QUERY

Do you know of any studies, tools, or guidelines discussing the importance of anti-corruption compliance mechanisms in state-owned enterprises? In particular, we would like to know how these mechanisms should function or can be applied and what areas and issues are considered critical and deserve special attention.

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SUMMARY

State-owned enterprises (SOEs) are operated by governments around the world in critical sectors such as finance, infrastructure, energy and natural resources. SOEs are exposed to the same governance challenges as those faced by private firms and should be held to the same high standards of governance as private companies. In addition, due to their close relationship with policy makers and regulators, SOEs may face additional challenges that are more specific, such as undue political influence, conflict of interest for board members appointed by the state, and a lack of knowledge and expertise within the board and management to carry out their functions.

The OECD and the World Bank have developed specific guidelines for corporate governance of SOEs. Many corruption risk factors for SOEs are closely aligned with these corporate governance issues. Some of the critical issues related to anti-corruption compliance in SOEs include the smart management of the state’s role as the owner and regulator of the enterprises, selection and appointment of the SOE boards, establishing internal controls and strong auditing procedures, transparency and disclosure of financial and non-financial information, and adopting and integrating ethics, code of conduct and anti-corruption compliance across the entire organisation.

Governments and SOEs that have followed these principles have had success in curbing levels of corruption and promoting high integrity amongst their SOEs.
1 STATE-OWNED ENTERPRISES AND THE NEED FOR ANTI-CORRUPTION COMPLIANCE

Defining a state-owned enterprise

State-owned enterprises are commercial enterprises that have been created and are owned by the state. The OECD defines an SOE as when the state has “significant control through full, majority or significant majority ownership”.

SOEs can operate in competitive or non-competitive sectors of the economy, be listed on a stock exchange or not, and may or may not pursue a public policy objective. According to the OECD, the rationale for state ownership of companies typically combines social, strategic and economic interests, such as industrial policies, supply of public goods or regional development. In many countries, SOEs are key providers of infrastructure and utility oriented services such as road, rail, power and communications. In several countries, SOEs also play a significant role in the extractives industries, controlling substantial revenue flows. In many low income countries, SOEs are often among the largest employers, contributing to a substantial percentage of the workforce.

Specific corruption risks of state-owned enterprises

Although SOEs face similar governance challenges as private sector firms, according to the World Bank SOEs are prone to greater corruption risks due to some additional challenges. These are mainly due to factors such as multiple principals, politicised boards and management, and low levels of transparency and accountability (World Bank 2014).

In many SOEs, the state frequently exercises its ownership responsibilities through multiple actors such as line ministries, ministry of finance and other governmental bodies that lead to SOEs being used for short-term political goals rather than fostering accountability and achieving efficiency. The proximity of SOEs to other state organs or state-owned entities, such as banks or financial institutions, which can be clients or suppliers to the SOEs, creates a potential risk for favouritism and unfair procurement.

In addition, politicised boards and political appointment of chief executives leads to poor oversight of managers and increases the risk of corrupt activities going unchecked. Many SOEs have weak internal controls with inadequate and/or irregular auditing practices as well as low levels of financial and non-financial disclosures. Such practices limit accountability creating conditions, thereby making them more prone to corruption (World Bank 2014).

Principles for fighting corruption

Any enterprise, including SOEs, need to have clear standards or principles to which the SOE and its representatives must adhere to counter corruption. Such anti-corruption standards are established either through law by the state and/or through a code of conduct put forth by the SOE. The OECD convention on combatting foreign bribery and the UN Global Compact’s 10th principle against corruption offer standards and principles on which an effective anti-corruption compliance mechanism can be built. The UN Global Compact also provides a business case for companies to not engage in corruption.

2 STANDARDS OF CORPORATE GOVERNANCE FOR STATE-OWNED ENTERPRISES

Anti-corruption compliance mechanisms in SOEs are tightly aligned with good standards of corporate governance. International guidance on good corporate governance standards for SOEs is available mainly from the OECD and the World Bank. In addition, Transparency International’s Business Principles for Countering Bribery provides a framework for companies to develop anti-bribery programmes. Although this is not tailored to SOEs, most of the principles are also applicable to SOEs (Transparency International 2010).

SOEs that are listed on stock exchanges are bound by the regulations of the stock exchanges and are therefore more likely to have stronger corporate governance standards. However, all SOEs should be accountable to their stakeholders and comply with corporate governance standards similar to that of private companies.
Key anti-corruption guidelines for state-owned enterprises

The OECD SOE corporate governance principles and the World Bank corporate governance toolkit for SOEs provide guidance on measures to be taken by the state to deal with corruption risks in several areas (OECD 2005; World Bank 2014).

Ensuring effective legal and regulatory framework

Given that the state is the primary owner and plays an important role in the management of the SOE, there should be a clear separation between the state’s ownership function and other state functions that may influence the conditions for SOEs, particularly with regard to market regulation. Such a separation of powers will enhance the identification of the state as the owner and will favour transparency in defining objectives and monitoring performance. To prevent conflict of interest, it is also necessary to separate the ownership function from any entities within the state administration that might be clients or suppliers to SOEs. Therefore, general procurement rules that apply to other companies must also apply for SOEs.

SOEs are also at times expected to carry out public service responsibilities and receive compensation from the state budget for these activities. These must be clearly mandated by laws and regulations to ensure the general public are informed of these obligations and their financial compensation (OECD 2005).

The state acting as an owner

The government should develop an ownership policy that defines the overall objectives of the state ownership. The ownership strategy should contain a structured board nomination process and avoid a role for the state in day to day management of the SOE. The state should also let SOE boards exercise their responsibilities without undue political interference.

Board of directors

Board members should act independently in the interest of the company and should not act as representatives of different constituencies or take part in regulatory decisions concerning the SOE. All potential conflicts of interest concerning board members should be disclosed together with the chosen management decision.

Modern good practice suggests that boards consist of more independent directors to enhance objectivity and independence of the SOE. In many countries, ministers and political appointees are prohibited from being on SOE boards. It is also good practice to restrict the number of government appointees on the board. To reduce ministerial influence, a number of countries have adopted governance reforms that delegate part or all of the nomination process to an advisory body, expert panel, or the SOEs themselves (World Bank 2014).

Auditing

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 (OECD 2005). The board is responsible for ensuring the integrity of the SOE’s accounting and financial reporting systems. Internal audit reports should be included in the financial statements. SOEs should also be subject to an annual external audit by auditors who are independent from the management and shareholders. These external audits must be carried out in accordance with international standards.

Transparency and disclosure

SOEs should abide by high standards of transparency, many of which are in accordance with the principles of corporate governance applied to private companies. The government’s ownership entity should establish consistent and aggregate reporting on SOEs and produce an annual aggregate report as a key transparency tool directed to parliament as well as the media and general public. It should provide information on the financial performance, main financial indicators and value of SOEs, as well as the general statement of the state’s ownership policy and its implementation, including information on how the ownership function is organised.

Transparency International (2014) provides recommendations and guidance to companies in
relation to their corporate reporting, most of which can equally apply to SOEs:

- Companies should disclose detailed information about their anti-corruption programmes. Global Compact’s Anti-corruption Reporting Guidance provides a matrix for anti-corruption reporting, ranging from zero-tolerance statements and whistleblowing mechanisms to staff training and publicity of corruption cases.
- Companies should publish complete lists of their affiliates, subsidiaries, joint ventures and other related entities.
- Companies should publish individual financial accounts for each country where they operate.
- Companies should have a corporate website that centralises all disclosed information and is available in at least one international language.

Ethics and codes of conduct

Irrespective of the type and size of SOE, it is good practice to have an ethics code of conduct that applies both to the business practices as well as to the personal conduct of employees within the organisation. Such an ethics code should:

- prohibit the giving or accepting of bribery, facilitation payments and other forms of corruption, such as gifts, in unequivocal terms
- clearly state that the company’s policy on anti-corruption applies to all individuals acting on the company’s behalf, including board members, management and other staff
- mandate all employees and company representatives to be aware of the company’s code of conduct and anti-corruption policies
- set guidelines for conflict of interest situations and disclosure policies on conflict of interest for the SOE board and management
- set up an ethics helpline that is accessible to all individuals in the company to consult/report on ethics cases ensuring anonymity of the reporter

The OECD good practice guidelines on internal controls, ethics and compliance recommends that companies’ senior management express strong, explicit and visible support and commitment to internal controls, ethics and compliance programmes in place to detect bribery and corruption. In addition, adequate oversight measures should be in place to monitor ethics and compliance programmes, including the authority to report matters directly to either the internal audit committee or the ethics committee of the board of directors. To be effective, the ethics programme should rely on employees and others to raise concerns about violations as early as possible. To this end, the company should provide secure and accessible channels through which employees and others should feel able to raise concerns and report violations (whistleblowing) in confidence and without risk of reprisal.

The SOE could also appoint a compliance officer to head the anti-corruption compliance function. The responsibility of the compliance officer includes:

- administer the anti-corruption compliance programme by designing and coordinating appropriate training for all employees
- initiate investigations related to corruption on behalf of the organisation
- monitor and receive reports from the ethics helpline
- provide guidance to SOE staff on ethical challenges

SOEs should also undertake periodic reviews of the ethics and compliance programmes in order to evaluate their effectiveness in preventing and detecting bribery, taking in to account relevant developments in the field and evolving international and national standards for anti-corruption compliance (OECD 2010).

3 GOOD PRACTICE COUNTRY EXAMPLES

The following country examples provide some good practice guidelines for the state and SOEs to implement measures to enhance transparency and reduce risk of corruption.

Good practice examples of government initiatives

Croatia

According to the OSCE, the Croatian government set out a strategy to enhance integrity, ethics and reduce corruption in SOEs. The set of anti-corruption measures adopted included appointing an information officer for all SOEs and ethics commissioners. In addition, SOEs are required to
appoint an irregularities officer to create an effective system for reporting. All SOE employees were trained in ethics, anti-corruption, financial management, internal supervision and control, informing and public procurement.

The new strategy set out to make prevention and defence against corruption the responsibility of everyone within and outside the company. Following the implementation of the new anti-corruption strategy, 95 per cent of SOEs appointed a supervisory board to monitor anti-corruption, 92 per cent appointed an ethics commissioner and 91 per cent appointed information officers. This has strengthened transparency, integrity and accountability in Croatian SOEs (OSCE 2012).

Spain

In Spain, legal change was enacted in 2006 to prevent conflicts of interest for directors and managers of SOEs. The new law first defines conflicts of interest, including the proximity of such individuals who can be considered as sharing the personal interest of SOE officials. It establishes rules on full-time commitment to the duties of managing or overseeing an SOE, restrictions on shareholding in the SOE and companies related to the SOE, as well as compatibility with non-remunerated public activities. The law also establishes rules for the disclosure of financial and corporate assets by high-ranking officials in the SOE sector. Further change in 2010 reduced the number of SOE directors (and managers) to make boards smaller and more efficient (OECD 2011).

Sweden

In 2007, the Swedish government adopted new guidelines regarding SOEs reporting requirements, making the reporting requirements as thorough as for listed companies. These requirements include the publication of an annual report, interim reports, corporate governance report, a statement on internal control and a sustainability report. The government gives the SOEs’ boards the responsibility to submit a sustainability report in line with the Global Reporting Initiative. All these documents should be available on the SOEs’ corporate websites. The guidelines follow the principle of “comply or explain” and SOEs should justify any deviation in the annual report (Transparency International 2013).

Examples of Transparency International national chapters promoting transparency and accountability of state-owned enterprise

TI India and integrity pacts with state-owned enterprises

As of 2014, 49 Indian SOEs have signed integrity pacts with Transparency International India to increase the level of transparency in public contracting. Some of India’s major oil and gas corporations participate in the project. The goal of the integrity pact is to reduce any chances of corrupt practices during procurement through a binding agreement between the agency and bidders for specific contracts. These pacts get assurance from the government procurement, privatisation or licensing agencies to prevent corruption, including extortion, by their officials and to follow transparent procedures. These pacts enable governments to reduce the high cost and the distortionary impact of corruption on public procurement, privatisation or licensing, building transparency in public procurement by both public institutions and private agencies.

For the state, SOEs and private companies to enter into an integrity pact, they would need to share their code of conduct policy with TI India, provide a clear commitment to implementing the integrity pact, and appoint a nodal officer to deal with issues related to the pact with TI India. All parties should be present at the time of signing the integrity pact.

These “pre-contract” integrity pacts have had an impact on reducing corruption in procurement processes. In 2014, the Indian government terminated a €556 million with the Anglo-Italian helicopter manufacturing company, AgustaWestland, owing to allegations of bribes paid to public officials by the company. Similarly, the ministry of agriculture in India also blacklisted an American company for a period five years due to allegations of bribery. The integrity pacts were instrumental to the sanctioning of foreign companies when corruption risks were identified in the process.
ANTI-CORRUPTION COMPLIANCE FOR STATE-OWNED ENTERPRISES

Website

Blog post

**TI Hungary’s research on state-owned enterprises compliance with transparency and integrity disclosure requirements**

In 2014, TI Hungary assessed 66 SOEs for their compliance with transparency and disclosure requirements as stipulated by the law. The survey found that not a single SOE in Hungary disclosed all of the data that is prescribed by the law. On average, companies scored 46 out of 100 points. In addition to the general transparency of companies, the study also examined the integrity of corporate governance as well as the implementation of organisational solutions for promoting integrity. They used the information available on the companies’ websites. Furthermore, structured interviews were conducted with key executives of seven state-owned enterprises in which they were asked about the prevalence of transparency as a value, organisational and regulatory solutions promoting integrity, as well as how these were made operational in the company.

One of the important lessons of the study is that much depends on the attitude of a company’s chief executive. The majority of executives viewed compliance with existing laws as establishing integrity and transparency and did not concern themselves with questions of transparency. Modern regulatory tools for promoting integrity were absent, and most of the executives were unfamiliar with the advantages and positive effects such tools have on a company’s efficiency.

Website

**TI Slovakia’s ranking of Slovak state-owned companies**

In 2012, Transparency International Slovakia produced a transparency ranking of the state and municipality-owned companies in Slovakia. The data was collected from companies’ websites as well as through freedom of information requests and journalists’ answers to a questionnaire. The survey measured information availability, as well the presence of anti-corruption measures in six policy areas: economic indicators; communication and access to information policy; public procurement policy; human resources policy; ethics; grants and charity policy.

In 2013, TI Slovakia launched a website focused on SOEs, with continuously updated information on new tenders announced, key financial information such as debt and profit/loss on quarterly basis, property sales, key personnel changes (CVs and salaries included), grants given to make public monitoring of SOEs easier and more comparable. Data available on this website is obtained through scraping, official registers and, in part, collected manually.

Since September 2014, TI Slovakia has been carrying out an anti-corruption audit in the SOE Slovak Post. Four to six experts assess the firms’ internal rules and practices in cooperation with SOE managers. The audit serves as a tool to help managers implement anti-corruption measures. It will be designed for those who are interested in deeper changes yet lack capacity to carry them out.

Website

**TI Russia’s monitoring of procurement to state-owned enterprises**

As of 2012, Russian SOEs need to publish rules for purchasing and service contracts, as well as report all public contracts exceeding €2,500. Since 2009, Transparency International Russia has been involved in monitoring buying patterns and procurement in Russian SOEs, starting with Rosatom, followed by Olympstroy, Rotechnolgii, Vnesheconombank and other SOEs.

The transparency of SOEs was evaluated on the following factors: management features, full disclosure of corporate information and disclosure of information on public procurement. The study found that the websites of four out of the six SOEs evaluated had no section devoted to compliance and anti-corruption. There was also had no information on the existence of committees for resolving conflict of interest and no information published on financial returns for specific periods. The study identified many conflict of interest issues related to board
chairpersons in the SOEs studied.

Website (in Russian)

Blog Post

4 REFERENCES


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