatever the future of public equity markets however, BIAC reminds the Committee that public equity is not the only source of risk capital. The explosive growth in recent years of debt markets, including tradable corporate bond index funds, for example, begins to approach the separation in investment horizon between savers and corporations that equity offers. It is also uncertain that,
despite clear evidence provided in the report of declines in equity markets, we have seen a decline in innovation over the same period. Whether the properties of equity markets are uniquely suited for growth and innovation is one of the more intriguing and unsettled questions raised by the report.

BIAC supports the proposed next steps for future empirical and analytical work within the value creation project as described in paragraph 15 of the background document. In particular, we support further investigation in the following areas, and again offer support from the business community to help the Committee in its work:

- Given shifts in equity markets in favor of controlling ownership structures (Pg. 15), BIAC supports greater research into governance improvements at controlled companies. Such research may consider if control impacts corporate governance in different ways in developed and emerging markets (see also recent research into the effects of control in the US).

- BIAC supports the proposed empirical overview of ownership structures, with a view to understand how this impacts decisions to stay public. The Committee should be aware of private efforts to create similar taxonomies of ownership that may complement its work.

- BIAC supports efforts to identify public or private incentives for owners to monitor investments. To some extent, recent trends in portfolio diversification may be too late to reverse, but there are lessons no doubt to be learned from jurisdictions that have introduced stewardship codes, changes in tax policy, or other mechanisms to enhance monitoring. It is in this context that BIAC encourages completion of the report and its Part III, which should provide additional thinking about shareholder monitoring and the incentives in place and governance at shareholders themselves. BIAC also encourages the OECD to address the substantial existing barriers to cross-border voting.

- BIAC also encourages the committee to examine how good governance could be encouraged during the listing process where debt funders can have a positive impact on corporate governance.

- We appreciate the inclusion of emerging markets in the proposed analysis, in particular as the world’s fastest growing economies are concerned, so that the final report is of relevance to both OECD and non-OECD countries. The project could also make a contribution to the OECD horizontal project on New Approaches to Economic Challenges.

**Initial Comments on the Update of the OECD Corporate Governance Principles**

The OECD Corporate Governance Principles are one of the 12 key standards for international financial stability of the Financial Stability Board. They are widely recognized by policy makers and business as a key international point of reference, and form the basis of countless local codes of corporate governance around the world. The preamble to the OECD Principles states
that they are evolutionary in nature and should be reviewed in light of significant changes and circumstances. Among their other virtues, they remain a principle-based approach to address key corporate governance issues, whether these relate to the principal agent problems of companies with dispersed ownership or those related to controlled companies.

Since the last update of the OECD Corporate Governance Principles in 2004, the process of globalization in all its different aspects has significantly accelerated. At the same time, the world economy has been confronted with significant economic challenges over the last few years. In light of this, BIAC believes that it is important and timely to now initiate discussions on how the changes that have taken place over the last 8 years should be reflected in the Principles. BIAC would like to express its strong wish to become actively involved in discussions with the Corporate Governance Committee and provide input early in the process.

In the context of the future update, BIAC would like to raise some initial considerations:

- The analysis of the changes that have taken place since the last update should be an important contribution to the update. The OECD peer reviews, the findings on the analysis of the financial crisis, as well as new work on value creation and growth should make an important input to inform the discussions.

- We also support including analysis of non-OECD country experiences. It is important that the updated Principles are based on detailed information on the changed environment and that they are relevant to as many companies and jurisdictions as possible. In particular, the movement toward controlled ownership structures pointed out in the work on value creation and growth necessitates a fresh look at how the Principles apply to majority owners. Disclosures of beneficial ownership and control should be considered.

- With respect to specific possible changes to the Principles, we support an enhanced focus on promoting long-term thinking by management and shareholders, both in terms of how remuneration is structured and how shareholders provide oversight of executive pay. We also believe the Principles should support appropriate reforms in boardroom diversity in all its aspects, board committees, board governance and oversight of risk management, non-financial reporting, shareholder voting and director qualifications. These are just a few examples of the areas where BIAC believes the existing Principles may be strengthened or where new issues may be introduced.

- We encourage the OECD to resist over-regulation, place increased emphasis on regulatory impact assessments in the area of corporate governance and seek regulatory stability. These may enhance the understanding of the potential impact of policy measures and reduce the risk of ill-conceived or overly burdensome regulation.

- We call upon the OECD to pay due consideration to the importance of fostering implementation, bearing in mind that in the past, corporate governance shortcomings have often reflected a lack of implementation of the Principles. This implementation gap must be addressed, and we support further efforts to share experiences and “best practices” among countries while striving to avoid conflicting requirements.
As a derivative of the Corporate Governance Principles, we understand that the SOE Guidelines will also be updated. Recognizing the importance of those Guidelines both for competitive neutrality and for strong oversight of state-commercial activities, BIAC would be pleased to be actively involved early in the process as well.

BIAC appreciated the transparent way in which the 2004 revision was organized and to which BIAC actively contributed. We hope that the update to be initiated next year will be organized in a similar way. This will allow BIAC to provide input, based on the contribution of its wide range of business organizations and their member companies, all along the process.

**Enforcement**

BIAC welcomes the Peer Review Paper on Supervision and Enforcement in Corporate Governance. The paper is timely in view of the proposed update of the Principles and BIAC strongly supports the issues proposed for in-depth investigation during the country analysis stage of the review. In particular, BIAC would welcome research into increasing the functional independence and funding position of securities regulators, with a view to insulating them from political interference. BIAC would also support consideration of the link between stage of market development and enforcement as well as research into the optimal interplay between public and private enforcement; non-complementary relationships in this area can lead to under- or over-enforcement which can impact growth and innovation.

In addition, BIAC supports a wider definition of private enforcement, beyond litigation. Private enforcement, depending on jurisdiction, can include the impact of changes in ratings, public approbation including in social media, external auditors, whistleblowers, and positive incentives as enforcement, such as those provided by ‘good governance’ segments of stock exchanges and investment indices. The definition of private enforcement should also include key ‘internal gatekeepers’, internal to the company, such as the company secretary, the internal auditor and independent directors. We generally support a wider definition beyond litigation and we support wider application of enforcement.

BIAC also supports research into how public and private enforcement may differ among non-listed companies. Given the decline in numbers of listed companies in many jurisdictions, policymakers may wish to understand how governance practices at private firms are enforced to ensure the public interest is served.

**Risk oversight and peer review 6**

BIAC welcomes the introduction of Peer Review 6 and encourages a wide review of existing practices for oversight of risk. However, while risk governance is important, BIAC also underlines the importance for business to take risk, recognizing that risk-taking always involves striking a balance between managing risk and managing opportunity. At the same time, we would like to note that as far as terminology is concerned, ‘risk management’ implies a role for management whereas the recent crisis has shown there was insufficient ‘risk governance’ by the boards. We would therefore encourage the consistent use of ‘risk governance’ or ‘risk oversight’.
Oversight of risk-taking is one of the most urgent tasks facing business in the wake of the financial crisis, and there are few areas of consensus about how boards of directors should do this most effectively. While there have been attempts in some jurisdictions to introduce a board-level risk committee (for example in Singapore and in the US, for large banks), there are other views that it is the board as a whole that should be responsible for oversight of risk. Certain enterprise-wide risks, like technology risk, regulatory risk, and reputational risk, may argue for involvement from the entire board. On the other hand, BIAC wishes to learn from global experience in this area, and to understand the advantages and disadvantages of different models.

BIAC supports the peer review’s focus on how companies can best manage risks on an enterprise-wide basis, and avoid management by silo. BIAC also supports the focus on state-owned enterprises, where risk practices may in some cases be less-developed. Here, again, professionalization of SOE directors should be encouraged. As in 2011 and 2012, COSO has been reviewing its framework the OECD work on risk should seek to benefit from COSO’s recent knowledge in this area.

There is currently very little reference to risk in the OECD Principles. Consideration should be given to an increase in the guidance to be provided both in the Principles and in the Annotations after the review. Finally, BIAC also encourages the Committee to look at the role of investors in encouraging advances in board risk oversight: investors have historically asked few questions of boards and management about risk management practices, or sought improved disclosure in this area. It remains to be seen how investors can be encouraged to use enhanced disclosure about risk management to better seek accountability or pursue private enforcement.

**Future work on diversity, including gender**

BIAC has been actively involved in OECD gender work and submitted a major report to the 2012 OECD Ministerial Council Meeting. The report highlights a number of programs that support and promote change in advancing women’s leadership opportunities in business organizations. Business fully recognizes that there are important equity issues associated with the economic empowerment of women. At the same time, there is an undeniable business and economic case in promoting, attracting and retaining female talent in business.

In this context, a lot of attention has focused on increasing the number of women on boards. More women are needed on executive committees and in senior executive positions. But it also means that there must be more women in the talent “pipeline.” In some countries, law-enforced targets for the percentage of women on boards have achieved greater representation. However, in BIAC’s view, quotas do not address the actual causes for the lower percentage of women in executive positions that already arise much earlier in women’s careers. Importantly, there are some examples of voluntary multi-stakeholder initiatives that are producing positive results.

In addition, there are companies that have successfully implemented voluntary strategies to establish greater gender balance throughout the organization. Improving gender diversity and equality in business requires diverse solutions, adapted to the socio-cultural context. There is no one-size-fits-all approach for successful diversity programs, which require a combination of
proactive leadership and company practices and measures throughout all levels of the organization.

We recently learned that the OECD Directorate for Employment, Labor and Social Affairs has launched discussions on a Draft Council Recommendation related to gender issues. While not legally binding, practice accords OECD Council Recommendations great moral force as representing the political will of Member countries and there is an expectation that countries will do their utmost to fully implement a Recommendation. While realizing that the current draft is an initial draft and that the Corporate Governance Committee has not yet discussed it, we call upon the Committee to become actively involved in discussions on the draft Recommendation, which among others refers to target setting for leadership positions and introduction of quotas for women in executive and supervisory boards of listed companies.

As mentioned above, in BIAC’s view, quotas do not address the actual causes for the lower percentage of women in executive positions that already arise much earlier in women’s careers. BIAC will submit broad-based business input in due course, bringing together comments from a range of BIAC Committees.

With regard to future work, we generally believe that the Corporate Governance Committee can make an important contribution to the gender project, e.g. by analyzing the effectiveness of different approaches that have been taken and sharing best practices and experiences, including through case studies of company specific practices and experiences. However, BIAC underlines that diversity is broader than just gender.

We generally support work on the role and impact of women on boards. However, it should be noted that research has shown diverse results, and it is not a foregone conclusion that women on boards improve corporate governance and performance. On the other hand, there is some evidence with regard to non-executive directors and to some extent, independent directors. BIAC would be pleased to make an active contribution to future work in this area.

**Global relations strategy**

BIAC appreciates that the OECD Corporate Governance Committee has established an active and constructive dialogue with non-member countries. Document DAF/CA/CG(2012)12 provides an impressive overview the regional and bilateral work with a number of key non-member economies. BIAC broadly supports the increased work of the Organization with “key partners” and other non-OECD countries and has significantly stepped up its own outreach activities. BIAC now has observer business organizations in the following countries: Argentina, Brazil, Colombia, India, Indonesia, Latvia, Morocco, Russia and South Africa, which are becoming increasingly active in our policy work. BIAC also has an active China Task Force, and has recently organized several meetings with in major emerging economies on different topics. We would be pleased to explore ways to become increasingly involved in the Corporate Governance Committee’s work with non-members and help establish contacts with local business organizations as appropriate.
Corporate Governance of state-owned assets and privatization practices

BIAC appreciated the opportunity to participate in the recent SOPP Working Party. Among others, BIAC expressed its appreciation for the OECD report “Competitive Neutrality: Maintaining a Level Playing Field between Public and Private Business”, which was published earlier this year. The report provides an excellent analysis and meaningful guidance for governments to address their relationship with SOEs with a view to establish competitive neutrality between SOEs and privately capitalized firms.

BIAC would like to take the opportunity to express again its strong support for a robust, broad-based OECD work program on competitive neutrality, which would bring together corporate governance, competition, trade and investment considerations. The OECD can make an important contribution by providing a deeper and wider understanding of key challenges and opportunities, while fostering capacity building by sharing its analysis with emerging economies and engaging in a constructive dialogue with them. BIAC would like to congratulate the OECD for demonstrating leadership in the area of competitive neutrality, which is of crucial importance to business. We offer strong support for further work and encourage the OECD to keep looking for better models of oversight that take into account the unique principal agent issue in SOEs. BIAC would be pleased to remain actively involved in further work in this area.