Corporate Governance of State-owned Enterprises: A Framework for Addressing Board Accountability Deficit in State-owned Enterprises

A thesis submitted for a degree of Doctor of Philosophy

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DECLARATION

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SUMMARY

Accountability is the quintessence of a successful corporate governance regime; it pushes a board act in the best interests of an SOE and ensures a board is responsible for its actions. This thesis highlights how accountability standards for boards of SOEs have failed to provide an adequate governance framework, which has resulted in an accountability deficit. The recommendations contained within this thesis sets out proposals for implementing a better regime to increase board accountability.

This thesis examines central aspects of board accountability, along with internal and external mechanisms of accountability. The regulatory framework underpinning accountability is reviewed, governance on a quasi-legal basis can be successful, but this requires robust principles that demand more than an expectation that SOEs will comply with governance standards. It is recommended in a departure from the traditional comply or explain principle, SOEs should implement governance on a comply and co-operate basis. This requires a board to co-operate with the relevant Minister to advise them in advance of governance standards it will not implement and provide a statement on how it has met their governance objectives. A lack of board accountability and monitoring of SOEs was evident through an examination of the actions of the board in the FÁS saga. This case highlighted the freedom the board exercised in spending State funds, the failure to implement government policy, and for which the board suffered minimal repercussions for its actions.

A framework has been drafted which takes steps to reduce board accountability deficit in SOEs. Provisions dealing with board accountability should be structured on a three tier basis. Firstly, there should be a planning and consultation process, with the establishment of a governance committee to form the corporate governance regime, through a statement of corporate intent. This should be subject to Ministerial approval who may exercise a veto, if necessary. The second stage should involve the implementation of governance and the application of governance principles. As part of this a board should complete a self-evaluation questionnaire indicating how they have engaged with standards and what standards they did not implement. The third stage in the process is a review of how governance principles have been executed by the board, as accountability requires the

board to be responsible and answerable for their decisions. Penalties should be imposed and a revision of governance practices going forward should be implemented where necessary.

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CHAPTER 1:
ADDRESSING BOARD ACCOUNTABILITY IN STATE-OWNED ENTERPRISES

A. INTRODUCTION

It's a commonly cited dictum that the 'State has no business in business.'[1] Indeed the State has no business in the vast majority of companies registered in Ireland. However, the State is required to meet social and public policy objectives to drive national economic development and to provide public utilities.

To pursue this objective, governments often use State Owned Enterprises (SOEs) to deliver public goods and services. It is necessary for the State to be involved in business where it is in the national interest and SOEs also fill the gap left by the private sector where there is no commercial incentive to enter a particular sector. For example, the State facilitated the supply of electricity[2] through the Electricity Supply Board (ESB) in Ireland.

The OECD has recognised that in certain situations it is more appropriate for the State to provide a service. These situations are recognised as being where it is a national necessity, for providing merit goods, i.e. services free of charge such as healthcare and education or situations where the private sector overproduces goods with negative externalities, such as pollution.[3] Such enterprises may have commercial objectives to generate income from the goods and services they provide to the public or they may have non-economic objectives and be specialist bodies with a focus of maximising public welfare.

In providing these services ensuring efficiency, transparency and competitiveness is crucial. To establish this SOEs need to implement strong governance practices on board accountability in order to maximise their contribution. Accountability portrays a sense to the public of trustworthiness and openness that those in management are working responsibly and respecting their obligations. Accountability within SOEs is complex, the

[1] Rentsch, C. & Finger, M "Yes, No, Maybe: The Ambiguous Relationships between State-Owned Enterprises and the State" (2015) 86 (4) *Annals of Public & Cooperative Economics* 617 p. 625.
[2] *Electricity Supply Act* 1927.
[3] OECD *Corporate Governance of State-Owned Enterprises: A Survey of OECD Countries* (Paris 2005) p 20 & 21.

dynamics of an enterprise where the State has a stake differ significantly to enterprises without State involvement and the relationship between the State and SOEs adds to the complexity.

Luke recognises that accountability in SOEs becomes less clear as SOEs are subject to government influence, answerable to the government as shareholders and monitor by the government.[4] The pertinent issue is how should the government manage their relationship with the board of SOEs as both owner and regulator of SOEs? A balance between the State having control over SOEs without impinging on economic enterprises should be sought. How governance decisions are made in the case of State ownership is a key issue. The motivation for decision-makers is central to this analysis, how politicians when acting in their capacity as owners on behalf of the State should monitor and incentivise managers of SOEs. But how close should the relationship be between government and SOEs? A Minister appoints a board of directors but the directors are obliged to implement government strategic policies and are accountable to government and the Oireachtas for their actions. This highlights the dependence both SOEs and the government have on each other which centralises both Agency theory as key corporate governance principle in the State-SOE relationship.

SOEs face governance challenges that can impact their ability to perform efficiently. This is linked to the principal-agent relationship that arises in the context of SOEs. SOEs are assets that a government manages on behalf of citizens. Good corporate governance practices are expected from SOEs so the assets create value for money. Agency theory recognises that agents may not act in the best interests of the entity. Within SOEs the State has additional powers and capabilities so these relationships need to be co-ordinated effectively. Stakeholder theory overlaps with Agency theory, Agency theory takes a narrow focus of shareholders whereas Stakeholder theory expands this taking into account the interests of many stakeholder groups. The State is owner of SOEs but has influence over SOEs but the commitment to accountability in SOEs is to multiple stakeholders who may have conflicting interests. This thesis seeks to establish how a code of corporate

[4] Luke, B. "Examining Accountability Dimensions in State-owned Enterprises" (2010) 26(2) *Financial Accountability & Management* 134 p. 134.

governance can fulfil the obligation of ensuring boards of SOEs operate in the best interests of stakeholders as corporate governance for SOEs covers:

"the set of responsibilities and practices, policies and procedures, exercised by an agency's executive, to provide strategic direction, ensure objectives are achieved, manage risks and use resources responsibly and with accountability."[5]

The board of directors is central to an accountability framework. The board implements corporate governance standards as it has a responsibility for promoting the success of organisations' governance.[6] When irregular activities come to light within a corporation the first area that comes under scrutiny is the board of directors, to examine if they are an effective functioning board. It is therefore logical that a board becomes the central internal control for measuring how governance standards are utilised in practice. The role of a director is a substantial job in any circumstances but directors for SOEs have additional permutations to consider, including having to factor in the requirement of serving the interests of the public, while having to report to government departments. Traditionally directors are expected to act in the best interests of the company but the scope of their duties must move stakeholders to the forefront and act in their best interests. Identifying stakeholders becomes an important factor in SOEs as whose interest directors should consider from the groups of stakeholders. While there may be an expectation for governance for listed companies to be driven to protect those who fund the companies, should the same premise filter into governance for SOEs and place taxpayers as central stakeholders? It is argued that good governance should help define shared measures of success between organisations and its stakeholders.[7] The board is directly accountable to taxpayers/shareholders for the performance of SOEs and:

[5] Australia ANAO and Department of the Prime Minister and Cabinet, 2006, Implementation of Programme and Policy Initiatives: Making Implementation Matter, Better Practice Guide, Commonwealth of Australia, Canberra p. 13.
[6] Financial Reporting Council (UK) Report: Review of the Role and Effectiveness of Non-Executive Directors (*The Higgs Report*) (2003) p. 5.
[7] Kenny, P. "Corporate Governance for the Irish Arts Sector" (Chartered Accountants Ireland Publishing Dublin 2014) p. 6.

"The board's key purpose is to ensure the governance and prosperity of the body by collectively overseeing the board's affairs, whilst meeting the appropriate interests of its shareholders and stakeholders."[8]

However, Ebrahim questions "if is feasible, or even desirable for non-profit organisations to be accountable to everyone for everything?"[9]

Accountability is important because State investment into SOEs should reflect the value of the contribution by ensuring the investment is spent correctly and the enterprise is managed efficiently and fulfilling its function. The State's involvement in the running of SOEs should be carried out while strictly adhering to corporate governance standards, which balance the political involvement in business to ensure that SOEs are run effectively and in the best interests of society. The Code of Practice for the Governance of State Bodies[10] sets out corporate governance standards for Irish SOEs.

This thesis examines the role of corporate governance standards currently in place for SOEs. It will examine the extent whether current standards offer appropriate safeguards to manage accountability expectations or if alternative code provisions for board accountability for SOEs is required. Corporate governance of SOEs is topical because corporate governance of certain commercial SOEs has recently been reformed. Corporate governance for commercial SOEs that include the ESB, Bord Gáis, EirGrid, Bord na Móna, Coillte has now been centralised under the recently formed New Economy and Recovery Authority (NewERA). The result of this new body moved the responsibility for corporate governance from the government to NewERA.[11] NewERA was established on a statutory basis as a Shareholder Executive under the National Treasury Management

[8]See the Role of Board Members, appointments to State boards, available www.stateboards.ie/stateboards/questionnaire/intro/24.htm?lang=en last accessed August 2017.
[9] Ebrahim, A. "The Many Faces of Non-profit Accountability (2010) *Harvard Business School* Working Paper No 10-069.
[10] The Department of Public Expenditure and Reform *Code of Practice for the Governance of State Bodies* (Dublin 2016).
[11] RTÉ News "NewERA Body to Manage State Stakes" 29 September 2011. Available at http://www.rte.ie/news/2011/0929/newera-business.html last accessed August 2017.

Agency.[12] It is envisaged that NewERA will become a holding-company owning shares in SOEs but there is a sunset clause that will dissolve the organisation after seven years.13

The objective of this research is to assess the accountability dimensions within boards of Irish SOEs. This will help give an understanding on the quality of existing governance standards. With a focus on corporate governance it will address the State-SOE relationship. This requires analysis to extend to accountability within both commercial and non-commercial SOEs as the regulatory approach between both entities emphasise the need for a strong engagement with Agency and Stakeholder theory. Limiting research to either commercial or non-commercial SOEs may undermine the level of board accountability expected from SOEs and will result in an unwelcomed gap in the accountability framework expected from both entities. Ultimately both entities have similar goals, albeit commercial SOEs focus on profit maximisation, whereas non-commercial SOEs is focused on welfare maximisation. Robust accountability provisions should ensure sound financial reporting and risk management, which is critical if SOEs want to earn autonomy.

B. SOES IN CONTEXT

(1) Defining SOEs

An SOE has been described as "any autonomous public body with a board appointed by the Government to discharge those functions assigned to it by the Government."[14] It is accepted that SOEs operate at arm's length from the government but remain accountable to the government.[15] State ownership takes many forms, making the task of defining SOEs particularly difficult, as a definition would have to encompass the broad range of what SOEs cover.[16] State bodies can be divided into commercial, non-commercial and

[12] See National Treasury Management Agency "New Economy and Recovery Authority" Available at http://www.ntma.ie/business-areas/new-economy-and-recovery-authority/ last accessed August 2017.
[13] Palcic, E. & Reeves, D. "Is this a New Era for the State-owned Sector or a False Dawn?" *The Irish Times* 16 December 2011.
[14] MacCarthaigh, M. *The Corporate Governance of Commercial State-Owned Enterprises in Ireland* (Dublin 2009 IPA CPMR Research Report 9) p. 4.
[15] McGauran, A.M., Verhoest, K. & Humphreys, P. *The Corporate Governance of Agencies in Ireland* (Dublin 2005 IPA CPMR Research Report 6) p. 4.
[16] Research carried out by Forfás (Ireland's policy advisory board for enterprise and science) pointed out that is difficult to find a definition of SOEs that can be used to compare SOEs between countries as the nature of

regulatory bodies. Commercial bodies have a commercial function, whereas non-commercial board have regulatory, development or advisory functions.[17] A key difference is from their Revenue source:

"There is a fundamental difference between commercial and non-commercial State-sponsored bodies. Commercial State-sponsored bodies derive the greater part of their current revenue from the sale of goods and services; non-commercial State-sponsored bodies are similar to executive branches of Government Departments with almost all revenue provided by way of voted moneys."[18]

There is no precise definition of a State body but it can be identified by the following criteria:

"The Minister presents legislation relating to the body to the Houses of the Oireachtas.
The Minister lays the body's financial statements and/or annual report before the Houses of Oireachtas.
The Minister and/or the Department has statutory responsibility for one of more of the following:
a. provision of funding;
b. presentation of estimates in the Dáil;
c. nomination / dismissal of all / majority of the members of a body's Board, d. appointment of Chief Executive Officer (CEO);
e. consent functions in relation to remuneration, superannuation, fees;
f. consent functions in relation to borrowing.
The statutory basis of the body.
The Minister sets policy direction for the body.
The Minister has the power to issue directions, codes, regulations or guidelines in respect of the body.
The Minister approves Statements of Strategy."[19]

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an SOE is particular to that country. Forfás *The Role of State Owned Enterprises: Providing Infrastructure and Supporting Economic Recovery* (Dublin 2010) p. 13.

[17] Supra note 10.

[18] Summarised by the Chairman of the PAC, Gay Mitchell T.D. in a Dáil Éireann debate 1989.

[19] Adapted from Department of Public Expenditure and Reform "Corporate Governance Standard for the Civil Service" (2015) p. 28.

Interestingly the term SOE is often used interchangeably with semi-State bodies and State-sponsored bodies, which are a useful starting point in defining SOEs. Fitzgerald sees semi-State bodies arising during times of national importance and when they are unlikely to be undertaken privately. He defined semi-State bodies as:

"Autonomous public bodies, neither temporary in character nor purely advisory in their functions, whose staff is not drawn from the civil service, but to whose board or council the government or ministers in the government appoint directors etc."[20]

It is important the difference between SOEs and semi-State bodies is recognised. At first inspection of the definition of SOEs there appears very little that distinguishes a semi-State body from SOEs but the dissimilarity is easier to identify in commercial SOEs. Lee advocated the distinction is understood in terms of their use, where semi-state bodies are established by government, with public funds, to undertake a specific function in the public interest. Commercial SOEs are expected to combine enterprise with public accountability. They must have flexibility and initiative of private enterprises but to observe a public interest mandate.[21]

Another distinguishing factor is SOEs will be established by the State, whereas semi-State bodies may be initially incorporated as private companies without State assistance but the State may buy a stake in the company at a later stage. To take an example, Comhlucht Siúicre Éireann, The Irish Sugar Manufacturing Company was initially established as a private company but when it faced severe financial difficulties in the 1930's it would not have been viable to continue as a going concern without State intervention, and so it became an SOE under the *Sugar Manufacturing Act* 1933 so that Ireland could continue to produce its own sugar.[22]

[20] FitzGerald, G. *State-Sponsored Bodies* (Institute of Public Administration Ireland 1963) p. 29.
[21] Lee, F. "Ireland's Semi-State Bodies in a Time of Change" (2007) *Department of Government Working Paper, No. 4* p. 4.
[22] *Sugar Manufacture Act 1933.*

Aside from resulting in an intervention from governments another distinguishing feature between SOEs and semi-State companies is SOEs will often have a sole shareholder namely the State, whereas semi-State companies the State may be the main shareholder but not the only shareholder and institutional investors may also be shareholders. For example, the State took the initiative to provide transport within Ireland and so CIÉ was established with the government as the sole shareholder.[23]

(2) Categories of SOEs

As the term SOE has been the subject of much debate and in defining SOEs, an examination of State agencies is required. A popular approach is for State agencies to be broken down into classifications. In recognition of the different classes of State agencies, Scott recommends six classifications based on ownership, legal form, funding functions, powers and governance level.[24] The categorisation based on the State being owner of an organisation does not offer sufficient clarity to the composition of SOEs, this broad definition includes all agencies concerned with the provision of goods and services using government revenue. Scott provides further analysis and advocates a legal form categorisation based on how State bodies are established, which primarily is through statute or Ministerial order.[25] State agencies are established through one of the following methods:

- statutory corporations, deriving authority and powers directly from statute and not incorporated as companies under the Companies Act;
- corporate bodies, established through secondary legislation by ministerial order;
- public companies, established under statute and registered as a company under the Companies Act; and
- private companies, registered as a company under the Companies Act and with any special conditions as to operations included in their memorandum or articles of association.[26]

[23] Córas Iompair Éireann established under *The Transport Act* 1950.
[24] Scott, C. "Organizational Variety in Regulatory Governance: An Agenda for a Comparative Investigation of OECD Countries" 2003 3 (3) *Public Organization Review* 301 p. 305.
[25] Ibid.
[26] Supra note 15 p. 41.

The most common method for establishing State agencies is through legislation.[27] Scott points out that, while State agencies are owned by the State, it is their legal form that distinguishes different agencies based on their legal form.[28]

Other categories recommended by Scott includes classification based on who fund the organisation, but raises concern using classification based on funding as he doubts if there is any discretion over who funds the organisation and to what amount.[29] Function categorisation is based on what role and purpose of the organisation.[30] Categorising of State agencies based on powers and governance level is linked to the manner in which power is exercised.[31]

Hardiman and Scott analysis the changing profile of State agencies and consider that State agencies are based on one of the four modes of State action: development, regulatory, adjudicatory and moral advocacy.[32] Development State agencies describe the role that State agencies had in the economic development of the country. This happened in different stages, which include the establishment of the Free State and when Ireland joined the EEC in 1973. Examples of development State agencies include the Electricity Supply Board (ESB), Industrial Development Authority (IDA) Ireland and National Treasury Management Agency.

The regulatory State classification focuses the establishment of free-standing semi-independent regulatory bodies to regulate economic and social issues, which include the Higher Education Authority and the Irish Sports Council. The adjudicatory State was the introduction of conflict resolution bodies to have recourse to law, such as the Personal Injuries Assessment Board and Criminal Injuries Compensation Tribunal. The moral advocacy State, refers to the development of State agencies, which is described as the

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[27] Ibid p. 49.
[28] Scott, C. "Understanding Variety in Public Agencies" 2008 UCD Geary Institute Dublin 1 p. 4.
[29] Supra note 24 p. 306.
[30] Ibid p. 308.
[31] Ibid.
[32] Hardiman, N. & Scott, C. "Governance as Polity: An Institutional Approach to the Evolution of State Functions in Ireland" (2010) 88(1) *Public Administration* 170 p. 170.

States regulation in private life, this spans the protection of individual rights within the home, to the promotion of moral Catholic values on contraception and abortion. Examples of these State Agencies include Crisis Pregnancy Agency and Residential Institutions Redress Board.

The Irish State Administration Database (ISAD) divides State agencies based on their public functions under public authority, which includes all agencies with State ownership and the second classification based on events in State agencies, which provides for merges and secession.[33] Scott provides further analysis on the classification of State agencies and points out that identification based on form and function on their own does not provide adequate guidance for categorising State agencies. He argues the varying degree of ownership and role of accountability should also be considered.[34] He points out that funding, authority and accountability are important aspects to be considered together, because an entity funded by the State does not infer it is controlled by the State, for example with education.[35]

State ownership in enterprises takes a number of forms, with consensus on a definition for SOEs not reached as the criteria can vary. The OECD defines SOEs as operating in the public sector controlled by the government and can be classified as profit-oriented entities or government business activities.[36] This can be equated to being categorised as commercial and non-commercial SOEs in Ireland. As a general rule commercial SOEs are expected to maximise earnings subject to achieving policy objectives, whereas non-commercial SOEs fulfil the public sector obligation first and generating income is not the main priority.[37]

Humphreys and Gorman identify State ownership as entities, funded by the State, where the majority of board members are appointed by an Irish Minister and derives revenue

[33] See www.ISAD.ie Last accessed 2 May 2017.
[34] Supra note 28 p. 2.
[35] Ibid.
[36] Supra note 36 p. 48.
[37] Ibid p. 83.

from public funds.[38] McGauran, Verhoest and Humphreys indorse this classification and point out that public services include both commercial and non-commercial organisations; bodies which do and do not derive the bulk of their revenue from trading and commercial activities.[39] This is based on an expectation of commercial agencies to make profits, pay dividends and finance new investment and that non-commercial State agencies are commonly established to provide advice, implementation of policy and regulation and the provision of policy.

Indorsing the definition of SOEs provided by McGauran, Verhoest and Humphreys, the starting point for defining SOEs is through their ownership structure where the State has control over the organisation. As SOEs may provide non-financial services they should also be identified by their attributes. Commercial SOEs have financial and economic objectives with an expectation for them to be profit making. Christiansen points out that often the reason that non-commercial SOEs are established as SOEs, rather than carried out by the government, is that it is more efficient for the activity to be carried out through an SOE.[40]

(3) Commercial State bodies

A distinction between commercial and non-commercial SOEs arises as it's necessary to define main objectives between the two entities, formulate expectations of how SOEs will operate on either a commercial or non-commercial basis and to be in a position to assess their performance.[41] Commercial SOEs have the potential from their income streams to be profitable.[42] Commercial State bodies tend to be self-supporting, or at least there is mounting pressure for them to be self-sufficient,[43] so that they are able to generate revenue in the hope that they will not need to be subsidised by the State once their start-up costs

[38] Humphreys, P. & Gorman, P. Information on Public Sector Employment and Manpower (1987) *Institute of Public Administration* 1 p. 8.
[39] Supra note 15 p. 31.
[40] Supra note 36 p. 6.
[41] Supra note 36 p. 47.
[42] Supra note 36 p. 19.
[43] MacCarthaigh, M. *Government in Modern Ireland* (Institute of Public Administration Dublin 2008) p. 95.

have been provided.[44] Despite the fact that an SOE may be a commercial body it will always have the security of going back to the government to seek additional funding should difficulties arise. Aer Lingus was incorporated as a commercial State enterprise but when it made significant losses in the early 1990s for a number of reasons, which included the rising costs incurred for transatlantic flights, overcoming this problem was a matter of returning to the government to look for financial support, which it received in the form of an equity injection of £175million[45] over three years.[46]

(4) Non-commercial SOEs

Non-commercial SOEs are established to pursue non-commercial activities that can operate more efficiently as SOEs rather than through government institutions.[47] The classification of non-commercial SOEs covers SOEs which by their structure will not generate revenue and so will need continuous funding by the State. They have been described as "public benefit companies."[48] Such companies are generally formed out of necessity and therefore will often operate at a loss. SOEs continue to operate at a loss because it is in the national interest to provide the services offered by SOEs. The National Transport Authority is an example of a non-commercial SOE that does not generate revenue but it aims to retrain people so as to improve employment prospects. Lemass indicates that a lack of a commercial focus may lead to inefficiencies and proposes to prevent this he advocates that:

[44] There are occasions where commercial State bodies will not generate revenue and so will provide "uneconomic services in the national interest." MacCarthaigh CPMR Research Report 9 *The Corporate Governance of Commercial State-Owned Enterprises in Ireland* (IPA Dublin 2009) p. 4. For instance not all the routes offered by CIÉ will make a profit but it is in the national interest to keep those destinations on the route.
[45] Approximately €222million.
[46] Garavan, T. O Cinneide, B. Garavan, M & Cunnningham, A. *Cases in Irish Business Strategy and Policy* (Oak Tree Press Dublin 1996) p. 261.
[47] Supra note 36 p. 3.
[48] Supra note 36 p. 19.

"The State-sponsored boards, if they are to fulfil their proper role in the national economy are required to be kept under continuous pressure, from inside and outside, to revise their procedures and costs in a continuous effort to maintain their efficiency." [49]

The importance of SOEs was recognised by Forfás, in their report where they indicated that SOEs should play a key role in economic recovery in the economic crisis due to SOEs accounting for 5.8% of GNP and employing over 40,000 people in the State.[50] SOEs play an important role in Irish society by providing infrastructures and services. These services provided by the State include the provision of electricity,[51] gas,[52] airports,[53] rail,[54] bus,[55] and broadcasting.[56] SOEs have a long history within the Irish State, the ESB[57] was one of the earliest SOEs formed.

MacCarthaigh points out agencies provide organisational focus and with sufficient autonomy can seek efficiencies.[58] This creates an expectation for non-commercial SOEs to perform in a cost effective means. MacCarthaigh also highlights that agencies provide an enhanced responsiveness, effectiveness and efficiency in performing their functions.[59] SOEs are distinguished from other State agencies based on the level of autonomy and accountability attributed to SOEs. Scott identifies statutory corporations with trading functions within the bounds of legislative authority as commercial entities. Taking the inverse of this, non-commercial SOEs can be described, rather than having a trading

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[49] Lemass, S. "The Role of the State-sponsored Bodies in the Economy" (1959) *Administration* IPA 277 p. 287. See also Barberis, P. & May.T. *Government, Industry and Political Economy* (OUP Philadelphia 1993) p. 174.
[50] "The Role of State Owned Enterprises: Providing Infrastructure and Supporting Economic Recovery" Press Release of Forfás 30 July 2010.
[51] *The Electricity Supply Board Act* 1927 section 2 established the ESB, which was the provider of electricity in Ireland.
[52] *The Gas Act* 1976 established Bord Gáis to sell gas within Ireland.
[53] Aer Rianta was established to manage Irish airports.
[54] Córas Iompair Éireann established under *The Transport Act* 1950 which set up the national bus and rail services within Ireland.
[55] Ibid.
[56] RTÉ provides radio, television and publishing services within Ireland established under the Broadcasting Authority Act 1960.
[57] The *Electricity Supply Board Act* 1927 established the ESB, which was the provider of electricity in Ireland.
[58] MacCarthaigh, M. "From Agencification to De-agencification The Changing Bureaucratic Model in O'Malley and MacCarthaigh (eds) Governing Ireland: From Cabinet Government to Delegated Governance (Institute of Public Administration Dublin 2012) 128 p. 133.
[59] Supra note 58 p. 132.

function and a social policy requirement to maximise public welfare. This indicates that the function of SOEs is the basis for categorising different classes of SOEs. For example, where the function is trading, this is what separates commercial SOEs, such as CIÉ, from non-commercial SOEs, such as Enterprise Ireland.

This thesis covers both commercial and non-commercial SOEs, as the relationship with their owner and the subjection to accountability mechanisms apply regardless of whether the SOE operates on a commercial or non-commercial basis. MacCarthaigh points out that both commercial and non-commercial SOEs have many features, including their legal status, structures of governance and modes of accountability.[60] There is support and special privileges, which include State investment, that exist in SOEs that is not present where the State is not the owner, and therefore, this requires an examination of both commercial and non-commercial SOEs. There is no distinction made in the 2009 or 2016 *Code of Practice for State Bodies*.[61] The function of SOEs doesn't demand a separation in governance standards, as both types of entities are established with taxpayer's money and have an obligation to achieve value for money. As recognised by the OECD the distinction between commercial and non-commercial SOEs is not based on public policy objectives but on their actual ability to be profitable given the company's orientation.[62] It is for these reasons, along with board accountability and political and organisational problems associated with both commercial and non-commercial SOEs, a departure in the analysis between commercial and non-commercial SOEs is not made in this thesis.

The ownership structure within SOEs presents new challenges within the principal-agent relationship. The influence of State ownership, the nature of the State's role in the funding SOEs and its role in monitoring creates issues. MacCarthaigh recognises the creation of agencies can act as a buffer between Ministerial accountability and the administrative accountability, where Minsters take credit for creating agencies but deflect criticism as the activities are carried out by a separate entity.[63] This indicates that the further removed a principal is, the less likely they are to act in the company's interest. There is an expectation

[60] Supra note 58 p. 134.
[61] Supra note 10.
[62] Supra note 36 p. 19.
[63] Supra note 58 p. 132.

that SOEs will conduct themselves to pursue the public interest. However, the objectives of SOEs are determined by government which may not always reconcile with the best interests of citizens. De-agencification arises to reduce the number of agencies due to agencies providing inadequate service delivery, a lack of accountability and fraud within organisations. MacCarthaigh supports the view of re-organisation of State agencies where guiding principles should be based on:

"responding to the needs of citizens;
The appropriate use of agencies for carrying our functions requiring specialist skills and expertise;
Regular reviews of the relevance of agency objectives in line with government policies."[64]

Conteh refers to the difficulty in establishing a definition for accountability, how it has good meaning but it not clear what obligations it entails.[65] Gray and Jenkins refer to "the obligation to present an account of and answer for the execution of responsibilities to those who entrusted those responsibilities"[66] Lewis, O' Flynn and Sullivan refer to the different purposes of accountability with public interest being a predominant purpose but the active and passive sides of accountability fosters a sense of responsibility for a successful model of accountability.[67] They note how accountability is ultimately based on performance and passing judgement on those in office.[68]

Moore highlights the concepts of board authority and board accountability are not mutually exclusive and that to increase one does not have to be at the expense of the other, the board can still enjoy the same power albeit with certain curtailment of their freedom in exercising it where the board is accountable to shareholders.[69]

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[64] Supra note 58 p. 149.
[65] Conteh, C. "Rethinking Accountability in Complex and Horizontal Network Delivery Systems" (2016) 59 (2) *Canadian Public Administration* 224 p. 225.
[66] Gray, A. & Jenkins, B. "Codes of Accountability in the New Public Sector" (1993) 6(3) *Accounting, Auditing & Accountability Journal* 52 p. 55.
[67] Lewis, J. O'Flynn, J. & Sullivan, H. "Accountability: To Whom, in Relation to What, and Why?" (2014) 73(4) *Australian Journal of Public Administration* 401 p. 402.
[68] Ibid p. 403.
[69] Moore, M. "The (Neglected) Value of Board Accountability in Corporate Governance" (2015) 9(1) *Law & Financial Markets Review* 10 p. 10.

In this regard, this remains an underlying requirement for SOEs to operate effectively and efficiently and how is will be achieved is linked to board accountability.

(5) Historical Evolution of Corporate Governance Standards in Ireland

Setting a historical development of a corporate governance framework Ireland has a history of being proactive in providing guidelines to be followed by State bodies. In 1992 *State Body Guidelines* were issued.[70] The guidelines were well received to give State bodies direction on acceptable practices and they became the foundation for what would later become the most significant governance code for State bodies.[71] Core provisions of the report dealt with directors and their obligations to adhere to codes of conduct and to avoid conflicts of interest.[72] The *Code of Practice for SOEs*[73] introduced in 2001 and later updated in 2009 and most recently in 2016 is the guidelines used for governance of SOEs.

The 2001 guidelines differentiated from previous guidelines by distinguishing principles on the basis that State bodies had an obligation to implement the Code's provisions, furthermore ethics were introduced as part of the 2001 guidelines and there was a stronger emphasis on the role of the relevant Minister.[74] The 2001 guidelines were revised in 2009 as it became clear it was time for Code for State bodies to be updated. This was influenced by the *Mullarkey Report* which aimed to address governance and accountability issues of public bodies.[75] The Report found:

"There is a need for clarity in relation to responsibility and accountability, and the constitutional and legal basis for same, in both existing and new State entities.
The requirement that the existing system provide for an increasing focus on the performance of the Secretary General/Accounting Officer.

[70] The Department of Finance *Guidelines for State Bodies* (Dublin 1992).
[71] "Guidelines for State Bodies" Dáil Éireann Dáil Debates Volume 423 13 October 1992.
[72] "Written Answers Semi-State Bodies" Dáil Éireann Debate Volume 419 05 May 1992.
[73] The Department of Finance *The Code of Practice for the Governance of State Bodies* (Dublin 2009).
[74] Department of Finance *Code of Practice for the Governance of State Bodies* (Dublin 2001).
[75] *Mullarkey Report - Report of the Working Group on the Accountability of Secretaries General and Accounting Officers* Department of Finance 2002.

The importance of having management and governance systems balanced to support constructive review and continuous improvement while having the capacity to deal with serious issues as they arise."[76]

The *Code of Best Practice for State-owned Bodies* 2009 had several updates on the 2001 Code which included the boards' collective responsibility for promoting the success of the SOE:

"The Board is collectively responsible for promoting the success of the State body by leading and directing the Body's activities. It should provide strategic guidance to the State body, and monitor the activities and effectiveness of management. Board members should act on a fully informed basis, in good faith, with due diligence and care, and in the best interest of the State body, subject to the objectives set by Government."[77]

Other updated recommendations include the requirement for the role of the chief executive and chairperson not to be combined.[78] The requirement to introduce risk management policy was firstly introduced in the 2009 report.[79]

Having governance guidelines in place on Irish State bodies as far back as 1992 gives recognition to the unique position they have in the market, with the Department of Finance taking an active role in providing a corporate governance framework. However, an independent review of the Department of Finance in the Wright Report criticises the performance of the Department of Finance for its oversight of State bodies, including the Central Bank.[80]

[76] Ibid at principle 4.
[77] Supra note 73 principle 2.
[78] Ibid principle 2.16.
[79] "*An effective risk management system identifies and assesses risk, decides on appropriate responses and then provides assurance that the chosen responses are effective"* The Department of Finance *The Code of Practice for the Governance of State Bodies* (Dublin 2009) principle 8.
[80] Wright, R. "Strengthening the Capacity of the Department of Finance" "Wright Report" 2010 p. 30.

C. CENTRAL RESEARCH QUESTION AND THESIS STRUCTURE

(1) Central Research Question

The aim of this thesis is to examine board accountability in corporate governance standards for SOEs. For the purposes of this thesis accountability is concerned with the wider context of public sector governance, to provide goals to improve performance. It is based on agreed goal objectives, rather than process implementation of an inflexible "one model fits all." It is based on a more open fluid system that is driven by incentives that rewards efficiency and transparency. This should provide a better understanding of board performance, knowing the why and how systems are implemented is important. A system should encourage reflection to improve performance management, in recognition of the role of board accountability as central in supervisory capacity of SOEs.

Corporate governance standards are relied on as a method to ensure organisations are run effectively and efficiently. The starting assumption is that corporate governance should provide a value contribution to an organisation to ensure certain standards are upheld. However, given the challenges that exist, the value of a governance framework is questioned when organisations are exposed for not implementing governance standards, which raises doubt as to what level of safeguarding governance standards can provide. Board members of SOEs should not have freedom to exercise their duties without having to be held to account for the actions and omissions. This raises the question of how a *Code of Practice for State Bodies* can make adequate provisions that foster a strong sense of accountability.

While there is a substantial amount of global literature on corporate governance, the area of board accountability within SOEs has not been adequately addressed in an Irish context. The IPA published work on corporate governance relating to SOEs, where MacCarthaigh gave an extensive overview of some of the governance issues surrounding commercial SOEs in Ireland.[81] Research on corporate governance standards is beginning to increase in

[81] MacCarthaigh, M. Committee for Public Management Research Report 9 *The Corporate Governance of Commercial State-Owned Enterprises in Ireland* (Institute of Public Administration Dublin 2009). See also

more recent years in Ireland.[82] The area of SOEs in Ireland has always been a subject of research for the IPA and Forfás as they have published work on SOEs dealing with role and aspects of SOEs in Ireland.[83] This thesis will build upon this research by investigating the board accountability dimension within corporate governance for SOEs, as there has not been a comprehensive discussion of this issue in relation to Ireland within academic literature.

This research is timely as Ireland the *Code of Practice for State Bodies* has most recently been updated in September 2016 which for the first time includes extensive provisions dealing with accountability.[84] This recognises the importance of having strong accountability framework in place for SOEs.

The Wright report highlighted the shortcoming of the Department of Finance in their monitoring role of State bodies. [85] This implies a lack of leadership and direction as there wasn't a robust engagement with government policy:

"the Department of Finance should have done more to avoid this outcome. It did provide warnings on pro-cyclical fiscal policy and expressed concern about the risks of an overheated construction sector. However, it should have adapted its advice in tone and urgency after a number of years of fiscal complacency. It should have been more sensitive to and provided specific advice on broader macroeconomic risks. And it should have shown more initiative in making these points and in its advice on the construction sector, and tax policy generally."[86]

MacCarthaigh, M. "Managing State-owned Enterprises in an Age of Crisis" (2010) *UCD Geary Institute Discussion Paper Series*.
Further research by the IPA also includes McGauran, A.M., Verhoest, K. & Humphreys, P. Committee for Public Management Research Report No. 6 *The Corporate Governance of Agencies in Ireland: Non-Commercial National Agencies* (Institute of Public Administration Dublin 2005).
[82] See Keane, R. & O'Neill, A. (eds) *Corporate Governance and Regulation* (Round Hall Publishing Dublin 2009).
[83] Forfás *The Role of State Owned Enterprises: Providing Infrastructure and Supporting Economic Recovery* (Dublin 2010). FitzGerald, G. *State-Sponsored Bodies* (Institute of Public Administration, Ireland, 1963). See also, Institute of Public Administration Ireland *The Structural Characteristics of State-Sponsored Bodies* (IPA Dublin 1980).
[84] Supra note 10 at principle 8.
[85] Supra note 92 p. 30.
[86] Ibid p. 6.

This indicates the department was insufficiently proactive in its reaction to factors which resulted in the recent financial crisis.

Based on the foregoing, this thesis aims to evaluate how corporate governance standards were inadequate as evidenced by the FÁS saga and this thesis will explore how this arose. The central research question will address the role of accountability in corporate governance standards in SOEs, focusing on existing governance framework and analysing how the *Code of Practice for State Bodies* implemented in 2016 improved accountability and the limitations to it.

Corporate governance standards for SOEs are based on standards set for listed companies, however, as the repercussions for SOEs are not the same for listed companies, this thesis will outline what additional requirements are necessary for SOEs.

This research differs from prior research by focusing specifically on board accountability within the context of Irish SOEs, examining the related accountability implications and recommending best practice principles.

(2) Thesis Outline and Structure

A key objective of this research is to provide a framework which takes steps to increase board accountability within SOEs. This chapter provides an examination of the definition of SOEs and why both commercial and non-commercial SOEs will be included in the thesis. The remainder of this chapter will also assess key factors impacting accountability in SOEs, namely Agency and Stakeholder theory. Chapter 2 will outline what is happening with board accountability from an international perspective and the aim of this is to identify successful elements that can be used when drafting a best practice framework for accountability. This chapter will also provide a contextual setting of SOEs in Ireland.

Chapter 3 will focus on the regulatory model of corporate governance standards. Corporate governance standards differ from hard law when implemented on a quasi-legal basis. A

soft law approach is often favoured for governance standards due to the flexibility offered by soft law. The consequence of this, however, is it is driven by self-motivation for engagement with standards. This may not be considered a main priority or there may be application of codes at a minimum standard. A popular principle included in corporate governance standards is the principle of 'comply or explain' which gives governance codes a unique status as not all provisions of codes need to be implemented where an explanation for non-compliance is provided. It is vital to examine both the soft law approach taken for corporate governance standards and to investigate the 'comply or explain' principle. To appreciate the role and value governance standards bring it is necessary to evaluate the content of the *Code of Practice for State Bodies* 2016 and its predecessor 2009 code and so chapter 3 examines the substantive content of existing governance provisions for SOEs.

Chapter 4 addresses internal and external mechanisms of accountability for SOEs. One of the most substantial issues for governance of SOEs is how accountability and transparency is incorporated into a governance framework and so the issues surrounding this will be examined. As it is the board who implement governance their role in engagement with standards will be reviewed.

SOEs should ensure they are acting in the best interests of stakeholders. But it can be difficult to determine which stakeholders take priority in the context of SOEs, making it challenging for SOEs to act in the best interest of stakeholders and so the role of stakeholders will be examined in chapter 4.

Chapter 5 examines the consequences when SOEs are mismanaged and waste public resources. This chapter looks at one of the biggest corporate governance scandals of SOEs in this country to date, with the focus on the FÁS saga.[87] The FÁS scandal in Ireland is perhaps one of the more interesting recent cases of an examination of corporate governance standards in an SOE. While the board of FÁS claimed to follow corporate governance standards, the practices exposed in the organisation throws into question what

[87] See further Comptroller and Auditor General *Special Report Internal Control and Governance in FÁS* (Dublin 2009). Byrne "Public Pays High Price for Financial Mismanagement" *The Irish Times* 2 December 2008. Keena "FÁS Official Gives His Side of The Story to PAC" *The Irish Times* 9 January 2009. Keena "High-Flyers at FÁS Are Brought Down To Earth" *The Irish Times* 26 November 2008.

it means to implement corporate governance principles. This chapter will take an account of the events of FÁS and see how they fit with the standards set by the *Code of Practice for the Governance of State Bodies* 2001.[88]

Examining FÁS's governance practices should give an insight into the operation of the governance Code with SOEs and how they operate. This chapter addresses the question whether the governance code for State Bodies 2001 in place at that time was ignored or whether it was inadequate to prevent the FÁS scandal.

The contribution this thesis makes will also be highlighted in chapter 6 where a best practice framework of accountability for corporate governance for SOEs is drafted. By comparing existing governance standards to what a best practice framework this will attempt to highlight what would be expected from a robust set of corporate governance standards. This will draw on information from previous chapters by highlighting weakness in governance standards currently in place for SOEs and comparing how governance principle operate in different jurisdictions.

Therefore, based on the extensive analysis of corporate governance standards this thesis will produce a working model for a framework of accountability for corporate governance standards for SOEs in Ireland.

Chapter 7 is the concluding chapter and outlines the final reasons for the recommendations made for an accountability framework for SOEs.

[88] Supra note 73.

(3) Research Methodology

The principal methodology employed in this thesis is doctrinal research which enables an in-depth analysis of governance provisions which have been utilised to date both nationally and internationally. This thesis will consult primary and secondary sources of law including statutory material, case law, academic commentary and reports. It will look at current and historical information that forms corporate governance. An examination of the literature highlights current awareness on corporate governance in the context of academic articles, journals and legal research websites. Freedom of Information requests were also made for information on board meetings of Irish SOEs to the Minister to ascertain how governance has been implemented. FOI requests were made to *CIÉ*, Irish Rail and SOLAS, which became the replacement body when FÁS was dissolved.[89] This assisted in the identification of key influential factors for accountability within SOEs. This thesis was conducted through library based research and time was spent in the IPA library. A request to discuss the FÁS scandal was made to Shane Ross and Nick Webb who were the key reporters who broke the FÁS story but a response was not received. This research will examine if corporate governance provisions fell short of their objectives as the corporate scandal of excessive spending in FÁS suggests that there was little engagement with standards.

This thesis is interdisciplinary, with a wider context including social, historical, economic and political factors that stem from this research. Corporate governance covers areas such as management, law and regulation. Legal issues cannot be studied in isolation as they have a major impact on the society from which they arise. Thus, this thesis has sociological elements. Legal rules are heavily influenced and are a reaction from the society from which they emerge and so this will impact corporate governance framework.

[89] See Appendix for FOI responses.

D. ASSESSING KEY FACTORS WHICH IMPACT ON BOARD ACCOUNTABILITY IN SOES

Two key mechanisms which impact on the structure of accountability of SOEs centre on Agency theory and Stakeholder theory.

(1) Agency Theory

Agency theory argues that the managers may behave opportunistically to maximise their own welfare.[90] The "moral hazard conflict"[91] leaves management in a position where decisions they make should not reflect self-interest but choices that are in the best interest of the company must prevail. This dilemma, later coined the "Agency theory" by Jensen and Meckling.[92] Agency theory is based on the relationship of the principal and the agent, who are in the context of corporate governance the shareholder and the company's managers respectively. Agency theory denotes how managers of a company may be tempted by economic self-interest and therefore not act in the best interest of the agent.[93] There is a presumed expectation that a principal will at all times act in the best interests of the agent, but who is to interpret what is best for the company? This indicates that acting in the best interests of the company is subjective and there will not always be an alignment of interests. When shareholders invest in a company management will take risks on their behalf with an investment, but it is often only when the risks don't pay off that management is considered not to have acted in the best interest of the company.

Corporate governance standards can provide a solution to this problem as separation of ownership and control is well-recognised in corporate governance theory and standards

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[90] Meckling, J. "Theory of the Firm: Managerial Behaviour, Agency Costs and Ownership Structure" (1976) 3 *Journal of Financial Economics* 305.
[91] Bitler, M., Moskowitz, T. & Vissing-Jorgensen, T. "Testing Agency Theory with Entrepreneur Effort and Wealth" (2005) 2 *The Journal of Finance* p. 539.
[92] Supra note 90.
[93] Bryant, P. & Davis, C. describe the agency theory as "agents of an organization are responsible for conducting business in the interest of the organization, and given that an agent's own self-interests will never align completely with the interests of the organisation, agents of an organisation will sometimes experience conflicts of interest when conducting business on behalf of the organization."
therefore the organisation has to control self-interested behaviour. Bryant, P. & Davis, C. "Regulated Change Effects on Boards of Directors: A Look At Agency Theory And Resource Dependency Theory" (2012) 11(2) *Academy of Strategic Management Journal* 1 p. 3.

define how corporate rights and duties are managed within an enterprise; it gives solutions to decision-making processes and how control is distributed.[94] The underlying principle of corporate governance is that problems can arise in entities where there is separation between ownership and control.[95] Investors have no input into the daily decisions of the company and because of this there is a fear that management will not act with the same vigilance if the investment into the company were their own. Berle and Means point out that corporate executives have almost complete discretion in management.[96] Smith claimed due to this separation of control it was necessary to impose safeguards that ensures those in charge are accountable to investors.[97]

(2) Institutional investors

The role institutional investors play in corporate governance standards cannot be underestimated as they hold significant power. Institutional investors include pension funds, insurance companies, hedge funds and private equity funds. Their power arises as they are going to monitor firms they have funded making them key shareholders.[98] Institutional investors can affect management's actions through their ownership and this will reduce the agency problems.[99] This is conducive for directors to act in the best interests of shareholders as institutional investors have an incentive to monitor management.[100] Intuitional investors will expect management to conform to best practice.[101] In the UK the Stewardship Code actively encourages institutional investors to

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[94] Dallago, B. & Iwasaki, I. *Corporate Restructuring and Governance in Transition Economics* (Palgrave Macmillan New York 2007) p. 15.
[95] Supra note 90.
[96] Berle, A. & Means, G. *The Modern Corporation and Private Property* (Macmillan New York 1932) p. 139.
[97] "The directors of such companies being the managers rather of other people's money than of their own, it cannot well be expected that they should watch over it with the same anxious vigilance with which the partners in a private copartnery frequently watch over their own. Therefore the Separation of Ownership and Control must always prevail, more or less, in the management of the affairs of such a company." Smith, A. *The Wealth of Nations* (Strahan and Cadell Publishing London 1976) Book 5 Chapter 1 Part 3 Article 1.
[98] See Jackson, A. "Towards a Mutual Understanding of Objectives?" Attitudes of Institutional Investors and Listed Companies to Corporate Governance Reform" (2001) 9 *Corporate Governance: An International Review* 196.
[99] Noe, T. "Institutional Activism and Financial Market Structure" (2002) 15 *Review of Financial Studies* 15 289 p. 289.
[100] Bathala, B. Moon, K. & Rao R. "Managerial Ownership, Debt Policy, and the Impact of Institutional Holdings: An Agency Perspective" (1994) 23 (3) *Financial Management* 38 p. 38.
[101] Rashid, A. "Largest Blockholding and Firm Performance: Evidence from an Emerging Economy" (2011) 65 *International Research Journal of Finance and Economics* 25 p. 25.

enhance communication with companies.[102] The principle of comply or explain is used by boards and listed companies and choosing not to comply may result in shareholders, particularly institutional investors not investing in a company.[103] It is the power expertise and incentives that make institutional investors efficient monitors:

"the efficient monitoring hypothesis contends that the larger the shareholding of the institutional shareholder the more efficient the monitoring exerted by that shareholder and the higher the likelihood of dissident success"[104]

Within SOEs the State has a dual role as shareholder and regulator and therefore can control the levels of disclosure that is released to the public. Institutional investor should help minimise the agency problem as if conflicts of interest arise between principals and agent a disclosure of information will leave to a reduction of such conflicts. By accepting that the groups of interests expands in the context of SOEs should address the agency problem. Stakeholders have the potential to drive corporate standards but this has not played as much a role as it might to date in Ireland in the SOE sector.

(i) The Public Private Partnership (PPP)

Institutional investors invest can invest in SOEs through Public Private Partnerships (PPP). SOEs can be expensive entities for the State. One way of alleviating the financial burden on the State is to enter PPPs.[105] PPPs are relevant to SOEs as they bridge the gap between the financial burden that SOEs place on the State and privatisation. PPP, can provide an interim solution before the State decides to privatise an SOE. PPP was quite interestingly referred to as 'allowing each sector to do what they do best.'[106] The premise of PPP is to allow the private sector to produce goods and services in a more efficient and economical

[102] Financial Reporting Council (UK) *The UK Stewardship Code* (2012) p. 1.
[103] Ibid.
[104] Salehi, Hematfar & Heydari "A Study of the Relationship between Institutional Investors and Corporate Value: Empirical Evidence of Iran" (2011) 8(1) *Middle-East Journal of Scientific Research* 72 p. 72.
[105] *The State Authorities (Public Private Partnership Arrangements) Act* 2002 enables State bodies to enter into partnership with the private sector.
[106] Scally, J. "Public Private Partnerships in Ireland: An Overview" (2004) *Central Bank Publications Quarterly Bulletin* 79 p. 80.

manner than if it were provided by the public sector.[107] The private sector builds and will remain responsible for the long term maintenance of the infrastructure but the public sector will remain to have outright ownership. Traditionally the PPP method is used in building infrastructure such as roads[108] and hospitals but now it has also been incorporated into the public finance and accounting practice.[109]

The PPP Programme has evolved with required changes by the government and more recently it is used as a mechanism to create jobs. Job creation will come more as an indirect consequence of the Phase 1 PPP Programme by the government.[110] The programme will consist of building and remodeling schools, courthouses and building of roads, and so the job creation is aimed at those who work in the construction service.[111] It is envisaged that the main source of the private funding will come from domestic banks, EIB and the National Pension Reserve Fund.[112]

The PPP method is a good means of utilising the private sector so that services and infrastructures can be provided in a more efficient and cost effective, while allowing the State to retain ownership, and be a shareholder, despite the input from the private sector. The ability of a PPP to be used in sectors where a government can generate funding from the private sector is also a key advantage of the method. In addition to this, another attractive feature of a PPP is it alleviates the financial burden that falls on the public sector as the private sector will be a large source of funding. The consequence of this is that the private sector will take its share in profits.

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[107] Ibid p. 79.
See further Landow, P. & Ebdon, C. "Public-Private Partnerships, Public Authorities, and Democratic Governance" (2012) 35(4) *Public Performance & Management Review* 727.
[108] In 1999 the government announced the PPP with the National Roads Authority which raised 1.27bn (23%) of the funding for the following projects;
the N25 Waterford By-Pass, incorporating a major river crossing;
the Limerick Southern Ring Road Phase 2, including 10km of dual carriageway and a major crossing of the Shannon estuary, and the construction of a second bridge at West-Link on the M50 in Dublin.
See National Roads Authority at http://www.nra.ie/PublicPrivatePartnership/ last accessed August 2017.
[109] Supra note 106.
[110] Speech by Minister Brendan Howlin T.D. *Government Infrastructure Stimulus* 17 July 2012. Available at http://per.gov.ie/2012/07/17/speech-by-minister-brendan-howlin-td-government-infrastructure-stimulus/ last accessed August 2017.
[111] Ibid.
[112] Ibid.

(3) Directors Duties to act in the best interests of the company

In addressing the issue of acting in the best interest of the company directors are bound fiduciary duties. The *Code of Practice for State Bodies* 2016 takes inspiration from the *Companies Act* 2014, which for the first time puts directors' fiduciary duties on a legislative basis. In the UK directors owe duties to:

- Act within the powers conferred by the company's constitution.
- Promote the success of the company.
- Exercise independent judgement.
- Exercise reasonable care, skill and diligence.
- Avoid conflicts of interest.
- Not accept benefits from third parties.
- Declare interests in proposed transactions or arrangements.[113]

These duties reflect similar duties that were implemented in Ireland in the *Companies Act* 2014,[114] with an overriding obligation to act in what they consider to be the best interests of the company. The courts also recognise the fiduciary duties that are owed by directors, as they undertake to act on behalf of another person which gives rise to a relationship of trust and confidence.[115] The duty of directors to act in the best interests of the company is set out in the cases of *Re Smith & Fawcett Ltd*[116] and *Clark v Workman*[117] and these cases indicate that compliance is subjectively tested. It was considered that provided directors acted in good faith they would not be found negligent for failures of misjudgement. This allows for directors to use their discretion in the performance of their duties. MacCann pointed out that this is a requirement to act in the best interests of the company and no individual duty is owed to any particular shareholder or employee.[118] However, MacCann

[113] *Companies Act UK* 2006 Section 170-177.
[114] *Companies Act* 2014 Section 228 (1) (a).
[115] *Bristol and West Building Society v Mothew* [1998] Ch1.
[116] [1942] 1 All ER 452 p. 543.
[117] [1920] 1 IR 107 p. 113.
[118] MacCann, L. "Directors' Duties: To Whom Are They Owed?" (1991) 9 *Irish Law Times* 3 p. 3.

qualifies this statement by drawing attention to the case of *Percival v Wright*[119] where it was highlighted that "a director is not *per se* agent for the shareholder, but if he should undertake to act as such agent, then a fiduciary relationship is established between them."[120] The duty of directors to act in the best interests of the company means their primary focus should be to the company but for SOEs this should also include a duty to act in the public interest.

Notably the *Code of Practice for State Bodies* 2016 was the first time there were provisions listing fiduciary duties of directors.[121] This ensures that SOEs are within the remit of the Companies Act 2014 are bound by fiduciary duties. The Code lists the fiduciary duties being owed as follows:

1. "to act in good faith in what the board member considers to be the interest of the company;
2. to act honestly and responsibly in relation to the conduct of the affairs of the company;
3. to act in accordance with the company's constitution and exercise his or her powers only for the purposes allowed by law;
4. not to benefit from or use the company's property, information or opportunities for his or her own or anyone else's benefit unless the company's constitution permits it or a resolution is passed in a general meeting;
5. not to agree to restrict the board member's power to exercise an independent judgment unless this is expressly permitted by the company's constitution;
6. to avoid any conflict between the board member's duties to the company and the board member's other interests unless the board member is released from his or her duty to the company in relation to the matter concerned;
7. to exercise the care, skill and diligence which would be reasonably expected of a person in the same position with similar knowledge and experience as a board member. A board member may be held liable for any loss resulting from their negligent behaviour; and

[119] [1902] 2 *Ch* 421.
[120] Ibid.
[121] Supra note 10 at provision 3.1.

8. to have regard to interests of the company's members."[122]

SOEs are by their definition bound by laws of the State. SOEs take the form of a limited liability company where the State directly holds a majority shareholding. This infers SOEs are bound by the many of the laws and regulations that private companies are bound by. The regulatory framework for SOEs encompasses the recognised laws, codes and best practice guidelines that are applicable. All incorporated entities must comply with the *Companies Act*, which are enforced by the Office of the Director of Corporate Enforcement. SOEs are bound by the *Companies Act* 2014 (as amended) which provides general duties to directors:

1. Directors must ensure compliance with the Companies Act and the various tax Acts.
2. Directors must ensure that the company secretary is suitably qualified.
3. Directors must acknowledge the existence of their duties by signing a declaration to that effect.
4. Directors must take into account the interests of the members of the company and have regard to the interests of the employees.
5. Restrictions on loans, quasi loans, credit transactions and certain guarantees and security exist for directors, but will be subject to the new summary approval procedure.
6. Directors must disclose any interests in contracts made by the company.
7. Directors must notify the company of any interests in shares in the company, its parent or subsidiary but no obligation arises if the shares held represent less than 1% of the share capital of the company or the shares do not have voting rights.[123]

In the context of SOEs the issue arises to whom directors' duties are owed, the alignment of competing interests between the board and citizens is problematic. A board of directors should be accountable to shareholders and management should be accountable to the board. Board members of SOEs are accountable to government Ministers but Minsters also have power over SOEs results in a balancing requirement for independence for SOEs. This makes separation of ownership and control more challenging in the context of SOEs.

[122] Ibid provision 3.1.
[123] *Companies Act* (as amended) 2014 Part 5.

(4) Government Involvement in SOEs

SOEs must have protective measures to ensure they are free from undue political interference. The board of directors whilst responsible to the overseeing Ministers should have the freedom to exercise its duties independently. However, difficulties emerge when Ministers are not informed of all the key affairs within SOEs and as a result what is reported to the public may not be an accurate picture and so the separation of ownership and control model may come under scrutiny. For example, the then Minister for Transport Noel Dempsey was not aware of the malpractices of spending and procurement within CIÉ until details were exposed in the *Baker Tilly Ryan Glennon Report*.[124] Lemass had pointed out that it is difficult for Ministers to know what their level of involvement should be:

"The relationship between State boards and the Ministers who are responsible to the Dáil for their operations is not always very precisely defined and a great deal depends on the confidence which a Minister may have in the board or executives of a particular concern and on the readiness of a board to accept that the particular operations for which they are responsible should be kept in line, through the Minister as the co-ordinating authority, with the over-all development plans of the Government."[125]

From this approach it appears that it is up to the Minister to decide how much involvement they will have in the SOE. Andrews argues that a lack of defining the Ministers role may result in excessive autonomy for the SOEs:

"the Government should take power in the legislation to direct the companies on broad policy. This would obviate the very real danger to which the Minister refers of the companies beginning to think of themselves as autonomous entities, free to pursue the personal economic theories of members of the board."[126]

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[124] "Railway Procurement Processes" Dáil Eireann Debate Volume 697 No. 3 9 December 2009. See further "Departmental Investigations" Dáil Eireann Debate Volume 730 No. 4 20 April 2011.
[125] Supra note 49 p. 288.
[126] Andrews "The Role of the State-Sponsored Bodies in the Economy" (1959) *Administration* IPA 295 p. 296.

It is possible that the Minister may not scrutinise the activities of the enterprise so as maximise their output. For example, if the financial statements show SOEs are not increasing profits there is no requirement for the Minister to investigate the poor performance further. The appropriate relationship held between the board and the government may also be cause for examination.[127] Debates arise as to what level of input and political control the government should have in public enterprises.[128] Political involvement in enterprise does not come without criticism. How then should these SOEs be viewed? Is the involvement of the State political or business? In New Zealand *the State Senior Act* 1998 set out what is expected of government agencies:

"to promote efficiency in the State services and the agencies; to ensure the responsible management of the State services; and to maintain appropriate standards of integrity and conduct among employees in the State services and other agencies."[129]

Hastings argues, in more recent years enterprises where the State has a stake do not get favourable treatment over enterprises in the private sector and in fact for commercial SOEs the government puts more pressure for increased profitability.[130] Many enterprises are now competing in an environment that is very different from the environment they were founded in and, in addition to this, some State enterprises have been deregulated and privatised. The 1990's was a time where many SOEs were privatised. The sale of Eircom in 1999 removed the State's monopoly on the telecommunications market, and other examples of privatisation of SOEs included Greencore Group plc and Irish Life Assurance plc. MacCarthaigh describes the privatisation of the 1980's and 1990's as a desire to sell off inefficient SOEs.[131]

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[127] Barberis, P. & May, T. *Government, Industry and Political Economy* (OUP Philadelphia 1993) p. 175.
[128] It is clear that this has being a continuing problem for SOEs;
"The question of control is a vexed one as there are diametrically opposed views—one to the effect that a semi-State body should be absolutely independent on policy and management; the other view being that they are virtually departments of State working under direction as to policy."
Beddy, J.P. "The Role of the State-Sponsored Bodies in the Economy" (1959) *Administration* IPA 300 at 301.
[129] *State Senior Act* 1998 New Zealand section 2.
[130] Hastings, T. *Politics, Management and Industrial Relations: Semi-State Companies and the Challenges of Marketization* (Blackhall Publishing Dublin 2003) p. 11.
[131] MacCarthaigh, M. "Managing State-owned Enterprises in an Age of Crisis: an Analysis of Irish Experience" (2011) 32(3) *Policy Studies* 215 p. 216.

In order for SOEs to be considered reputable entities and to appreciate the value that the State can bring by being involved in providing services it is necessary for them to ensure they follow good corporate governance standards and so this thesis will address this relationship and interaction of corporate governance principles and SOEs. It is often suggested that governance should be construed in a way that the best interests of the shareholders are protected. This is one of the views taken by the Financial Reporting Council:

"Good corporate governance should aim to better a company's overall performance by helping the board discharge its duties in the interests of the shareholders."[132]

While this can be achieved by applying various best practice codes to all aspects of the company's governance the same rules do not apply for SOEs. The reason for this is that when a government sets up an SOE, it is for the most part intended to benefit and protect the welfare of the citizens of the country. Therefore, the role of shareholders has dramatically changed between that of SOEs and listed companies. While governments may seek financial reward through SOEs, it is more likely that they will require that the interests of stakeholders are taken into account. Difficulties arise when stakeholders are not identifiable or which groups of stakeholders should be prioritised and if this is a decision to be made by the board or government. Stakeholders have been defined as "any group or individual who can is or affected by the achievement of the organisation's objectives."[133] But who should decide how or which stakeholders are prioritised? Freeman's Stakeholder theory is premised on this idea that corporations should not focus solely on profit maximisation but to have regard for other stakeholder groups that the corporation is associated with and balance the competing interests.[134] This theory developed with private companies in mind as the effect of actions of the shareholders on stakeholders could not be underestimated. Therefore, it will be examined how Stakeholder theory fits in for SOEs and how stakeholders should be identified and how their interests should be protected. Due

[132] Financial Reporting Council *The Combined Code on Corporate Governance* (London 2008).
[133] Freeman, E. *Strategic Management: A Stakeholder Approach* (Boston Pitman 1984) p. 46.
[134] Ibid.

to the involvement the government has in SOEs the government should lead by example and set a high standard of implementing corporate governance standards.

E. THE POSITION OF STAKEHOLDERS

Stakeholders have a significant role in an accountability model for SOEs as investment from the State into SOEs is generally for the benefit of stakeholders and protecting their interests should be ensured. Acting in the interests of stakeholders shifts management's focus beyond the traditional primary role of goal profit maximisation, to include the interests of other stakeholder groups that are affiliated with SOEs. Therefore, it will be necessary to identify stakeholders and how they should be prioritised.

(1) Stakeholder Theory

Freeman was one of the instigators of ensuring the interests of stakeholders were considered through Stakeholder theory.[135] He defined stakeholders as "any group or individual who can affect or is affected by the achievement of the organisation's objectives."[136] The underlying basis of Freeman's theory is that ethics and economics can be separated.[137] Ethics have been described as obligations that arise when decisions made by the firm affect other people.[138] Freeman considers separation of ethics and economics is necessary as moral obligations to stakeholders cannot be ignored simply because they do not fit into the firms' economic goals.[139] Engaging Stakeholder theory requires managers to balance the ethical prerequisite of the principle of fairness to act in the best interests of those affected by the firm but also their duty to shareholders to maximise profits.

Critics of Stakeholder theory disagree with Freeman and argue that separation of ethics and economics is a fatal flaw of his theory. Berman discredits Freeman's theory as he argues ethics and economics cannot be easily separated as even when a firm makes ethical

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[135] Ibid.
[136] Ibid p. 46.
[137] Freeman, E. Wicks, A. & Parmar, B. "Stakeholder Theory and the Corporate Objective Revisited" (2004) 15(3) *Organization Science* 364 p. 364.
[138] Berman, S., Wicks, A., Kotha, S. & Jones, T. "Does Stakeholder Orientation Matter? The Relationship between Stakeholder Management Models and Firm Financial Performance" (1999) 42(5) *Academy of Management Journal* 488 p. 493.
[139] Supra note 137.

decisions this is likely to improve the firm's reputation which can result in providing an organisation with economic benefits.[140] Harrison and Wicks recognise it is difficult to implement Stakeholder theory as what is considered value is often affiliated with improving economic gain.[141] Sternberg appreciates that there are good features of 'stakeholding' which include people are more likely to take an interest in an organisation whether they have an interest be it financial or otherwise.[142] However, Sternberg believes that Stakeholder theory is flawed and will not lead to good governance. He argues, if an organisation is operating in the interests of stakeholders the substantive objectives of the organisation may become second place and he also points out what counts as benefiting stakeholders is ambiguous and so it is a difficult requirement to fulfil.

However, Stakeholder theory is important in governance of SOEs as it is necessary for the organisation to add value to stakeholders. SOEs may find it easier to implement Stakeholder theory as separation from economics and ethics may be achieved more easily as SOEs are unlikely to have profit maximisation as their primary or sole objective. Additionally, ethics has a role in governance for SOEs to ensure a board actions are in line with protecting stakeholders' interests.

Freeman claims that managers can engage with Stakeholder theory by asking two questions, firstly what is the purpose of the firm and secondly what responsibility do managers have to stakeholders.[143] He suggests that the first question will give managers a shared sense of value of the aim of the firm, while the second question will allow managers the opportunity to assess the relationship they will have with their stakeholders.[144] He points out that Stakeholder theory will benefit the company overall as he considers that

[140] Supra note 138.
[141] Harrison, J. & Wicks, A. Stakeholder Theory, Value, and Firm Performance (2013) 23(1) Business Ethics Quarterly 97 p. 98.
[142] Sternberg, E. "The Stakeholder Concept: A Mistaken Doctrine" (1999) *Foundations for Business Responsibilities* 1 p. 11.
[143] Freeman, E. Wicks, A. & Parmar, B. "Stakeholder Theory and the Corporate Objective Revisited" (2004) 15(3) *Organization Science* 364 p. 364. See further Spurgin, E. "Do Shareholders Have Obligations to Stakeholders?" (2001) 33(4) *Journal of Business Ethics* 287 p. 296.
[144] Supra note 137 p. 364.

economic value is created where people voluntary come together to improve everyone's circumstances.[145]

It appears that Freeman bases his theory on two assumptions. Firstly, to benefit as a stakeholder you must have a role or involvement with the firm and this will not be relevant for SOEs as often stakeholders will have little association with SOEs and have no motivation for associating with SOEs. The second assumption is based on stakeholders being aware of their position in proximity to SOEs and that they can benefit from the firm. However, identifying stakeholders is a difficult challenge.

(2) Identifying Stakeholders

In order for a board to protect the interests of stakeholders they must be able to identify stakeholders but there are significant challenges defining and identifying stakeholders. Stakeholders have been defined as "any group or individual who is or can be affected by the achievement of the organisation's objectives."[146] This indicates that this will include shareholders but will also include those who will not gain from the company's profits but, nonetheless, are affected by the actions of the company and therefore, are more likely to take an interest in the corporation if it will affect them. Therefore, stakeholders can include employees, customers, trade unions or even citizens who are in close proximity to a corporation. The *UK Companies Act* 2006 requires directors to act in the long term interest of members but to take into account other named constituencies.[147] This approach should be implemented into governance for Irish SOEs but to narrow the board's focus groups of stakeholders should be prioritised.

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[145] Ibid.

[146] Freeman, E. *Strategic Management: A Stakeholder Approach* (Boston Pitman Publishing 1984) p. 46. Zif, J. has highlighted the various groups of stakeholders as those who have an interest or an impact on the enterprises. Zif, J. "Managerial Strategic Behavior in State-Owned Enterprises - Business and Political Orientations" (1981) 27(11) *Management Science* 1326 p. 1328. Jansson has a broader definition of stakeholders and includes employees, creditors, suppliers, consumers and the community in which the firm is located as coming under the definition of stakeholders. Jansson, E. "The Stakeholder Model: The Influence of the Ownership and Governance Structures" (2005) 56(1) *Journal of Business Ethics* 1 p. 1.

[147] The *Companies Act* UK 2006 section 172.

Berman examines two schools of thought managers can use in assessing which stakeholders' interest to act in, known as the "strategic stakeholder model" and the "intrinsic stakeholder commitment model."[148] The former model is used where it is foreseen to improve the company's economic performance whereas the latter model is used where managers consider the firm has a moral obligation to the stakeholders.[149] Stakeholders can improve the firm's economic performance where decisions are made in the interest of stakeholders and can also achieve the firm's objectives.[150] However, this model is influenced by economic gain and so other methods of identifying stakeholders should be examined.

(3) Prioritising groups of Stakeholders

To narrow down the potential wide ambit of groups of stakeholders a popular approach has been to prioritise groups of stakeholders. Clarkson describes this division of stakeholders as primary and secondary stakeholders.[151] Primary stakeholders are those "without whose continuing participation the corporation cannot survive as a going concern" such as shareholders and investors, employees, customers and suppliers,[152] whereas secondary stakeholders are "those who influence or affect, or are influenced or affected by, the corporation, but they are not engaged in transactions with the corporation and are not essential for its survival."[153] Stakeholders who are given priority are identified as those with attributes to influence the firm, the legitimacy of the stakeholder's relationship with the firm, and the urgency of the stakeholder's claim on the firm.[154]

Affirming Clarkson's grouping of stakeholders Mallin agrees with a division of stakeholders, giving priority to those who claim a central position to those directly affected by the corporation which include employees, customers and providers of credit and those

[148] Supra note 138 p. 488.
[149] Ibid.
[150] Ibid p. 491.
[151] Clarkson, M. "A Stakeholder Framework for Analysing and Evaluating Corporate Social Performance" (1995) 20(1) *Academy of Management Review* 92.
[152] Ibid p. 106.
[153] Ibid p. 107.
[154] Lückerath-Rovers, M., Mijntje De Bos, A. "Code of Conduct for Non-Executive and Supervisory Directors" (2011) 100 (3) *Journal of Business Ethics* 465 p. 467.

who are removed enough only to be indirectly impacted by the enterprise but are nonetheless affected by it to include local communities, environmental group, government and interest groups.[155] An issue raised by Carney, Gedajlovic & Sur is the potential conflict between the various groups of stakeholders.[156] Such conflict arises with stakeholders who share a common fate but the different groups of stakeholders do not have the same capacity and motivation to achieve their goals.[157] To overcome stakeholder conflict Harrison and Wicks argue it would be useful for stakeholders to share similar goals and overlap interests so co-operation between stakeholders can be established.[158] However, if stakeholders are divided into primary and secondary stakeholder such co-operation may not be forthcoming.

It is questionable if the trend of prioritising groups of stakeholders is suitable for SOEs. Categorising stakeholders allows SOEs the freedom to keep the interests of dominant stakeholders a top priority and also implementing stakeholder interests will be easier for a board as there are a reduced number of classes of stakeholders to consider. This leaves the question as to which are primary stakeholders for SOEs? If directors are expected to act in the best interest of stakeholders this suggests primary stakeholders should be users of SOEs. This leaves employees, suppliers and the government as the shareholder as secondary stakeholders. However, this means that in satisfying the interests of prevalent stakeholders will be at the disadvantage of others. Additional 'mute' stakeholders such as the environment and 'absent' stakeholders, which are future generations, also have to be considered by SOEs.[159] While both categories have an important role to play in society, it is harder to categorise the importance of such category over more accepted conventional stakeholders as they are not a current human category.

In deciding how SOEs can act in the interests of its stakeholders an option offered by Harrison and Wicks takes a stakeholder utility approach to maximise value for

[155] Mallin, C. *Corporate Governance* (OUP New York 2007) p. 50.
[156] Carney, M., Gedajlovic E. & Sur, S. "Corporate Governance and Stakeholder Conflict" (2011) 15(3) *Journal of Management & Governance* 483.
[157] Ibid p. 485.
[158] Supra note 141 p. 102.
[159] Branco, M. & Rodrigues, L. "Positioning Stakeholder Theory within the Debate on Corporate Social Responsibility" (2007) 12(1) *Electronic Journal of Business Ethics and Organization Studies* 5 p. 7.

stakeholders. They outline how the board can ensure that the interests of stakeholders are maximised where:

"1) recognition that the purpose of a firm, and thus its performance, is based on the amount of value the firm provides to its stakeholders,
2) inclusion of both economic and non-economic factors that provide utility to stakeholders,
3) inclusion of measures for all of a firm's primary stakeholders,
4) recognition that different stakeholders are likely to value different things
5) measures should have the capacity to recognize a level of utility to stakeholders that exceeds mere satisfaction with the firm."160

The above guidelines are extensive but quite general and for a board to fulfil them would result in a high recognition of stakeholders. Eliminating the categorising of stakeholders should result in a more balanced approach with a board having to act in the interests of stakeholders as a whole rather than acting for the benefit of any one group.

[160] Supra note 141 p. 113.

F. CONCLUSION

Corporate governance standards have an important role in SOEs as they can prove to be an invaluable tool for a board of directors to achieve responsible management of entities but only where there is adequate governance standards are in place. State's involvement in the running of SOEs should be carried out by strictly adhering to corporate governance standards that balance the political involvement in business to ensure that SOEs are run effectively and in the best interests of society. Domestic standards are influenced by international codes. This is apparent from examining the OECD *Guidelines on Corporate Governance of State-Owned Enterprise*.[161] However, OECD guidelines are intended to be a foundation for countries to use when drafting their own governance standards and therefore, not all provisions will be included in national guidelines for State bodies.

Uncertainty brought by the financial downturn changed the way in which corporate governance standards are viewed. With a surge in an interest in public finances, it never has been more important that there is a revised set of standards to increase accountability. The weaknesses of standards are highlighted particularly where they fail to prevent corporate scandals. The penalties that arise from the failure to implement governance for private companies is not equivalent in companies where the State is providing the financial backing. Pulling funding from SOEs would not be a viable or realistic opinion for the government. But what should be the ramification when an enterprise does not comply with the wishes of the State? It is questionable whether there is enough control over enterprise where the State is the main shareholder. This may be the area that requires greater improvement as there does not appear to be meaningful repercussions for non-compliance with State requirements.

The following chapter focuses on the importance of SOEs in Irish society, their role in the Irish market and the chapter will also provide an international context for accountability within SOEs.

[161] Supra note 3.

CHAPTER 2:
A COMPARATIVE PERSPECTIVE ON BOARD ACCOUNTABILITY BETWEEN SOES IN IRELAND AND INTERNATIONALLY

A. INTRODUCTION

The complexity of board accountability is not unique to Irish SOEs and this chapter presents reasons why governance on board accountability is a significant issue internationally. The normative standards on board accountability are evolving as it is used as a tool for improving quality governance in SOEs. The move to increase board accountability is developing parallel to the demand for greater autonomy. Corporate governance is being implemented in line with New Public Management philosophy, which places emphasis on leadership principles and for cost efficiency of public services.[162] This provides a means for increasing board autonomy based on agreed principles but in exchange, State bodies must demonstrate they can achieve efficiency and value for money.

This chapter also reflects and compares major theoretical issues associated with governance for SOEs in Ireland. This includes examining fundamental issues, including definitions of governance and SOEs and key corporate governance principles relevant to strengthen board accountability. By setting a historical context for SOEs, this chapter provides analysis on how SOEs are established. This chapter outlines central governance issues for increasing board accountability, which should improve the relationship between principal and agent, and also increase transparency and provide monitoring mechanisms.

By providing a context for corporate governance for SOEs this chapter addresses three core issues;

- how board accountability of SOEs is evolving in Europe,
- the role of SOEs in Ireland, which address the key issues of corporate governance, and lastly,

[162] Laegreid, P. "Accountability and New Public Management" (2014) in Bovens, Goodin, & Schillemans (Eds.) *The Oxford Handbook of Public Accountability* Oxford University Press 324 p. 324.

- focusing on international comparators for Irish SOEs, encompassing both commercial activities and non-commercial functions which serve a social purpose.

The approach taken in the chapter is providing a setting to the factors that have a role that has resulted in the existing framework of corporate governance for SOEs.

B. BOARD ACCOUNTABILITY IN EUROPE

(1) Balancing Accountability with Board Autonomy

The State acting as owner of SOEs raises many issues in Europe as it does in Ireland due to the complex relationship between the State and SOEs.[163] Board performance is a topical issue in SOEs in Europe because accountability guides behaviour and stabilises expectations but there is a desire for increased board autonomy.[164] Boards shape governance mechanism of organisations as they are the link between shareholders and mangers. Boards make decisions which affect citizens, and every citizen has the right to demand greater accountability from boards to prevent misused power.

The OECD offered comprehensive guidance to governments to manage their responsibilities as acting "owners" of SOEs but shield them from undue political intrusion to allow for independent decision-making:

"Governments are encouraged to clearly evaluate and disclose the policy rationale that motivates state ownership of enterprises and subject these to recurrent review. The State is well advised to act as an informed, professional, and active owner and to allow SOEs full operational autonomy to achieve their defined objectives. The establishment of a central ownership entity, not responsible for regulating SOEs, can help clarify the responsibility for state ownership within the state administration. When SOEs undertake activities in the marketplace, it is important that they compete on a level playing field with private

[163] OECD "State-Owned Enterprise Governance Reform An Inventory of Recent Change" (2011) OECD Publishing Paris.
[164] Ibid p. 38.

enterprises, and that their commercial activities face market-consistent financing conditions;
Where SOEs are listed or otherwise have non-state investors among their owners, all shareholders should be treated equitably and have equal access to corporate information.

It is in the interest of both SOEs and their state owners to ensure that SOEs observe high standards of responsible business conduct, and that the state's expectations of this are clearly communicated and disclosed.
SOEs are encouraged to observe the same high standards of accounting, disclosure and audit as listed companies. Government accountability for state ownership can be reinforced through the publication of an annual aggregate report on the size and performance of the state's SOE portfolio.

SOE boards can most effectively carry out their functions of strategic guidance and monitoring of management when they have the authority and competence to do so. SOE boards are encouraged to act with integrity in the best interest of the SOE and to be held accountable for SOE performance."[165]

The OECD note how there is a growing trend for increased board autonomy with measures that shields SOEs from receiving instruction from government.[166] For example, in Estonia, the main opportunity for government to influence SOEs is at AGMs, and this allows a board to function more similarly to those of private companies.[167] The OECD recognises the demand of SOEs to perform better and to emulate private sector practices and this can be achieved by adjusting governance practices.[168]

Rentsch and Finger focus on the changing relationship between SOEs and the State, how this relationship is cyclical; firstly a stage of mutual dependence and co-operation,

[165] OECD "State-Owned Enterprise Governance Good Governance a facilitator for development" (2015) 5 OECD Publishing Paris p. 4.
[166] Supra note 163 p. 38.
[167] Supra note 163 p. 41.
[168] Frederick "Enhancing the Role of the Boards of Directors of State-Owned Enterprises" (2011) OECD Corporate Governance Working Papers, No. 2, OECD Publishing Paris p. 8.

progressing to an adversarial stage and finally evolving towards autonomy.[169] In a bid for autonomy, the wave of privatisation did not escape SOEs in Europe, with the State becoming less involved with the provision of goods and services.[170] This changes the relationship from the State being owner, to the State being regulator as SOEs become more autonomous. To deal with this transformation sector specific regulators were introduced in Europe for the State to protect their evolving corporate strategies.[171]

Flinders and Moon discuss categories of accountability based on principal agent approaches that are less applicable in unsettled organizational orders, in multi-level and webs of accountability, that also include diagonal or horizontal accountability relationships. They analyse a form of accountability that is required to address complex combinations of multiple, co-existing, contested and dynamic accountability relationships.[172] The importance of board accountability has been noted as essential to bring certainty so users of SOEs do not feel there is unpredictability and they are treated equally.[173]

(2) Increasing Board Autonomy through New Public Management (NPM)

A means of increasing board autonomy is through New Public Management (NPM). A reform of public administration in many countries is influenced by ideas of New Public Management (NPM) and Post-New Public Management (Post-NPM), with the aim to achieve better accountability but not to impinge on board autonomy.[174] NPM claims a stronger focus on public sector performance improves government accountability, whereas Post-NPM insist that co-ordination and network-based delivery lead to better accountability.[175]

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[169] Rentsch, C. & Finger, M. "Yes, No, Maybe: The Ambiguous Relationships between State-Owned Enterprises and the State" (2015) 86(4) *Annals of Public and Cooperative Economics* 617 p. 618.
[170] Supra note 168 p. 9.
[171] Supra note 169 p. 637.
[172] Flinders, M. & Moon, D. "The Problem of Letting Go: The "Big Society," Accountable Governance and the Curse of the Decentralizing Minister" (2011) 26(8) *Local Economy* 652 p. 652.
[173] OECD "Directorate for Financial and Enterprise Affairs Corporate Governance: Relationship of State-Owned Enterprises with other Shareholders" *Cesifo DICE Report* 3/2007 p. 1.
[174] Christensen & Lægreid "Performance and Accountability—A Theoretical Discussion and an Empirical Assessment" (2014) *Public Organization Review* 1 p. 1.
[175] Supra note 162.

Many European countries have commenced reforms toward greater board accountability using NPM principles as a benchmark, as essentially it prevents governments interfering with the day to day management of SOEs. Germany is influenced by the NPM principles by implementing individual incentives, which include 'pay-for-performance,' for a board, which is a compliance-based model of accountability. However, Pollitt recognises that linking accountability with performance is problematic as the two concepts are difficult to reconcile.[176] Page suggests due to the contradictory interpretations of accountability it is essential to be explicit about the perspective and dimension of accountability.[177] In terms of board accountability, the wave of NPM is linked with performance, so this is a suitable dimension to adopt as it is an "obligation to explain and justify conduct."[178] Romzek describes NPM accountability as answerability for performance.[179] This makes performance management key in public sector reform as it key from a principal-agent perspective to hold individuals to account.

Olsen highlights that performance management creates new accountability structures but while this may improve performance accountability, it does not imply better outcome on their performance, as resources are used for measuring and reporting rather than getting the job done.[180] NPM emphasises the need to measure public service, so to assess performance, supreme audit institutions (SAIs) are implemented across Europe which are independent reviews to access the efficiency and effectiveness in the use of public resources.[181] In Norway and Denmark these are publically assessable, which increases

[176] Pollitt, C. "Performance Blight and Tyranny of Light? Accountability in Advanced Performance Measurement Regimes" (2010) in Dubnick & Frederickson (Eds.) *Accountable Governance: Problems and Promises* Armonk: Sharpe 81.
[177] Page E. "Accountability as a Bureaucratic Minefield: Lessons from a Comparative Study (2010) 33(5) *West European Politics* 1010 p. 1011.
[178] Bovens, M. "Analysing and Assessing Accountability: A Conceptual Framework" (2007) 13(4) *European Law Journal* 447 p. 450.
[179] Romzek, B. "Dynamics of Public Sector Accountability in an Era of Reform" (2000) *International Review of Administrative Sciences 66*(1) 21 p. 22.
[180] Olsen, P. "The Institutional Basis of Democratic Accountability" (2013) 36(3) West European Politics 447 p. 462.
[181] Skærbæk Public Sector Auditor Identities in Making Efficiency Auditable: The National Audit Office of Denmark as Independent Auditor and Modernizer (2009) 34(8) Accounting, *Organizations and Society* 971 p. 971.

transparency and are used to hold ministries accountable.[182] To balance the relationship between a company and SOEs in Norway, the government is entitled to exercise authority at general meetings only and has no authority outside these parameters.[183] As the board and management have been charged with managing the State's investment is SOEs, they are accountable to the State on the following key issues:

"What are the company's main objectives, financial and other, and how are they measured and managed?
How does the company gain insight into the indicators, parameters and stakeholders that have the greatest impact on value creation in the company?
What measures does the company take to achieve its goals?
How does the board follow up the company's defined strategy?
How does the company work on managing its resources – financial, physical and human capital (including diversity and talent development)?
Does the company have a strategy or established measures or goals to get more female managers and senior executives?
If the management has variable remuneration: how will the board ensure alignment between the criteria for bonuses and the company's goals and targets?"[184]

Accountability in Norwegian SOEs is a priority and SOEs are subject to the same financial reporting codes and regulations as private companies.[185] In France, the Government Shareholding Agency was established to define the State's role as shareholder in SOEs.[186] The Agency ensures that annual reports on SOE operations are published, giving a true and fair view of the companies' performance.[187] The Agency makes strategic decisions for companies whereby the interests of all shareholders and the long-term viability of the

[182] Arthur, A. Rydland, L.S. & Amundsen, K. "The User Perspective in Performance Auditing – A Case Study of Norway" (2012) 33(1) *American Journal of Evaluation* 44 p. 44.
[183] Norwegian Ministry of Trade, Industry and Fisheries "The State Ownership Report" (2015) p. 28.
[184] Ibid.
[185] Department of Ownership, Royal Norwegian Ministry of Trade and Industry "Ownership Function of the Norwegian State" (2005) p. 6.
[186] Established in 2004 the Agency performs its services in connection with the Ministry of the Economy, Industry and Employment and the Ministry of Finance.
[187] See further https://www.economie.gouv.fr/welcome-to-the-french-ministry-for-the-economy-and-finance last accessed 20 June 2017.

companies is taken into consideration.[188] It also adopts annual budgets and medium-term plans and makes strategic decisions.[189]

To provide a clear separation between the State's role as owner and regulator, Finland adopted the *State Shareholdings and Ownership Steering Act* 2007.[190] This provided a harmonised approach of making the State independent from other regulatory organs. To measure non-listed SOEs success, Finnish SOEs are required to report their sustainability performance to allow for greater comparison between SOEs.[191] In Norway the Government provided a White Paper, which outlines ten main principles for SOEs:

"All shareholders shall be treated equally.
There shall be transparency in the State's ownership of companies.
Ownership decisions and resolutions shall be made at the General Meeting.
The State may set performance targets for each company together with other owners. The board is responsible for meeting these targets.
The capital structure of the company shall be consistent with the objective of the ownership and the company's situation.
The composition of the board shall be characterised by competence, capacity and diversity and shall reflect the distinctive characteristics of each company.
Compensations and incentive systems shall promote the creation of value in the companies and shall be generally regarded as reasonable.
The board shall exercise an independent control of the of the company's management on behalf of the owners.
The board shall adopt a plan for its own work and shall work actively with development of its own competence. The board's activities shall be assessed.
The company shall recognise its responsibilities to all shareholders and stakeholders in the company."[192]

[188] Ibid.
[189] Ibid.
[190] *The State Shareholdings and Ownership Steering Act* 2007 Finland (1368/2007).
[191] Prime Minister Office "Government Resolution on State Ownership Policy" 2011 Finland.
[192] Norwegian Ministry of Trade Industry and Fisheries "White Paper No. 22" 2002 Norway.

Sustainability reporting initiatives are growing across Europe. In Portugal the "Principles of Good Governance for companies belonging to the State-owned Corporate Sector"[193] was issued. These principles require SOEs to establish clear governance structures which have effective segregation of executive management and supervisory roles. SOEs are also expected to follow the same standards companies on the stock market are bound by.

C. IRISH STATE-OWNED ENTERPRISES IN CONTEXT

There are a number of different motivations that led to the establishment of SOEs. SOEs were founded shortly after independence in Ireland as the country was largely underdeveloped. With little private sector activity in the country or foreign investment it was up to the government to establish infrastructure and resources. SOEs expanded between the 1930s and 1950s when Ireland was experiencing a period of protectionism, so that trading outside of Ireland was restricted.[194] This meant that Ireland was left with little choice and so it had to become self-sufficient in many areas such as agriculture and industry.[195] The establishment of SOEs continued to grow and so they became vital component of enterprises in Ireland.[196]

The establishment of SOEs is more likely to arise if it is of national importance and the private sector is not prepared to step in and provide the service. Private sector companies are unlikely to enter an industry if there is no commercial incentive and they do not envisage a return on their investment. As a result of this it is left to SOEs to fill this gap. This was pinpointed by Lemass, who served in government during the foundation of many SOEs.[197] This point is reaffirmed by Hastings who pointed out that:

[193] "Cabinet Resolution" Portugal no. 49/2007 of 28 March 2008.
[194] O'Hagan & Newman *The Economy of Ireland, National and Sectorial Policy Issues* (10th ed. Gill and Macmillan Dublin 2008) p. 17.
[195] Reeves & Palcic "Privatization Policy and Enterprise Performance: The Case of Ireland" (2004) 75(4) *Annals of Public and Cooperative Economics* 525 p. 527.
[196] King, L. "Saints, Shamrocks, and Signifying Practices: Aer Lingus and the Materialization of Irish Identity" (2011) 46(1) *Eire-Ireland A Journal of Irish Studies* 128.
[197] Lemass, S. 'The Role of State-sponsored Bodies in the Economy' (1959) 6 (4) *Administration* p. 278.

"State financed industries have been set up only where considerations of national policy were involved or where the projects were beyond the scope or unlikely to be undertaken by private enterprise."[198]

The State has, in some cases, to provide a service even if there is no commercial advantage of doing so if it is required for the national interest. This is referred to as the public service obligation (PSO).[199] A nominal levy will be charged to customers to offset the commercial disadvantage of providing such services.[200] For example, there is a PSO charge applied to electricity bills[201] and a PSO levy is charged by airlines.[202] The State is not required to provide services where there is a commercial disadvantage but it must *provide for* these services.[203] So effectively, the State has to either provide these services, or it should organise for another enterprise to provide the service. In return for providing these services, the State will allow subsidies to be given to the entity who will take on the PSO. It is the final consumer who bears the responsibility for paying the PSO but the levy must be apportioned equally by the supplier.[204] Bovis suggests that a State should ensure that the PSO is being carried out by the operator who requires the lowest financial compensation.[205] It is apparent the State took an active role in setting up SOEs which included enterprises that would accumulate revenue and those that would not. The result of the PSO is that if it is in the national interest to provide a service this must be done even if it provided at a loss.

However, it is entrenched in Irish history that SOEs were established to help develop the country and the requirement of becoming successful businesses was largely overlooked.

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[198] Hastings, T. *Semi-States in Crisis* (Blackhall Publishing Dublin 2003) p. 30.
[199]See further Hennig, M. *Public Service Obligations: Protection of Public Service Values in a National and European Context* Legal Issues of Services of General Interest (Asser Press The Hague 2011) p. 179.
[200] See further Defeuilley, C. "Competition and Public Service Obligations: Regulatory Rules and Industries Games" (1999) 70(1) *Annals of Public and Cooperative Economics* 25.
[201] Public Service Obligations Order (Amended) 2002 Statutory Instrument 217.
[202] See further Santana, I. "Do Public Service Obligations Hamper the Cost Competitiveness of Regional Airlines?" (2009) 15(6) *Journal of Air Transport Management* 344.
[203] See further Sauter, W. "Services of General Economic Interest and Universal Service in EU Law" (2008) *European Law Review* 172.
[204] *The Electricity Regulation Act* 1999 (Public Service Obligations) (Statutory Instrument No 217 of 2002) Schedule 2 section 1and 3.
[205] Bovis, C. "Public Procurement, Public-Private Partnerships and Public Services in the EU" (2010) 5(2) *European Public Private Partnership Law Review* 85 p. 89.

Lane reiterates the point that earlier SOEs were formed as a result of underdeveloped capital markets, which prevented private entrepreneurs from raising capital so as to invest in the sectors that later became SOEs.[206] To illustrate this point, an SOE of central importance in Irish society is CIÉ.[207] The capital and resources to establish this body would be too large to be absorbed by a private company. Not only is money a factor but if providing transport was left to the private sector it is likely that rural parts of the country would be neglected where profit projections may be minimal. To take another example, the first airline established in the country was Aer Lingus,[208] which, without State involvement, would be unlikely to have happened at that time in 1936. The establishment of Aer Lingus was prompted by two underlying objectives, to provide air transport in Ireland and to promote tourism and economic growth.[209] The airline was the impetus for what was termed 'New Ireland' which after gaining independence it modernised the country to a State of progression and distinction.[210] The airline gave Ireland a national identity to an international audience. Over the years the airline diversified by broadening its business activities to provide transatlantic flights from the 1950's. The State share in the company diminishing from 85.1% to 25.11% in 2006.[211]

SOEs were also established to fulfil non-commercial roles, including promotional, regulatory or semi-judicial functions. The creation of separate legal entities removes political influence and from being involved in the decision making process. Examples of these entities are Bord Bia[212] and An Bord Pleanála.[213] This delegation and decentralisation takes controversial decision out of political ambit, whilst retaining the ability of these entities to be funded by government.

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[206] Lane, P. "The Role of the State" in O'Hagan *The Economy of Ireland: Policy and Performance of a European Region* (8th ed. Dublin Gill and Macmillan 2000) p. 92.
[207] Córas Iompair Éireann established under *The Transport Act* 1950.
[208] Established under the *Air Navigation and Transport Act* 1936.
[209] Garavan, T. O Cinneide, B. Garavan, M. & Cunnningham M. *Cases in Irish Business Strategy and Policy* (Oak Tree Press Dublin 1996) p. 53.
[210] O'Rian *Aer Lingus 1936-1986 A Business Monograph* (Magill Printing Dublin 1986) p. 9.
[211] https://www.aerlingus.com/about-us/corporate-information/iag-group/ last accessed 19 June 2017.
[212] Bord Bia was established under *An Bord Bia Act* 1994.
[213] Established under *the Local Government (Planning and Development) Act* 1976.

(1) The Classification of State Sponsored Bodies

Due to the scale of activities that can encompass State-sponsored bodies and the variety of purposes they serve, it can be difficult to classify public sector bodies. There are numerous terminologies describing State-sponsored bodies, including SOEs, semi-state agencies and State bodies. This thesis covers State-sponsored bodies that are commercial and non-commercial basis as regardless of their structure all State-sponsored bodies have a common objective of serving the public interest, which may also give rise to a commercial gain. While the term SOEs more commonly refers to commercial entities, this thesis also extends to non-commercial State enterprises due to the conflicting issues that arise with the State being owner, investor and controller of entities. It is also relevant to cover both commercial and non-commercial SOEs as commercial SOEs may not be able to be in a position to fully fund itself, if it runs at a loss, so the State may be financer rather than income from sales of goods and services. A way to distinguish between different State bodies is by looking at their structure.

(i) Commercial entities

Commercial SOEs can be defined as "primarily, that they operate in a commercial atmosphere where commercial criteria can be used to judge their effectiveness."[214] The key feature is how their revenue is generated, for commercial SOEs this is from selling goods or services. This makes commercial SOEs most comparable to private companies, which operate at an arm's length basis. MacCarthaigh defines commercial SOEs as:

"Commercial state enterprises are bodies that are self-financing or rely only partially on State funding would exclude those enterprises that depend on considerable State funding in the initial phase of their development, or on an ongoing basis because of the specific nature of their work, which is carried out in an explicitly commercial environment."[215]

[214] Report of the Public Services Organisation Review Group (Dublin: Stationery Office, 1969) p. 44.
[215] MacCarthaigh, M. *The Corporate Governance of Commercial State-Owned Enterprises in Ireland* (IPA CPMR Research Report 9 Dublin 2009) p. 5.

This indicates that while commercial SOEs may have received their initial funding from the government, as they generate their own income they should become self-sufficient. This allows commercial SOEs to operate so that State ownership is neither an advantage nor a disadvantage. For example, the ESB,[216] RTÉ[217] and Aer Lingus[218] were established as commercial SOES to provide services that are sold directly to the public.

(ii) Non-commercial State-sponsored Bodies

To meet the public interest State-sponsored bodies were established that do not have commercial objectives and instead the entity is focused on the nature of the services provided, where the primary objective is to provide goods or services that deliver social benefits for society. Non-commercial bodies have "regulatory, development, service delivery or advisory roles."[219] These bodies can be classified as follows: Development State bodies

Development State bodies provide 'back-up services.' Whilst they do not provide services directly to the public, they assist industries for example the IDA.[220]

Cultural State bodies

Cultural State bodies provide entertainment and education, such examples include the National Theatre Company[221] and the Irish Film Board.[222]

[216] *The Electricity Supply Board Act* 1927 established the ESB, which was the provider of electricity in Ireland. The ESB was one of the first SOEs founded in the State as it was one of the 19 SOEs part the Free State Infrastructure Programme between 1927 and 1939.
[217] RTÉ was established under the *Broadcasting Authority Act* 1960.
[218] Aer Lingus was incorporated on the 22 May 1936 by the Irish Government to provide an air travel service between Ireland and the UK.
[219] The Department of Public Expenditure and Reform *The Code of Practice for the Governance of State Bodies* (Dublin 2016) p. 11.
[220] The IDA Ireland was formed in 1949 as part of the Department of Industry & Commerce to encourage foreign investment in Ireland and exports from Ireland.
[221] The Theatre was given State subsidies from 1925 onwards to promote Irish writers and artists.
[222] Established under the *Irish Film Board Act* 1980.

Health State bodies

Health State bodies provide services in the health industry, for example, the Medical Council[223] and the National Drugs Advisory Board.[224]

Regulatory/advisory bodies

Regulatory bodies advise the government on areas of public policy, such as the Higher Education Authority.[225]

(2) Methods of Establishing SOEs

The method of establishment of SOEs will depend on the objectives and functions of each specific organisation. SOEs can be established through one of four different methods outlined below.

(i) Private Limited Company

The first method of establishing an SOE is to form a private company under the *Companies Act*.[226] Nítrigin Éireann Teoranta (NÉT)[227] is an example of an SOE which was established as a private company. It was the sole manufacturer of heavy chemicals in the country. It was recognised that because there was a decline in demand for such products,[228] it was wound up in 2002.

Having a choice in the method of establishing SOEs is useful as SOEs encompass a wide variety of enterprises, including commercial and non-commercial. A fundamental feature

[223] Established under the *Medical Practitioners Act* 1978.
[224] Established in July 2000 under the auspices of the Department of Tourism, Sport and Recreation to conduct, commission and analyse research on issues relating to drugs and to advise Government on policy development in the area.
[225] *Higher Education Authority Act* 1971.
[226] *The Companies Act* 2014 (as amended) and predecessor Acts.
[227] "Nítrigin Éireann Teoranta Bill 2000: Second Stage" Dáil Eireann Debate Volume 524 No. 2 17 October 2000.
[228] Ibid.

of a limited company is that it is a separate legal entity, however this cannot be strictly applied to SOEs, as the shareholding held by the government in SOEs is not directly equivalent to shareholders in limited companies. A government has extra responsibilities as owner of SOEs and accordingly the government will have greater powers than those of shareholders of listed companies. A government shareholder should scrutinise the actions of the board of SOEs. It is also necessary to ensure that sufficient measures are in place to ensure board of SOEs are monitored and accountable for its performance and so prevent shareholder passivity should not arise, a problem which often occurs from shareholders of listed companies. This issue can be dealt with through issuing a golden share which gives majority voting rights to the government, making them a dominant shareholder.

(ii) Public Company

The second method of establishing SOEs in Ireland is to form a public company, under the *Companies Act.*[229] Aer Rianta Ltd is a successful State-owned public company. It was established in 1937 with the task of managing Irish airports and developing Irish aviation.[230] It changed its name to DAA plc in November 2014.

(iii) Establishment of a Statutory Corporation

The third means of setting up SOEs is forming a statutory corporation that comes into existence through the enactment of legislation and will be governed by statute that will lay out its functions, duties and responsibilities. The statute provides the structures for the board of SOEs and identifies what powers the board has. Other matters included are the borrowing powers of SOEs and provisions are also laid out for accounts and audits and the procedures to follow for reporting information to the relevant Minister. There are many examples of such statutory SOEs including Bord na Móna,[231] which was established to manage Irelands peat resources, An Bord Fáilte[232] which was established to promote

[229] Supra note 226.
[230] "Written Answers Aer Rianta" Dáil Eireann Debate Volume 455 No 5 5 July 1995.
[231] Established by the *Turf Development Act* 1946.
[232] Established by the *Tourist Traffic Act* 1952.

tourists to the country and CIÉ[233] which was formed with the aim of providing a transport service within Ireland.

(iv) Establishment by Ministerial Order

The final method of creating SOEs is establishing a corporate body, by secondary legislation under an enabling Act. For example, a corporate body established under the *Local Government Services (Corporate Bodies) Act* 1971 is Limerick Northside Regeneration Agency, which was setup to secure the social and economic regeneration and for improvements in the physical environment of Limerick."[234]

Essentially, the most commonly used approaches taken in establishing SOEs is firstly under statute and secondly through establishing a private or public limited company where the Minister is the sole shareholder. The value of establishing SOEs under the latter option is it prevents having to amend the incorporating statute if there are changes in the role of the entity.[235] Golding advocates that it is more suitable for commercial SOEs to register as a company and for non-commercial SOEs to be registered under statute.[236] Commercial SOEs have many of the same objectives as private sector companies, making it more appropriate to allow SOEs to operate within the same parameters as their private sector equivalent. However, while this would appear a more suitable approach, SOEs were established out of expediency and so there was little forward thinking when they were established, so there is no consistency in their methods of establishment.[237] Perhaps a way of rectifying the problems that resulted in the lack of forward thinking is through an argument made by MacCarthaigh, where he considers it is more appropriate to change the legal status of statutory corporations to public companies. This gives a greater freedom so that legislation will not have to be amended when their objectives are altered.[238] For example, the ESB is bound by the *Electricity (Supply) Act* 1927 but there was several

[233] Established by the *Transport Act* 1944.
[234] The Regeneration Agency was established under the *Local Government Services (Corporate Bodies) Act* 1971 (Statutory Instrument No 275 2007) section 5.
[235] MacCarthaigh, M. *The Corporate Governance of Commercial State-Owned Enterprises in Ireland* (IPA CPMR Research Report 9 Dublin 2009) p. viii.
[236] Golding "The Juristic Basis of the Irish State Enterprise" (1978) 13(2) The Irish Jurist 302 p. 307.
[237] Ibid.
[238] Supra note 215 p. 8.

amendments to this Act for updates in the company objectives.[239] Despite suggestions as to the most appropriate way of establishing SOEs, it appears that the chosen method of establishment will depend on the framers of the individual enterprise.

(3) An example of strong application of governance standards

The ESB is an example of how good governance standards aim to improve the overall standards of the board. To date there has not been any significant doubt raised over the manner in which the board is run. The ESB gives detailed information on its corporate governance standards implemented by the organisation.[240] The emphasis on good practice of governance standards stems from the Department of Communications, Energy and Natural Resources as there is the Electricity Corporate Division which has a primary objective of ensuring the ESB is complying with governance standards where required. A feature in their governance is the importance of independence, where necessary to ensure effective governance standards. The ESB's audit committee comprises four non-executive directors (NEDs) which perhaps can be considered a requirement for the NEDs to utilise their supervisory function. The ESB Board established a separate committee, the Independent Transmission System Operator (ITSO) Committee, under the name EirGrid, to facilitate the independent management of the transmission system operator.[241] The ESB is also committed to accurate internal auditing and maintaining a code of ethics.[242]

To maintain a high standard of governance within the company there are internal control mechanisms in place which include:

- "A code of ethics that requires all Board members and employees to maintain the highest ethical standards in conducting business.

[239] *Electricity (Supply) Act* 1927 - 1988. For example the 1945 Amendment was "to authorise and provide for the preparation and execution by the electricity supply board of schemes for the generation of electricity by hydraulic power derived from suitable rivers (in addition to the Shannon and the Liffey), the acquisition and management by the said board of fisheries and fishing rights in such rivers, and the making to the said board of grants of public moneys for the electrification of rural areas" *Electricity (Supply) Act* 1945.
[240] See further http://www.esb.ie/main/about-esb/corporate-governance.jsp last accessed August 2017.
[241] See further http://www.esbelectricmail.com/_archives/em_archive/archives/indexba29.html?id=313&cat=2 last accessed June 2017.
[242] See http://www.esb.ie/main/about-esb/audit-committee-of-the-board.jsp last accessed August 2017.

- Clearly defined organisational structure, with defined authority limits and reporting mechanisms to higher levels of management and to the Board which support the maintenance of a strong control environment.
- A corporate governance framework which includes risk analysis, financial control review and formal annual governance compliance statements by the management of business lines.
- A comprehensive set of policies and procedures relating to operational and financial controls.
- Large capital projects require the approval of the Board, and are closely monitored on an ongoing basis by the Finance and Business Performance Committee. They can also be subject to post completion audits.
- Comprehensive budgeting systems with an annual budget approved by the Board.
- A comprehensive system of financial reporting.
- Cumulative actual results and key performance indicators are reported against budget and considered by the Board on a monthly basis. Any significant changes and / or material adverse variances are questioned by the Board, and remedial action taken where appropriate.
- A confidential helpline service to provide staff with a confidential, and if required, anonymous means to report fraud or ethical concerns.
- A designated risk management function in ESB.
- Review and consideration of the half-yearly risk review process and regular risk management updates.
- Independent advice on the adequacy of the current risk management process in operation in ESB.
- Review and consideration of certifications from management of satisfactory and effective operation of systems of internal control, both financial and operational.
- A review of the programme of Group Internal Audit and consideration of their findings and reports.
- Group Internal Audit also report regularly on the status of issues raised previously from their own reports and reports from the external auditor.

- A review of reports of the external auditor, KPMG, which contain details of any significant control issues identified, arising from its work as auditor."[243]

In assessing how SOEs perform, the measure will be based on board accountability and performance assessment. There are performance management mechanisms in place in an attempt to increase board accountability in the ESB.[244] The audit committee of the ESB is required to review how the ESB have adopted the principles of the Code of Practice for State Bodies.[245] However, the guidelines fail to identify how often this assessment should be carried out and the implications for not implanting the Code were not stipulated. The board is also required to adhere to the ESB's code of ethics which require the board to ensure they act in the best interests of the company and do not receive personal gain from their position in the company.[246]

SOEs are required to provide a statement of internal financial controls identifying any breaches that arose.[247] However, the independent auditor noted that this was not provided by ESB in their annual statement in 2015.[248] Whilst a failure to provide information does not imply wrongdoing, it highlights the shortcomings of corporate governance on a quasi-legal basis - SOEs do not have to follow all governance provisions and there are no clear implications for not adhering to governance standards. This is something which should be addressed in the ESB's 2016 annual report which has not yet been made available. A freedom of Information request was made to the ESB in February 2017, for further information into the corporate governance of the ESB, however the request was refused on the grounds that on the grounds that this was commercially sensitive information.[249]

[243] ESB *Annual Report* 2015 p. 73.
[244] Ibid p. 73.
[245] Ibid p. 73.
[246] ESB "Code of Ethics for Board Members" 2014.
[247] The Department of Finance *The Code of Practice for the Governance of State Bodies* (Dublin 2009) p. principle 13.1(iii).
[248] Supra note 243 p. 91.
[249] See thesis appendix for Freedom of Information refusal letter.

D. CORPORATE GOVERNANCE PRINCIPLES

(1) Definition of Corporate Governance

Corporate governance has been described as:

"the processes by which organisations are directed, controlled and held to account. It encompasses authority, accountability, stewardship, leadership, direction and control exercised in the organisation."[250]

By and large there is consensus in defining corporate governance. Inevitably it may vary from source to source but definitions will largely describe the manner in which the board of a company should carry out their duties keeping the best interests of the company in mind.[251] The initial attempt to draft corporate governance standards for listed companies on the stock exchange arrived in the form of the *Cadbury Report*[252] published in the UK in 1992. The *Cadbury Report* was introduced after scandal in the UK including the BCCI[253] bank fraud scandal and the Robert Maxwell scandal, where Maxwell alleged misappropriated £440 million pension funds.[254] The *Cadbury Report* defined corporate governance quite simply as "the system by which companies are directed and controlled."[255] Over twenty years later this definition is maintained in the most recent report on corporate governance the *UK Corporate Governance Code* (formerly the

[250] Australian National Audit Office (ANAO) *Public Sector Governance: Better Practice Guide* (2003) p. 6.
[251] See further Kroll, M. Walters, B & Wright, P. "Board Vigilance, Director Experience, and Corporate Outcomes" (2008) 29(4) *Strategic Management Journal* 363.
[252] *Report of the Committee on the Financial Aspects of Corporate Governance* ("*the Cadbury Report*") (UK 1992).
[253] Kanas, A. "Pure Contagion Effects in International Banking: The Case of BCCI's Failure" (2005) 8(1) *Journal of Applied Economics* p. 101.
[254] Hamill, P. Ward, A.M. & Wylie, J. "Corporate Governance Policy New Dawn in Ireland and the UK" (2010) 42(6) *Accountancy Ireland* p. 56.
[255] The full definition of corporate governance offered by *the Cadbury Report* is "Corporate governance is the system by which companies are directed and controlled. Boards of directors are responsible for the governance of their companies. The shareholders' role in governance is to appoint the directors and the auditors and to satisfy themselves that an appropriate governance structure is in place. The responsibilities of the board include setting the company's strategic aims, providing the leadership to put them into effect, supervising the management of the business and reporting to shareholders on their stewardship. The board's actions are subject to laws, regulations and the shareholders in general meeting." *Report of the Committee on the Financial Aspects of Corporate Governance* (Cadbury Report) (UK 1992) para. 2.5.

Combined Code).[256] However, alternative definitions of governance embrace more than control of organisations. The Australian National Audit Office defines governance as:

"corporate governance generally refers to the processes by which organisations are directed, controlled and held to account. It encompasses authority, accountability, stewardship, leadership, direction and control exercised in the organisation."[257]

This method of setting principles based on how the company is controlled remained in revised and updated versions of corporate governance codes. There is a move to a commercial understanding today of associating corporate governance with best practice standards in the boardroom, as it provides solution for the dynamics facing a board and it also gives incentives for good management and deters malpractice within the board.[258] Brennan and Solomon identify accountability as one of the key aspects of governance principles.[259] Shaoul, Stafford and Stapleton concur with Brennan and Solomon including a strong framework will improve the governance of SOEs.[260]

(2) Themes of Corporate Governance Standards

Corporate Governance is a key component in monitoring boards of SOEs. The standards seek to ensure accountability, transparency and efficiency, so these principles are the cornerstone of corporate governance. A corporate governance framework provides additional guidelines and duties for a board for SOEs. For example, it can contextualise the government's role in SOEs to alleviate the agency problem outlined in chapter one, that exists between the government and SOEs. A framework can also set additional obligations such as the requirement for SOEs to operate as successful businesses, these issues are addressed below.

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[256] Financial Reporting Council (UK) *The UK Corporate Governance Code* (2010) p. 1.
[257] ANAO *Principles and Better Practices: Corporate Governance in Commonwealth Authorities and Companies* (1999) Discussion Paper Canberra: Australian National Audit Office 1.
[258] Young, D. "The Real Agenda: Corporate Governance and Performance" (2006) 38(3) *Accountancy Ireland* 1.
[259] Brennan, N. & Solomon, J. "Corporate Governance, Accountability and Mechanisms of Accountability: An Overview" (2008) 21(7) *Accounting, Auditing & Accountability Journal* 885 p. 890.
[260] Shaoul, J., Stafford, A. & Stapleton, P. "Accountability and Corporate Governance of Public Private Partnerships" (2012) 23(3) *Critical Perspectives on Accounting* 213 p. 213.

Corporate governance can be identified by associating the key themes that comprise a governance framework. The OECD provides four key principles central to a corporate governance agenda, according in their *Principles of Corporate Governance*.[261] These principles are transparency, accountability, responsibility and fairness.

(i) Transparency

The importance of transparency is highlighted as:

"Transparency is required to ensure that stakeholders can have confidence in the decision-making processes and actions of public sector organisations, in the management of their activities, and in the individuals within them."[262]

In the OECD's *Principles of Corporate Governance*, transparency and disclosure are dealt with simultaneously,[263] by disclosing material information such as the performance of the company, the objectives and foreseeable risk factors will make the company more transparent.[264]

(ii) Disclosure

Disclosure is an important feature of corporate governance codes as it is expected that it will improve transparency.[265] Disclosure is an essential component of a corporate

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[261] OECD *Principles of Corporate Governance* (France 2004).
[262] Audit Office of New South Wales *Australian Performance Report: Public Sector Corporate Governance: Corporate Governance - Volume One: in Principle* (1997) p. 8.
[263] Supra note 261 p. 22.
[264] See further Timea "Corporate Governance - The Role and Application of the Principle of Transparency" (2011) 20(1) *Annals of the University of Oradea Economic Science Series* 616. See further Bushman, R., Piotroski, J. & Smith A. "What Determines Corporate Transparency?" (2004) 42(2) *Journal of Accounting Research* 207.
[265] See further Healy, P. & Palepu, K. "Information Asymmetry, Corporate Governance Disclosure, and the Capital Markets: A Review of the Empirical Literature" (2001) 31 *Journal of Accounting and Economics* 405. See further Bhasin, M. "Voluntary Corporate Governance Disclosures Made in the Annual Reports: An Empirical Study" (2012) 4(1) *International Journal of Management & Innovation*. See further Baek, H. Young, K., Johnson, D & Joung, K. "Managerial Ownership, Corporate Governance, and Voluntary Disclosure" (2009) 15(2) *Journal of Business & Economic Studies* 44.

governance regime to eliminate information asymmetries. In order to improve internal structures there needs to be an understanding of current practices and existing disclosure regimes and identify weaknesses and flaws. By highlighting tools of disclosure this will provide an insight to the operation of the relevant entities, which should aid in improving openness and performance. If reframing internal structures there should be careful consideration of tools that will result in robust well defined standard that will assist with implementation and improve the quality of standards in organisations. If SOEs are to retain autonomy it has to be shown they operate within prescribed established standards and there is correct allocation of resources.

(iii) Responsibility

Responsibility of the board is paramount.[266] Responsibility falls heavily on the board members, so that they are responsible and accountable for its actions.[267] Board duties are numerous and include the duty to act in good faith and in the interests of the shareholders, a duty on the directors as described in *Re Smith and Fawcett*[268] and also the duty of the board to monitor governance standards.[269]

The *Worker Participation (State Enterprises) Acts* 1977 – 1993 grants rights to employees of State bodies to be involved in the decision making process by board participation. The effect of this will allow employees to take an active part in the running of SOEs. The 1998 Act provides for sub-board participation for employees which should include the following essential features:

"a regular exchange of views and information between management and employees concerning matters which are specified in the agreement
timely delivery of information about certain decisions which are liable to have a significant effect on employees' interests

[266] See further Vera-Muñoz, S. "Corporate Governance Reforms: Redefined Expectations of Audit Committee Responsibilities and Effectiveness" (2005) 62(2) *Journal of Business Ethics* 115.
[267] Supra note 261 p. 24.
[268] [1942] 1 All ER 452.
[269] Ibid.

dissemination to all employees of information and views arising from the participative arrangements."[270]

(iv) Fairness

The requirement of fairness is reflected in rights given to shareholders.[271] Shareholders have the right to be informed of fundamental changes within entities and also the right to vote in general meetings and the right of all shareholders to be treated equally.[272] There are statutory rights for shareholders under the *Companies Act* 2014 which include the right to information:

- a right to inspect and receive copies of the books containing the minutes of general meetings and resolutions.[273]
- a right to inspect and obtain copies of the various registers kept by the company including the register of members, the register of directors and secretaries and the register of directors' and secretary's interests.[274]
- a right to a copy of the company's financial statements for the most recent financial year laid before the AGM and the directors' report for that year and the statutory auditors' report.[275]

Other statutory rights are in place to protect the company and its shareholders which include preventing directors abusing their position of using company funds and dealing with the termination of employee contracts.[276] Shareholders also have the right to attend and vote at meetings,[277] right to dividends[278] and rights on the winding up of a company.[279]

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[270] *The Worker Participation (State Enterprises) Acts* 1998 section 6.
[271] Supra note 261 p. 18.
[272] Supra note 261 p. 20.
[273] Supra note 226 section 216.
[274] Ibid section 216.
[275] Ibid section 339.
[276] Ibid section 186.
[277] Ibid section 189.
[278] Ibid section 117 (1).
[279] Ibid section 571.

The *UK Corporate Governance Code* provides principles of governance standards based on accountability, transparency, probity and focus.[280] These principles remain the cornerstone of Irish governance codes. This is reflected through the continued commitment to providing transparency, accountability and fairness in the Irish reports.[281] These principles are applied to the auditing process, management and remuneration. For example, it is paramount that the board is clear on what their role, functions and responsibilities are. This makes them aware of their parameters, so as to ensure that governance standards operate on a basis that is transparent and fair. This is addressed in early in the governance codes for State bodies:

"Each body should be clear about its mandate and from that identify the various functions, roles and responsibilities entailed in the delivery of that mandate."[282]

(3) Incentives for applying corporate governance standards

The value organisations place on corporate governance is important, as it varies significantly between entities. When trying to attract shareholders, there is an argument to be made that it is often individual and institutional shareholders that are interested in the standards of corporate governance in a company as they are associated with a better performing company.[283] Competitiveness is the driving force to implement good governance standards as this will attract investors.[284] Distinct corporate governance standards can act as a safety tool for investors, by giving reassurance that investments are made to a company that appears to be well run and managed. "Good governance leads to

[280] Supra note 256 p. 1.
[281] ISE *The Irish Corporate Governance Annex* 2010 p. 1.
[282] The Department of Finance *The Code of Practice for the Governance of State Bodies* (Dublin 2009) p. 1. See also "Code of Practice for the Governance of State Bodies" Department of Finance Press Release 4 October 2001.
[283] McClenaghan, O., Canning, M., O'Hallora, S. & Eiholzer, C. "The European Union and Corporate Governance: From Enron to Parmalat and Beyond" (2004) 11(2) *Commercial Law Practitioner* 31.
[284] A point advocated by the OECD, in particular they indicate that governance standards are necessary for collective investment institutions and pension funds. OECD *Principles of Corporate Governance* (France 2004) at 3. See also OECD *Corporate Governance of Non-Listed Companies in Emerging Markets* (Paris 2006) and European Commission Green Paper *The EU Corporate Governance Framework* (Brussels 2011).

good management, good performance, good stewardship of money, and ultimately, good outcomes."[285]

The value of relevant corporate governance will to a large extent depend on how entities implement principles. Corporate governance codes operate on a 'comply or explain' basis.[286] For listed companies, the 'comply or explain' principle is for a board of directors to follow the provisions and if this has not been done, an explanation for non-compliance must be provided. The *UK Code* recognises that in companies below FTSE 350 not all of the codes are applicable to them and so not all sections of the code will be applied to their governance standards.[287] Good governance is not only achieved by following the *UK Code* and so it is accepted that if alternative methods of governance leads to achieving better governance, then following all provision in the *UK Code* is not necessary.[288]

In a similar way, for State bodies, not all of the provision in the *Governance Code for State Bodies* will be applicable to all entities, as code highlights that this would have a disproportionate effect on some entities due to the diverging scale of their activities.[289] Instead, it is for the board with the authorisation of the relevant Minister to set the governance codes which will depend on the size and nature of the enterprise. This leaves the opportunity for other standards to be phased in over time, ensuring that as the enterprise grows and develops and so too will the governance standards.[290]

The requirement to comply with corporate governance standards was introduced in the *Cadbury Report*,[291] which was included in all subsequent corporate governance codes. The *Cadbury Report*[292] stressed that if a company did not comply with the standards, a reason for non-compliance had to be given.[293] It is for the board to decide which principles do not

[285] The UK Independent Commission on Good Governance in Public Services *Good Governance Standard for Public Services* (UK 2005 & 2011) see forward.
[286] *Report of the Committee on the Financial Aspects of Corporate Governance* (*Cadbury Report*) (UK 1992) p. 1.3.
[287] Supra note 256 p. 5.
[288] Ibid.
[289] Supra note 219 p. 6.
[290] Ibid p. 7.
[291] *Supra note 252.*
[292] Ibid.
[293] Ibid p.13.

have sufficient relevance to their company. However, a detailed explanation has to be given as to why the standards have not been implemented. The aim of the principle was to give shareholders an accurate picture of the affairs with companies which highlighted how much of standards were being implemented and reason as why particular code provisions were not applied.[294] For non-listed companies deciding to act in accordance with corporate governance codes can be established by following the quality standards set in the Institute of Directors and the National Standards Authority in Ireland, SWiFT 3000:2010 *Code of Practice for Corporate Governance Assessment in Ireland*.[295]

(4) The Link between Corporate Governance for Listed Companies and SOEs

The level of corporate governance for SOEs requires a higher level of standards and in some instances more than that required for listed companies.[296] However, corporate governance standards for SOEs frequently mirror standards set for listed companies. Board structure, the role of directors, non-executive director's remuneration and risk management are all important features for corporate governance standards as they are linked to board accountability. For example, board structure is paramount to an investigation of corporate governance standards as they are the impetus for implementing governance standards.

Reynolds questions if the legal basis of directors can be applicable in SOEs. However, Reynolds considers the term 'director' as having a legal basis only for SOEs established under the *Companies Act* and not through any other basis such as establishment through statute, as there is a distinction between the powers and duties of a registered company and a member of a board of a State agency.[297] However, when various reports[298] on governance for SOEs and legislation[299] are examined, this distinction of directors associated with SOEs established under legislation or statute does not exist. The Report on *The Structural*

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[294] Ibid.
[295] National Standards Authority in Ireland, *SWiFT 3000:Code of Practice for Corporate Governance Assessment in Ireland* 2010.
[296] TASC *Submission to the Central Bank and Financial Services Authority of Ireland in relation to Consultation Paper CP41 on Corporate Governance Requirements for Credit Institutions and Insurance Undertakings* (2010) p. 17.
[297] Reynolds, I. "Public Sector Corporate Governance" (2009) 3 *Accountancy Ireland* 51 p. 53.
[298] Institute of Public Administration *The Structural Characteristics of State-Sponsored Bodies* (IPA Dublin 1980).
[299] *Worker Participation (State Enterprises) Act* 1977 and 1988.

Characteristics of State-Sponsored Bodies points out that whether State-sponsored bodies are formed under the *Companies Act* or through legislation the Minister, will still appoint a board of directors.[300] In addition to this the *Worker Participation (State Enterprises) Act* 1977 and 1988 gives employees the right to have a representative on the board of directors, thereby recognising the status of a board of directors.

Remuneration for directors of SOEs is derived from taxpayers' money and so it is important that the rate of remuneration is fair and directors carry out their functions. While these issues are important for both SOEs and listed companies, there are very different requirements and objectives between the two entities. Therefore, comparisons will be made between the different requirements of codes for listed companies and SOEs.

(i) Corporate governance for listed companies

To investigate the link between corporate governance standards for SOEs[301] and listed companies feature of *UK Corporate Governance Code*,[302] will be examined. Irish standards for SOEs are modelled on this Code and companies on the Irish Stock Exchange are required to implement this Code.[303]

There has been a renewed interested in corporate governance models in the late 20th century and early 21st century.[304] This renewed interest in corporate governance is tied to the public scandals of the time. The events in Enron[305] and WorldCom[306] are associated

[300] Supra note 298 p. 4.
[301] Supra note 219.
[302] Financial Reporting Council (UK) *The UK Corporate Governance Code* (2014).
[303] Ibid.
[304] See further Blackwell, C. "Corporate Governance Evolution and Practice In Irish Companies" (2009) 41(2) *Accountancy Ireland* 34. See also Brennan, N. & McCafferty, J. "Corporate Governance Practices in Irish Companies (1997) 18 *Irish Business & Administration Research* 116.
[305] See further Parikh, K. "Enron Episode: Lessons for Power Policy" (1995) 30 (41/42) *Economic and Political Weekly* 2543, Deakin & Konzelmann "Learning from Enron" (2004) 12 *Corporate Governance: An International Review* 134, Coffee,J. "What Caused Enron? A Capsule Social and Economic History of the 1990's," (2003) 89 *Cornell Law Review* 269.
[306] Worldcom is now trading under the name of MCI, Inc. See further Kuhn, R. & Sutton, S. "Learning from WorldCom: Implications for Fraud Detection through Continuous Assurance" (2006) 3 *Journal of Emerging Technologies in Accounting* 61. See also Brickey, K. "From Enron to WorldCom and Beyond: Life and Crime after Sarbanes-Oxley" (2003) 81 *Washington University Law Quarterly* 357, Zekany, Braun & Warder "Behind Closed Doors at WorldCom" (2004) 19(1) *Issues in Accounting Education* 101. Scharff, M.

with the resurgence of an interest in corporate governance standards. Financial irregularities arising within the above named companies prompted the surge in interest in corporate governance standards,[307] as activities that were wrong and illegal were carried out by the senior officials in both companies.[308]

Clearly innovative activities of the directors gave Enron's directors the ability to raise the share prices to become the sixth largest energy company in the world, albeit based on fraudulent accounting activity.[309] Their activities inflated Enron's trading prices by implementing 'mark to market'[310] accountancy practices, which only gave a projection of figures and allowed for losses to be hidden by accounting for them in future years. Due to the flaws in the financial reporting system it resulted in the collapse of the company in 2001, which earlier that same year was reported the seventh largest company in the United States.[311]

The Enron scandal prompted the passing of the *Sarbanes-Oxley Act*[312] in the United States which was "to protect investors by improving the accuracy and reliability of corporate disclosures."[313] The act set to improve governance standards for public companies in the United States. In the UK the *Cadbury Report*[314] was introduced after scandals such as BCCI[315] and Polly Peck[316] and later reports have built upon this. These additions to corporate governance standards include the *Higgs Report,*[317] *the Combined Code*[318] and the

"Understanding WorldCom's Accounting Fraud: Did Groupthink Play a Role?" (2005) 11(3) *Journal of Leadership & Organizational Studies* 109.
[307] Supra note 252.
[308] Miceli Da Silveira, A. "The Enron Scandal a Decade Later: Lessons Learned?" (2013) 30(3) *Homo Oeconomicus* 315 p. 318.
[309] Catanach, A. & Rhoades, S. "Enron: A Financial Reporting Failure" (2003) 48 *Villanova Law Review* 1057 p. 1057.
[310] Boje, D. Gardner, C. & Smith, W."(Mis)using numbers in the Enron story" (2006) 9(4) *Organizational Research Methods* 456 p. 460.
[311] Deakin, S. & Konzelmann, S. "Learning from Enron" (2004) 12 *Corporate Governance: An International Review* 134 p. 134.
[312] *The Sarbanes-Oxley Act* 2002 United States of America.
[313] Ibid p. 3763.
[314] Supra note 252.
[315] See further Passas, N. "The Genesis of the BCCI Scandal" (1996) 3(1) *Journal of Law and Society* 57.
[316] See further Wearing, R. *Cases in Corporate Governance* (Sage Publications London 2005) p. 40.
[317] Financial Reporting Council, *Report: Review of the Role and Effectiveness of Non-Executive Directors* (*The Higgs Report*) (UK 2003).
[318] Supra note 256.

UK Corporate Governance Code.[319] The *UK Corporate Governance Code* updated in 2010 inserted a key provision which required FTSE companies to provide clear and meaningful explanations where there was non-compliance with the code under the 'comply or explain' provision.[320] The requirement for companies to put the external audit contract out to tender at least every ten years was also introduced.[321] The FRC has been updated the *UK Corporate Governance Code* again in 2016.[322]

Corporate governance standards came under scrutiny during the financial crisis and in particular it exposed the standards and practices set with the financial sector.[323] The corporate failures highlighted the inability of governance codes to prevent excessive risk taking and that there was a low level of regulation in place.[324] The Central Bank's *Corporate Governance Code for Credit Institutions and Insurance Undertakings* 2011 imposed minimum mandatory core standards on credit institutions and insurance undertakings, to prevent the governance failures from reoccurring.

(ii) Irish Corporate Governance Annex

Research into corporate governance standards for SOEs would not be complete without addressing corporate governance standards for listed companies as the basis for the Code for SOEs. Listing rules[325] are a set of obligations which companies must agree to must

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[319] Supra note 302.
[320] Financial Reporting Council *The UK Corporate Governance Code* (UK 2012) at 4.
[321] Ibid at principle C.3.7.
[322] Financial Reporting Council *The UK Corporate Governance Code* (UK 2014) Financial Reporting Council *The UK Corporate Governance Code* (UK 2016).
[323] See further Walker, D. *A Review of Corporate Governance in UK Banks and Other Financial Industry Entities Final Recommendations The Walker Report* 2009. See also Honohan, P. *The Irish Banking Crisis Regulatory and Financial Stability Policy 2003-2008 A Report to the Minister for Finance by the Governor of the Central Bank The Honohan Report* 2010.
[324] Kirkpatrick, G. *The Corporate Governance Lessons from the Financial Crisis* OECD Publications 2009 at 1.
[325] The full set of listing rules are as follows:
Listing Rules for Main Securities Markets (equity, debt, closed ended investment funds)
Open Ended Fund Rules
ESM Rules (equity)
GEM Rules for debt
GEM Rules for funds
ASM Rules (equity)
Admission to Trading Rules (equity, debt, investment funds)
Equity Sponsor Rules (equity MSM), ESM Advisor Rules (equity ESM) and ASM Advisor Rules (equity ASM)
Investment Fund Sponsor Rules (funds)

follow before they can be admitted on the Main Securities Market. Listed companies must incorporate standards set by the ISE, in addition to the *UK Corporate Governance Code*.[326] Where these obligations are not met, the ISE can impose sanctions, which include the suspension of cancellation of a company's listing on the ISE.[327]

The Irish Stock Exchange (ISE) recognised the importance of the *UK Code*[328] and decided in order for Ireland's governance standards to be received well internationally they opted for Ireland to incorporate the *UK Code*.[329] The ISE was influenced by the fact that many Irish listed companies have a primary listing on the London Stock Exchange. This was the decision taken in 1999 when the ISE firstly decided to implement UK codes when they applied the *Combined Code*[330] to their listing rules. It is not surprising that this was the decision taken by the ISE as the UK codes were receiving worldwide accreditation.[331] It is interesting that the ISE decided to apply the UK Code after the Irish Stock Exchange had only become independent from the UK in 1995 after merging with it in 1973.[332]

The ISE was not prepared to separate corporate governance from the UK as the decision had to be made in 2010 whether the UK standards would be applied to Irish listing rules.[333] At that time the FRC revised the UK corporate governance standards for listed companies with the notable feature of changing the name of the *Combined Code* to the *UK Corporate Governance Code.*[334] The option taken by the ISE in 2010 was to annex to the Listing Rules of *the Combined Code*.[335] The effect of this ensured that the standards followed by UK listed companies were also followed by companies on the Main Securities Market (MSM) of the ISE. This was an opportunity to introduce codes unique and exclusive for

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UK Corporate Governance Code (equity MSM)
Rules for Member Firms (trading rules)
Market Parameters to the Rules for Member Firms (trading parameters).

[326] Supra note 256.
[327] See further ISE Main Securities Market Listing Rules 2016 p. 6.
[328] Supra note 326.
[329] Supra note 281 at Appendix C.
[330] Supra note 318.
[331] Irish Stock Exchange *Consultation Paper Consultation on changes to the ISE Listing Rules relating to Corporate Governance* (2010).
[332] See further www.ise.ie/About-Us/History/ Last accessed June 2017.
[333] Supra note 331.
[334] Financial Reporting Council (UK) *Consultation on the revised UK Corporate Governance Code* 2009.
[335] Supra note 281 at Appendix C.

companies listed on the ISE and perhaps it can be seen as a wasted opportunity. However, this chance was not seized for a number of different reasons. It was considered that the introduction of a stand-alone Irish code might comprise the creditability as the *UK Code* was so well recognised and received internally.[336] Corporate governance codes set in the UK had received worldwide recognition as acceptable standards.[337] Many listed companies in the UK have a premium listing which means they exceed the minimum level of compliance regulations and corporate governance standards and so this ensures that there is the highest level of compliance. To gain premium listing status the company must provide:

"A statement of how the listed company has applied the Main Principles set out in the UK Corporate Governance Code in a manner that would enable shareholders to evaluate how the principles have been applied. There is an obligation to comply or explain against that Code. It also requires the making of a corporate governance statement in the directors' report covering the governance code to which the issuer is subject in relation to the financial reporting process and certain details of share capital and requires description of internal control and risk management systems and composition of committees." [338]

Tullow Oil Plc and Scotland's Energy Assets Group Plc are both examples of companies with premium listing on the LSE. Continuing to follow standards set in the UK promoted certainty for Irish listed companies and for those willing to invest in Irish companies who were already familiar with standards set by the UK FRC. In essence, it was considered that introducing exclusive codes to Ireland would cause confusion and eventually divergence over time.[339] It was also feared that a stand-alone Irish code would cause further regulatory burden.[340] The concern was that if investors had to look to both UK standards and Irish standards this would deter investment in Irish companies. Instead the decision was taken

[336] See generally Irish Stock Exchange *Consultation Paper Consultation on changes to the ISE Listing Rules relating to Corporate Governance* (2010) and also ISE *Irish Corporate Governance Code* 2010 p. 3.
[337]Irish Stock Exchange "Feedback Statement on Proposed Changes to the ISE Listing Rules Relating to Corporate Governance" Press Release of the 29 September 2010 p. 1.
[338]Linklaters "New UK Premium and Standard Listing Regime" 2010 available at www.linklaters.com/pdfs/publications/UKListingRegime.pdf last accessed August 2017.
[339] "Feedback Statement on Proposed Changes to the ISE Listing Rules Relating to Corporate Governance" Press Release of the Irish Stock Exchange 29 September 2010 para. 2.11.
[340] Ibid para. 2.13.

by the ISE that additional Listing Rules exclusive to Ireland would be set down, whilst still fully accepting and adopting the codes set in the UK by the FRC.

Ovenden argues that this requirement for Irish listed companies to follow extra standards will impact on the reputation of Irish governance as the new rules do have the same recognition held by the *UK Code*.[341] Like other corporate governance standards, these additional rules also operated on a 'comply or explain' basis.[342] By including the requirement of 'comply or explain,' the new standards operated on the same basis as UK standards.

The *Irish Corporate Governance Annex*[343] contains additional rules for board of directors, including the appointment, retention of board members and remuneration. Explanations are required for the composition and appointment of the board and further details on how the board is to be refreshed are provided. All of these requirements bring transparency and this is clear from the wording of the following provisions:

"Issuers should provide clear descriptions on the processes surrounding appointments to the board."[344]
"Boards should provide investors with a clear understanding of the board's refreshment policy including the optimum length of service for directors and the general policies in place for board renewal."[345]
"The board should state the objective and scope of the evaluation review, the methodology applied and a justification for this methodology."[346]

[341] Ovenden "Proposed New Corporate Governance Codes in Ireland" *Chartered Accountancy Ireland* 03 September 2010. Available at http://www.charteredaccountants.ie/Members/Technical1/Corporate-Governance/Corporate-Governance-Articles/Proposed-new-corporate-governance-codes-in-Ireland---Sinead-Ovenden-FCA/ last assessed August 2017.
[342] "Irish Stock Exchange Publishes Additional New Rules in Relation to Corporate Governance" Press Release of the Irish Stock Exchange 17th December 2010.
[343] Supra note 331.
[344] Supra note 281at provision 2.2.
[345] Ibid at provision 4.1.
[346] Ibid at provision 3.1.

When deciding if the *UK Code* or a unique code to Ireland would be introduced, the ISE gave the opportunity for feedback during a consultation period.[347]

(i) Arguments in Favour of Applying the UK Code

Feedback was given from a host of interested parties including PwC, who largely agreed with implementing the *UK Code* but highlighted their concern of exclusive Irish codes as likely to be confusing and diminish the value of Irish codes.[348] Arthur Cox's response was in agreement with the concerns expressed by PwC, in particular because many of the companies listed on the ISE were also listed on the London Stock Exchange and did not consider it necessary for companies to comply with two sets of listing rules.[349]

(ii) Arguments Against Applying the UK Code

Other opinions raised concern over a missed opportunity to cement an Irish identity by having stand-alone codes. Davy saw an advantage of Ireland introducing a standalone code, in so far as it would be valuable to companies listed on markets outside of Ireland and London to adhere to their standards of their own country and not have to explain to foreign investors why they follow the *UK Code*. But Davy appreciates the recognition that is given to the *UK Code* and so recommends that where possible the Irish standards should mirror those set by the UK and diverge where necessary.[350] Professor Blanaid Clarke also agrees that a stand-alone Irish code would be beneficial particularly for setting out the level of independence of directors, as following the *UK Code* is challenging as Ireland is limited

[347] ISE Consultation Paper, Structure of the ISE Listing Regime 2010.
[348] PwC *Feedback Statement Response to ISE Corporate Governance Annex* 2010. Available at http://www.ise.ie/Regulation/ConsultationPapers/Historic_Consultation_Papers/Corporate_Governance_Annex/Responses/PwC-response.pdf, last assessed 20/04/2011.
[349] Arthur Cox, *Feedback Statement Response to ISE Corporate Governance Annex* 2010. Available at http://www.ise.ie/Regulation/Consultation-Papers/Historic_Consultation_Papers/Corporate_Governance_Annex/Responses/Arthur-Cox-response.pdf last assessed 22 May 2011.
[350] Davy *Feedback Statement Response to ISE Corporate Governance Annex* 2010 Available at http://www.ise.ie/Regulation/Consultation-Papers/Historic_Consultation_Papers/Corporate_Governance_Annex/Responses/Davy-Response-to-ISE-on-Corp-Gov-Consultation-13-8-2010.pdf, last assessed August 2017.

in this capacity, due to the size of the country and the pool of directors available to perform such duties.[351]

E. INTERNATIONAL SOES AS COMPARATORS TO IRISH SOES

Ireland very often looks to the UK for inspiration when drafting laws and principles but it is necessary to look to other jurisdictions to examine other regulatory models of governance. Research by way of comparison of accountability provisions of corporate governance standards for commercial and non-commercial SOEs and State-sponsored bodies in foreign jurisdictions has not adequately been addressed and so this research will aim to bridge this gap.[352] The contribution this thesis seeks to make is to fill a gap by offering a current, substantial and comprehensive analysis of the role of accountability within corporate governance standards in an SOE setting, having regard to existing corporate governance standards and practices. A comparative analysis of corporate governance standards is taken in the thesis with a particular focus on principles in the UK, New Zealand and Australia. These countries were selected because all three countries have recognised the requirement to introduce governance codes for State entities separate to codes for listed companies and the countries have principles and features that can add to a study on accountability for Irish SOEs. Different approaches have been taken in all three countries and the research will highlight how the approach for governance for Irish SOEs falls somewhere between the three countries.

Defining SOEs is challenging, in New Zealand SOEs are bound by the *State-owned Enterprises Act* 1986 but the legislation does not provide a definition of SOEs, instead it

[351] Clarke, B. *Consultation on changes to the ISE Listing Rules relating to Corporate Governance* 2010 Available at http://www.ise.ie/Regulation/ConsultationPapers/Historic_Consultation_Papers/Corporate_Governance_Annex/Responses/UCD-response.pdf last assessed August 2017.

[352] Existing literature focuses on different areas of SOEs but do not offer an international comparative. See further, MacCarthaigh, M. *The Corporate Governance of Commercial State-Owned Enterprises in Ireland* (Dublin 2009 IPA CPMR Research Report 9). MacCarthaigh, M. Committee for Public Management Research Report 9 *The Corporate Governance of Commercial State-Owned Enterprises in Ireland* (Institute of Public Administration Dublin 2009). McGauran, A.M., Verhoest, K, and Humphreys P. *The Corporate Governance of Agencies in Ireland* (Dublin 2005 IPA CPMR Research Report 6) and Reynolds "Public Sector Corporate Governance" (2009) 3 *Accountancy Ireland* 51.

identifies all the SOEs that are bound by the legislation.[353] The UK also moves away from trying to define SOEs and instead provides governance to government departments where the State has ownership of an entity.[354] In Australia, corporations where the State has an interest are termed 'government controlled corporations.'[355]

(1) New Zealand

New Zealand is an interesting comparison to use as SOEs have different governance structures than those in place for Irish SOEs. New Zealand has not taken a soft law approach and instead has set standards in legislation for SOEs.[356] New Zealand follows a dual ministry model, leaving two Ministers responsible for each SOE. Along with this, there is the Crown Monitoring Advisory Unit, which also monitors SOEs for the government.

Distinct from Ireland, in order to maximise the value of SOEs, in New Zealand SOEs are established as a commercial entity, with a focus on profitability.[357] Whereas as outlined in chapter one, SOEs in Ireland are not confined to commercial activities and are also established to meet social policy objectives. Entities that are established to satisfy the public interest are referred to as crown-owned companies. SOEs in New Zealand are established as limited companies and are required to provide a Statement of Corporate Intent (SCI)[358] which sets out the objectives of SOEs. Such a business plan is useful for promoting the efficiency of each SOE. SOEs in New Zealand have gone through interesting changes where the *Mixed Ownership Act*[359] has been introduced which reduce the State's stake in some SOEs to 51%.

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[353] See *State-owned Enterprise Act* 1986 New Zealand schedule 1 and 2.
[354] HM Treasury Cabinet Office (UK) *Corporate Governance in Central Government Departments: Code of Good Practice* (2005).
[355] Bottomley, S. "Regulating Government-Owned Corporations: A Review of the Issues" (1994) 54(4) *Australian Journal of Public Administration* 521 p. 521.
[356] Supra note 353.
[357] *Supra note 196* section 6.
[358] *Supra note 353* section 14.
[359] *Public Finance Mixed Ownership Act* Amendment Act no 45 2012 New Zealand.

Distinct from Ireland, SOEs in New Zealand were introduced as the economy was performing badly and it was intended that reforming and commercialising the State's trading activities would bring prosperity to the country.[360] In 1984 there was a radical revision of government resources which was aimed at reducing the country's deficit and getting better value for government spending.[361] The decision was taken to corporatise government services[362] which involved:

"Forming government-owned enterprises with clear commercial objectives, a neutral policy environment, managerial flexibility and authority over decisions, performance monitoring, and explicit transfers for non-commercial activities required by government to meet social objectives such as keeping open small, unprofitable post offices or branch railway lines."[363]

The reforming process had the objective of trying to get more output from reduced government investment, through the reforming structures, management and efficiency.[364] It sought to do so this through:

"Sharper lines of accountability, contracting, more flexible employment conditions, and accrual accounting were imposed on remaining departments. Departments were forced to meet percentage reductions in their allocated funds."[365]

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[360]Crown Ownership Monitoring Unit *A Treasury Internal Paper State-Owned Enterprises: History of Policy Development and Implementation* (New Zealand 1996) Available at http://www.comu.govt.nz/resources/pdfs/soe-pol-dev.pdf p. 7.
[361] Evans, L. Grimes, A. & Wilkinson B. "Economic Reform in New Zealand 1984-95 The Pursuit of Efficiency" (1996) 34 *Journal of Economic Literature* 1856 p. 1872.
[362] The reforming of New Zealand's was known as the 'new public management and was described as 'probably the most comprehensive and radical set of public management reforms of any OECD country.' Pollitt, C. & Bouckaert, G. *Public Management Reform: A Comparative Analysis* (Oxford University Press *S*econd Edition 2004) p. 280.
[363] Bale M. & Dale T. "Public Sector Reform in New Zealand and Its Relevance to Developing Countries" (1998) 13(1) *The World Bank Research Observer* 103 p. 104.
[364] Reddy, K., Locke S. & Scrimgeour, F. "Improving Performance in New Zealand's Public Corporations: The Effect of Governance Practices Governance" *International Journal of Policy Administration and Institution* (2011) 24(3) 517 p. 519.
[365] Supra note 361 p. 1873.

The post office service[366] was one of the early SOEs established in New Zealand under the government's corporatisation policy to improve efficiency within SOEs. Multiple functions fell under post office services, including responsibility for telecommunication and a bank network. The functions conflicted as it was responsible for operation, policy advice, regulation and marketing.[367] Three distinct SOEs were established to separate out these functions and with a drive towards efficiency, an SOE was formed for postal services, telecommunications and banking.

Contrasting to SOEs in New Zealand a significant difference in the requirements for SOEs between Ireland and New Zealand is in New Zealand with the onus on SOEs to be a successful business through efficient and competitive practices:

"The principal objective of every State enterprise shall be to operate as a successful business and, to this end, to be as profitable and efficient as comparable businesses that are not owned by the Crown.[368]

In New Zealand all SOEs are established as limited liability companies bound by the *Companies Act* 1993 and *State-owned Enterprise Act* 1986. It was thought the advantages of forming SOEs as limited liability companies would incentivise SOEs to be profitable businesses as they would be financially independent from the government. The result of this would reduce undue political interference as there would be a clear division of responsibilities on both SOEs and the government.[369]

SOEs in New Zealand are required to be a successful business, a good employer; and an organisation that exhibits a sense of social responsibility by having regard to the interests of the community in which it operates and by accommodate or encourage these when able to do so.[370] Indicating that it is not simply enough for SOEs to provide services without regard to profitability, SOEs must prove themselves as a viable and successful

[366] *Post Office Amendment Act* 1985 No 53 New Zealand.
[367] State Services Commission, New Zealand's State Sector Reform: A Decade of Change 1998. Available at http://www.ssc.govt.nz/decade-of-change last accessed August 2017.
[368]Supra note 353 section 6.
[369]Supra note 360 p. 18.
[370] Supra note 353 section 6.

corporations. What is considered a successful business is not defined in legislation but it may be reasonable to expect a successful business to be a profitable business. There is increased pressure for SOEs in New Zealand to operate in a similar way to private businesses where the State has no involvement. McKinlay points out that the director's requirement to increase shareholders wealth is necessary.[371] The reason why there has been so much pressure on SOEs to be a successful is presented by Cullen. He suggests that SOEs were initially formed as a temporary measure intended to be sold on and privatised and so ensuring that they were successful would make them more attractive to potential investors.[372] While there has been privatisation in New Zealand the government in 1999 decided that SOEs which were performing well would be retained by the State, and so the 'long term hold' policy was introduced and reduced the amount of SOEs that were privatised.[373] The requirement to be a successful business remains for SOEs and so New Zealand considers it important to run SOEs as close as possible to private limited companies:

"The principal objective of an SOE is to operate as a successful business and to be as profitable and efficient as comparable businesses that are not owned by the Crown."[374]

More recently the government has introduced the *Public Finance (Mixed Ownership Model) Amendment Act* 2012. In a move to raise capital for the country shares in SOEs will become available to the extent that the State will only control 51% of the effected SOEs.[375] Air New Zealand currently operates under the mixed ownership structure where the Crown owns 51% of the shares. With Air New Zealand the State invested in the company when it

[371] McKinlay, D. "Turn of the Century, Change in New Zealand's Public Enterprises" (2002) 2(1) *Public Finance and Management* 30 at 48.
[372] Cullen, M. 'Cullen at Induction Seminar for SOE Directors' (2003) The New Zealand Government. Available at http://www.beehive.govt.nz/speech/cullen-induction-seminar-soe-directors last accessed August 2017.
[373] Luke, B. "Examining Accountability Dimensions In State-Owned Enterprises" (2010) 26(2) *Financial Accountability & Management* 134 p. 140.
[374] Controller and Auditor General Central Government: Results of the 2010/11 Audits (Volume 2) (2012) at para 2.3.
[375] *Public Finance (Mixed Ownership Model) Amendment Act* 2012 New Zealand. *See also* Ryall, T. "Mixed Ownership Model Bill has First Reading" 8 March 2012. Available at http://www.beehive.govt.nz/release/mixed-ownership-model-bill-has-first-reading last accessed August 2017.

got into severe financial difficulty, so as to prevent it from going bankrupt.[376] It appears that the mixed ownership model of State and non-State investment is happing for the opposite reasons, it is not the SOE that is in financial difficulty but rather the State needs to raise capital while still retaining majority ownership:

"As there often is no equivalent enterprise where the State is not a significant shareholder to use as a yardstick of comparison for the economic success, or the SOE does not have a share price that reflects the performance of the SOE, the SOE must operate in such a way "that output must be produced at least cost and the value or cost of the output must at least match the cost of its supply." [377]

State enterprises that are not mandated to operate on a commercial basis in New Zealand are known as crown-owned companies, for example, Housing New Zealand Limited, which provides housing services for people with housing needs.[378] As crown-owned entities are not expected to be profitable, their principle aim was for social objectives rather than maximising a return for shareholders. On this basis methods other than analysing financial return will be required to monitor and scrutinise the performance of the entity. Very often profitability should not be a central feature for all SOEs as it is not the sole objective for public enterprises, rather it should be monitored that public interest motives are considered and met and that entities are run efficiently.

(2) Australia

Corporate governances of SOEs in Australia will also be examined. The structure of SOEs in Australia is similar to SOEs in New Zealand. While there is legislation in place for SOEs this is more fragmented as the different States in Australia introduced their own legislation. It will be useful to compare the difference in codes between the different

[376] Duncan G. & Chapman, J. "New Millennium, New Public Management and the New Zealand Model" (2010) 69(3) *Australian Journal of Public Administration* 301 p. 304.
[377] Supra note 360 p. 8.
[378] *Housing Corporation Amendment Act* 2001.

States. In addition to legislation there are governance standards that SOEs implement where accountability and independence are central features of the codes.[379]

In Australia there is a more fragmented approach to establishing SOEs, termed in Australia as Government-owned corporations (GOC).[380] Australia became a federation in 1901[381] with six self-governing States; Queensland, New South Wales, Victoria, Tasmania, South Australia, and Western Australia. There is no single piece of legislation governing SOEs as there is in New Zealand, as in Australia different States take responsibility for governing their own SOEs. Many SOEs in Australia are established by *Commonwealth Authorities and Corporations Act* 1997 (CAC Act). SOEs where the government has a controlling interest are bound by this Act,[382] SOEs in Australia can also be established as corporations and will be governed under company law as either a limited or an unlimited corporation. Where the government does not have the controlling interest in the SOE, it is bound by the *Corporations Act* 2001. SOEs can also be established by ministers or through other government agencies.[383] SOE are introduced as a monopoly or can enter the market and provide competition. Non-commercial entities in Australia are referred to as a Government Business Enterprise (GBE). For example, the Defence Housing Authority was established to provide housing and related services to Defence members and their families.[384] Such entities are governed by the *Public Governance, Performance and Accountability Act* 2013, which imposes specific duties on the board relating to the use and management of resources.

There is a disjointed approach to legislating for SOEs as different States in Australia have introduced separate legislation. New South Wales enacted the *State Owned Corporations Act* 1989, which is modelled on *New Zealand's State-Owned Enterprises Act* 1986. There

[379] Audit Office of NSW *Australian Performance Report: Public Sector Corporate Governance: Corporate Governance - Volume One: in Principle* (1997).
[380] The corporatisation of public sector entities became known as GOCs, the terms has a narrower scope than SOEs as it deals only with corporations. The Commonwealth Authorities and Companies Act 1997 (CAC Act).
[381] See further http://www.australia.gov.au/about-government/how-government-works/federation last accessed 8 June 2017.
[382] *Commonwealth Authorities and Companies Act* 1997 Australia section 34.
[383] *Public Service Act* 1999 Australia. See Bottomley "Regulating Government-Owned Corporations: A Review of the Issues" (1994) 53(4) *Australian Journal of Public Administration* 521 p. 522.
[384] Established under the *Defence Housing Authority Act* 1987.

is the *Victorian State Owned Enterprises Act* 1992, and Queensland introduced the *Government Owned Corporations Act* 1993. There are 12 GOCs in the State of Queensland[385] and there is significant legislation and guidelines that have been implemented for these 12 SOEs. Perhaps this is a reflection not on the quantity of SOEs but an indication of the value they bring the State as they have an estimated value of $44 billion.[386] The core legislative basis of SOEs is the *Government Owned Corporations Act* 1993[387] and key guidelines include the *Government Owned Corporations Regulation* 2004,[388] *Cost of Capital Principles - Government Owned Corporations,*[389] *Investment Guidelines for Government Owned Corporations*[390] and the *Code of Practice for GOC Financial Arrangements.*[391] SOEs in Queensland are either established as statutory SOEs or as a company SOE where the *GOC Act*[392] applies to both classes of GOC but the latter GOC is also bound by Corporations Law. A company GOC will be established where there are commercial activities, which generate their own revenue and do not rely on Government funding.[393]

(3) The UK

The UK has set the standard of corporate governance for listed companies that have been followed all over the world. Therefore it will be useful to examine the approach taken by the UK towards governance of SOEs. The UK has set out standards for entities where the State has a stake and the development of the codes will be examined along with an examination of the codes used in practice. The importance that governance will bring to public bodies is recognised in the UK by Doncaster Metropolitan Borough Council:

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[385] See Department of the Premier and Cabinet Queensland Government website. Available at https://www.premiers.qld.gov.au/publications/categories/policies-and-codes/handbooks/welcome-aboard/gov-owned-corps.aspx last accessed June 2017.
[386] As per Queensland Government http://www.ogoc.qld.gov.au/current_gocs/index.shtml last accessed August 2017.
[387] The State of Queensland Australia *Government Owned Corporations Act* 1993.
[388] The State of Queensland Australia *Government Owned Corporations Regulations* 2004.
[389] The State of Queensland Australia *Cost of Capital Principles - Government Owned Corporations* 2006.
[390] The State of Queensland Australia *Investment Guidelines for Government Owned Corporations* 2011.
[391] The State of Queensland Australia *Code of Practice for GOC Financial Arrangements* 2009.
[392] Supra note 287.
[393] McDonough, D. "Corporate Governance and Government Owned Corporations in Queensland" (1998) 10(2) *Bond Law Review* 272 p. 272.

"Good governance is about running things properly. It is the means by which a public authority shows it is taking decisions for the good of the people of the area, in a fair, equitable and open way. It also requires standards of behaviour that support good decision making – collective and individual integrity, openness and honesty. It is the foundation for the delivery of good quality services that meet all local people's needs. It is fundamental to showing public money is well spent. Without good governance councils will struggle to improve services when they perform poorly."[394]

The UK will be used as a comparator primarily by examining corporate governance for listed companies. This contributes to this research as it highlights how successful corporate governance can be when implemented on a mandatory basis.

[394] Corporate Governance Inspection Doncaster Metropolitan Borough Council 2010 Audit Commission at 3.

F. CONCLUSION

Accountability is guided by the relationship between a board and how its performance is reviewed. There are principles to be followed and if they are not implemented there should be consequences ex-post. In Europe forms of accountability reflect similar models that are in Ireland, so that the hierarchical relationship between principle and agent are characterised by monitoring and control. It is apparent that board accountability is gaining momentum, with a focus on New Post Management in European countries, which requires improved performance delivery.

This chapter has reviewed the historical context of establishment and classification of SOEs in Ireland. A comparison to SOEs internationally was made, to review how board accountability is dealt with in other countries. New Zealand offers a corporate governance framework on a legislative basis. By comparison Irish SOEs fall between this hard law approach and soft law basis, as Irish SOEs are bound by the *Companies Act*[395] but are also obligated to follow the *Code of Practice*.[396]

This chapter has focused on the key issues of corporate governance – transparency, disclosure, fairness and responsibility, which are central to improving board accountability in SOEs. These principles are the basis for strengthening board accountability. This chapter also examined the impact of corporate governance for listed companies and how those standards are influenced by standards for SOEs.

The following chapter focuses on the regulatory model for corporate governance standards, focusing on the hard versus soft law debate. The role of the regulator will be examined and address enforcement and compliance issue for governance for SOEs. Key themes of corporate governance standards for SOEs will be addressed, by examining the standards currently in place drawing comparisons between the codes for listed bodies and SOEs. Compliance and enforcement issues will also be examined. Throughout the remainder of this thesis there will also be an in-depth study of governance codes currently in place for

[395] *The Companies Act* 2014 (as amended) and predecessor Acts.
[396] Supra note 219.

SOEs to establish if codes provide a suitable governance framework for accountability. SOEs have an added responsibility as it is the taxpayer who funds them and SOEs should provide a return to society for this investment. A comprehensive examination detailing the comparisons and distinctions that should be made for corporate governance standards for listed companies and SOEs will be provided. Chapter three will compare corporate governance codes for listed companies and SOEs and set out the different requirements for both types of entities.

CHAPTER 3:
THE REGULATORY MODEL

A. INTRODUCTION

Hobbes highlighted the importance of the regulatory process in society, as without regulation Hobbes envisages a war of attack, with an outcome that no-one could benefit from.[397] Therefore, regulation has become one of the basic mechanisms which society is based upon. Regulation is the adhesive that bonds society and the onset of the BSE crisis of the 1990's highlighted the impact when regulation fails as the shortcoming of food regulation not only in Ireland but from within the EU had severe consequences.[398] Prior to this crisis regulation was found with a lack of coordination, there were a plethora of complex EU laws transposed differently in Member States which meant that standards varied between countries and over time, all contributing to the crisis reaching level it did. The onset of the crisis led to a remodelling of food regulation, initially the European Commission issued Green and White paper 1997 and 2001 to restore consumer confidence in public health. This is an example which highlights the importance of regulation.

It is easy to see the logic in the popular opinion that laws are only as good as their ability to be enforced, making unenforceable laws redundant. For example, the ability to enforce laws is what the criminal justice system is based on. When a crime is committed there are clear procedures to be followed that aim to act as a deterrent to prevent future crimes. Legally binding obligations are characterised as hard law as they are mandatory instruments for implementing the law. An alternative to this is soft law, which has a quasi-legal basis and is the underlying basis for a vast amount of corporate governance standards implemented in Ireland to date.[399] Whilst a quasi-legal basis is not synonymous with voluntary application there is a perception that laws on such basis are not as critical as laws

[397]Hobbes, T. *Leviathan* (Penguin Publishing Harmondsworth 1968).
[398]Taylor, G & Millar, M. "The Appliance of Science: The Politics of European Food Regulation and Reform" (2002) 13(4) *Public Policy and Administration* 125.
[399] Wymeersch, E. "The Enforcement of Corporate Governance Codes" (2006) 6(1) *Journal of Corporate Law Studies* 113; Kingsford Smith, D. "Governing the Corporation: The Role of Soft Regulation" (2012) 35(1) *University of New South Wales Law Journal* 378.

implemented on a hard law basis and are differentiated as soft law and considered weaker obligations.[400]

Chapter one and two addressed some of the key corporate governance features and central to this were issues dealing with accountability, transparency and responsibility. In this respect identifying a suitable regulatory model of governance it should reflect how best those principles are implemented as this is an important aspect in determining how to increase accountability within SOEs. To ensure the best outcome for a regulatory model this chapter will focus on the basis of a regulatory model, what features it should contain and the barriers that will prevent its success.

If a board is accountable for implementing governance standards it is necessary to consider the benefits and consequences of implementing standards on a hard or soft law basis. While legislation provides precisely defined boundaries, organisations implementing governance standards on a soft law basis provide more autonomy in applying governance standards. Intrinsic to this autonomy is the widely used comply or explain principle, which has a clear mantra that if governance standards are not implemented, a reason for non-compliance must be given. Therefore, a company does not have to follow all corporate governance principles contained in a set of standards, provided an explanation is provided to shareholders, stating why they have chosen not to comply with governance standards.[401] In focusing on a regulatory model of governance, the issue of whether governance principles specific to each SOE is more appropriate than a more general set of principles covering all SOEs will be examined. This will highlight if a single code of governance is sufficient to provide adequate governance to all SOEs.

It will be useful to compare how corporate governance standards are implemented in SOEs in other jurisdictions, to determine how their regulatory structure serves their SOEs and the public and to access if features can be used to increase accountability within Irish SOEs.

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[400] Galander, A. Walgenbach, P. & Rost K. "A Social Norm Perspective on Corporate Governance Soft Law" (2015) 15(1) *Corporate Governance Journal* 31; Andres and Theissen "Setting a Fox to keep the Geese-does the Comply-or-Explain Principle Work?" (2008) 14(3) *Journal of Corporate Finance* 289.

[401] Financial Reporting Council (UK) *The UK Corporate Governance Code* (2014) p. 4. See further Arcot, S. Bruno V. & Faure-Grimaud, A. "Corporate Governance in the UK, Is the Comply or Explain Approach Working?" (2010) 32(2) *International Review of Law and Economics* 193.

Throughout the chapter comparisons will be drawn from corporate governance of SOEs in the UK, New Zealand, Australia and Canada. These countries were chosen as suitable regulatory comparators as Australia and Canada have implemented a mixture of principle-based and legislative corporate governance, whereas New Zealand's governance principles are drafted solely on a legislative basis. Ireland is heavily influenced by the UK in its governance standards for listed companies and so research into UK governance for SOEs will be beneficial.

B. REGULATORY FRAMEWORK

According to Black:

"Regulation is the sustained and focused attempt to alter the behaviour of others according to defined standards or purposes with the intention of producing a broadly identified outcome or outcomes, which may involve mechanisms of standard-setting, information-gathering and behaviour-modification."[402]

Regulation is a means of attaining what is considered acceptable activity and behaviour for individuals in society seeking stability which is primarily achieved by State intervention exercising control over entities by implementing laws.[403] The main aim of regulating is setting safeguards in place to protect society. In addition to setting safeguards, Akinbami identifies other components of regulation as establishing suitable framework of rules, the role and supervisory function of regulators along with enforcement regimes are important factors to consider.[404] May describes the process by which compliance can be measured and sanctions for non-compliance as equally important.[405]

Events of the financial crisis from 2008 in Ireland changed the attitude to regulation and it needs to be redefined taking a more prudent approach. Black and Baldwin argue that

[402] Black, J. "Critical Reflections on Regulation" (2002) 27 *Australian Journal of Legal Philosophy* 1 p. 26.
[403] Eberlein, B., Abbott, K., Black, J., Meidinger, E. & Wood, S. "Transnational Business Governance Interactions: Conceptualization and Framework for Analysis" (2014) 8(1) *Regulation & Governance* 1.
[404] Akinbami, F. "Is Meta-regulation all it's cracked up to be? The Case of UK Financial Regulation" (2013) 14(1) *Journal of Banking Regulation* 16 p. 17.
[405] May, P. "Regulatory Regimes and Accountability" (2007) 1 *Journal of Regulation & Governance* 8 at 8.

implementing one regulatory strategy may prove unsuccessful.[406] They suggest that risk should be assessed and have a number of intervention strategies including detection, enforcement, performance strategies.[407] Allowing for multiple regulation strategies provides greater flexibility for a board and given SOEs can be large or specific purpose this less rigid approach may be more suitable to allow risk management to become more fluid. Hutter foresees that trying to find a balance within regulation is difficult as serious risk may be inadvertently overlooked whereas smaller risks may be over regulated.[408] This may also lead to over monitoring and leaving little flexibility with frameworks.[409] Looking at regulatory objectives, a significant aim is risk management, being able to identify risks, measure monitor and control risks from risk based techniques such as cost benefit and risk assessments.[410] Hutter identifies the difficulty this places on regulators as they may not be in a position to identify the risks, primarily due to a lack of access to information.[411] Even within data provided there may be inaccuracies or data being interpreted incorrectly.[412]

Risk management for SOEs should include adequate monitoring and reporting mechanisms and should focus on the board implementing the *Code of Practice* but there are limitation to this so it will also require the government monitoring how is has been implemented. The *Code of Practice* calls for a risk management framework that assesses risk, provides solutions and from this assurances should be provided that chosen responses are adequate.[413] This should incentivise a board to revisit the decisions on risk management mitigating potential errors. This is fundamentally an extension of accountability framework and decision making strategies for a board and in doing so the board should make timely and accurate disclosures. This should offset the duplication of reporting as risk management has a built-in accountability agenda. With risk management for SOEs, an

[406] Black, J. & Baldwin, R. "When risk-based Regulation aims Low: A Strategic Framework" (2012) 6(2) *Regulation and Governance* 131 p. 132.
[407] Ibid p. 132.
[408] Hutter "What Makes a Regulator Excellent? A Risk Regulation Perspective" (2015) *Penn Program on Regulation* 1 p. 6.
[409] Bruno V. & Claessens, S. "Corporate Governance and Regulation: Can There be Too Much of a Good Thing?" 19(4) (2010) *Journal of Financial Intermediation* 461 p. 463.
[410] Supra note 408 p. 3.
[411] Ibid p. 3.
[412] Ibid p. 4.
[413] The Department of Public Expenditure and Reform *Code of Practice for the Governance of State Bodies* (Dublin 2016) principle 7 p. 33.

important aspect is financial risk management as there is a duty that public funds are not misappropriated. The audit committee and internal audits will have primary responsibility for monitoring and reporting financial activities within SOEs. However, it is suggested that areas of risk management should not be dealt with on a fragmented basis and that all risks should be considered together.[414] Rather than assessing risks in isolation a united approach improves overall effectiveness and efficiency within the firm.[415] The area of risk management is interlinked as financial decisions will be connected to how the board make decisions and this will impact on the appropriate response and mechanisms to engage.

Becher and Fryer examine the interaction between regulation and governance. They establish that regulation supports governance by not substituting each other and so will improve monitoring.[416] Solomon refers to "new governance" as a regulatory approach encompassing benchmarking, transparency and democratic participation.[417] A corporate governance framework adds to a redevelopment of regulation that can strive for effective regulation based on process orientation regulation. Process orientation regulation has been described as

"a self-regulation based on principle-based regulation which allows entities to use regulation within their own prescribed parameters."[418]

One of the dominating issues is whether governance should be implemented on strict compliance basis or principle basis. Black outlines a "principles-based regulation avoids reliance on detailed, prescriptive rules and relies more on high-level, broadly stated rules or principles."[419]

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[414] Grace, M., Leverty, T., Phillips, R. & Shimpi, P. "The Value of Investing in Enterprise Risk Management" (2015) 82(2) *Journal of Risk and Insurance* 289 p. 289.
[415] Ibid p. 311.
[416] Becher D. & Fryer, M. "Does Regulation Substitute or Complement Governance?" (2011) 35 *Journal of Banking & Finance* 736 p. 737.
[417] Solomon, J. "New Governance, Pre-emptive Self-Regulation and the blurring of boundaries in Regulatory Theory and Practice" (2010) 2 *Wisconsin Law Review* 591 p. 592.
[418] Gilad, S. "It Runs in the Family: Meta-regulation and its Siblings" (2010) 4(4) *Regulation Governance* 485 p. 485.
[419] Black, J. "Principles Based Regulation: Risks, Challenges and Opportunities" (2007) *London School of Economics and Political Science* 3.

She differentiates between the two types of regulation as process-orientated or outcome-orientated regulation. Outcome based regulation is measured on performance whereas process-orientated regulation allows organisations set their own goals within predefined regulatory objectives.[420] As corporate governance offers a new approach to principle-based regulation an argument in favour of principle-based regulation for SOEs moves the process of regulating to achieving objectives. Rather on the basis of strict compliance with legislation, which lends itself to being more outcome based, as SOEs will either be compliant with legislation or not. But a process based regulation on a quasi-legal basis would require a high level of accountability which will be addressed in the following chapter.

Responsive regulation is premised on the ability of existing regulation being able to adopt and respond within the institutions it is regulating.[421] Responsive regulation is designed having an overall aim to deal with any unforeseen circumstances without having to draft new regulations. Regulation that is introduced in reaction to particular events could result in a regulatory framework that is fragmented and disconnected. Braithwaite endorsed responsive regulation in the form of self-regulation but only where a supervisory body was in place, which resulted in sanctions for those not engaging in self-regulation.[422] It is an overlapping regulatory framework where a form of self-regulatory and standard setting regimes can be adopted.[423] Both of these regimes requires consensus on the part of the individual for the measure to be effective as it bridging a gap by providing a solution but only when individuals assumes responsibility for implementation.

[420] Ibid.
[421] Scott, C. "Regulation in the Age of Governance: The Rise of the Post Regulatory State" (2004) *The Politics of Regulation* 1 p. 12.
[422] Braithwaite, J. *To Punish or Persuade: Enforcement of Coal Mine Safety State* (University of New York Press 1985) p. 125.
[423] Black, J."Constitutionalising Self-Regulation" (1996) 59 *Modern Law Review* 24.

(1) Legislation as a Regulatory Tool

Implementing regulations on a legislative basis provides better guidance for entities on their duties and responsibilities along with sanctions are in place described by Kingsford Smith as a 'command and control' approach to regulation.[424] There is a hierarchal structure that delegates to government departments that will bring uniformity. There is no question of power and legitimacy for regulations on a legislative basis. The key characteristic of hard law is it is legally binding thus providing better assurance regulations will be complied with. However, it may result in regulation that is inflexible and unreasonable for organisations to comply with.[425] Regulation on a legislative basis can be time consuming for governments to implement.

The OECD endorses the process of Regulatory Impact Analysis (RIA's) as an important regulatory tool.[426] This is a useful feature of regulation on a hard law basis process is ex ante which has the objectives to identify and quantify the impact of new regulations. Its aim is that by conducting research into regulation this evidence will determine the effect of regulations. RIA's are used for proposals for primary legislation, changes to existing statutory instruments and for EU Directives and Regulations.
RIA's are conducted *ex ante*, at the time regulations will be implemented but also *ex post*, after regulations have been introduced. This is important as it allows for a review of current regulations so the process can also be useful in examining current regulations. RIA's are useful in circumventing problems that may arise when regulations are put in practice. It has been noted that RIA's aim to improve transparency for both government and the public.[427] However, one of the shortfalls of the process is the requirement of a RIA is waived in the case of emergency legislation, in this instance the value of an *ex post* RIA is necessary to ensure the outcomes set out were achieved.[428] In Ireland, it would be useful

[424] Kingsford Smith, D. "Governing the Corporation: The Role of Soft Regulation" (2012) 35(1) *University of New South Wales Law Journal* 378 at 386. See also Mörth (ed.) *Soft Law in Governance and Regulation: An Interdisciplinary Analysis* (Edward Elgar Publishing Cheltenham 2004) p. 1.
[425] Kingsford Smith, D. "Governing the Corporation: The Role of Soft Regulation" (2012) 35(1) *University of New South Wales Law Journal* 378 p. 386.
[426] OECD Report on Regulatory Reform (Paris 1997).
[427] Shapiro, S. & Morrall, J.F. "Does Haste Make Waste? How Long Does It Take to Do a Good Regulatory Impact Analysis?" (2016) 48(3) *Administration & Society* 367 p. 370.
[428] Ibid.

to have a similar independent committee investigating where the shortfalls are corporate governance standards for public bodies and setting out how they can be addressed.

(2) Alternative to regulation on a legislative basis

Regulation largely comes from State authorities so there is a presumption of the State being central to regulation but an alternative to regulation based on legislation is implementing corporate governance on a quasi-legal basis. Scott looks at alternatives to legislation and comments that other mechanisms and norms can be substitutes to legislation.[429] Scott's thesis is premised on the idea that law is only one method of regulating and a legal system is not independent from the environment in which it operates. He suggests that soft law techniques can be used, for example by directing letters of comfort or guidance this shapes the behaviour to those they are directed without using formal law.[430]

Mechanisms of a quasi-legal basis frequently referred to as soft law have a binding force which is relatively weaker than conventional legal instruments.[431] There are both advantages and disadvantages in taking a soft law approach. It is argued that hard laws are more successful than soft laws as setting legislation is regarded higher with sanctions in place for non-compliance.[432] However, while legislation may reflect what the State will do regarding sanctions, this does not simultaneously guarantee that an entity will be fully compliant with legislation.[433] However, if an entity takes a proactive approach in implementing soft law, this may provide a more accurate insight of the extent of

[429] Supra note 421 p. 2.
[430] Ibid p. 16. In support of Scott see also Lessig "The Law of The Horse: What Cyberspace Might Teach" (1999) 113 *Harvard Law Review* 501.
[431] Galander, A. Walgenbach, P. & Rost, K. "A Social Norm Perspective on Corporate Governance Soft Law" (2015) 15(1) *Corporate Governance* 31; Abbott, K. & Snidal, D. "Hard and Soft Law in International Governance" (2000) 54(3) *International Organization* 421; Shaffer, G. "Hard vs. Soft Law: Alternatives, Complements and Antagonists in International Governance" (2010) 94 *Minnesota Law Review* 706; Kinley, D. & Tadaki, J. "From Talk to Walk: The Emergence of Human Rights Responsibilities for Corporations at International Law" (2004) 44 *Virginia Journal International Law* 931 p. 960.
[432] Skjaerseth, J. "Exploring the Consequences of Soft Law and Hard Law: Implementing International Nutrient Commitments in Norwegian Agriculture" (2010) 10(1) *International Environmental Agreements: Politics, Law & Economics* 1 p. 10.
See further Stewart, A. & McNulty, T. "Convergence around Concepts of Actual Board Effectiveness in Hard and Soft Law" (2015) 9(1) *Law and Financial Markets Review* 29 and also Abbott, K. & Snidal, D. "Hard and Soft Law in International Governance" (2000) 54(3) *International Organization* 421.

organisations interest in adhering to regulations as they will have chosen to follow regulations. For example, in areas of self-regulation it is clear that entities have decided to follow regulations and this allows a sense of ownership and control over regulation.[434] Although a lack of sanctions may limit the application of regulation.

Entities may also be motivated to follow soft law where is it in their interest to do, termed by Jackson as the 'rule of reputation.'[435] Jackson rightly indicates that the reputation of a company is one of its most valuable assets and so a method of maintaining this reputation is following quasi-legal instruments.[436] This sends a message that an organisation is committed to not just complying with mandatory laws but taking further steps beyond these requirements.[437] Similarly, it is not a mandatory requirement for non-listed companies to follow corporate governance standards, often an organisation will choose to apply governance standards due to the recognition and prestige that is associated with implementing recognised standards.

Dairygold Co-operative Society Limited is an example of an unlisted Irish company committed to implementing corporate governance standards.[438] The company was one of the founding members of the Plunkett Institution, which was established to promote best practice governance in co-operatives.[439] The equal importance of non-listed companies implementing governance standards is recognised by the OECD[440] and the EU Commission, as they express the view that non-listed companies will frequently face many of the same challenges and problems as listed companies.[441] Essentially, there is a shared view that implementing corporate governance standards increases investors' confidence in the enterprise and so this is a driving force for implementing standards for non-listed companies. This appears to highlight that where an entity has something to gain from

[434] Ihugba, B. "The Governance of Corporate Social Responsibility Developing an Inclusive Regulation Framework" (2014) *56*(2) *International Journal of Law and Management* 105 p. 107.
[435] Jackson, K. "Global Corporate Governance: Soft Law and Reputational Accountability" (2010) 35(1) *Brooklyn Journal of International Law* 41 p. 47.
[436] Ibid.
[437] Ibid.
[438] Dairygold Co-operative Society Limited *Annual Report* 2016 p. 20.
[439] See Plunketinstitute.ie last accessed July 2017.
[440] OECD *Corporate Governance of Non-Listed Companies in Emerging Markets* (Paris 2006).
[441] European Commission Green Paper *The EU Corporate Governance Framework* (Brussels 2011) p. 4.

implementing soft law arrangements enforcement of standards may not be an issue as organisations will be more willing to apply principles. This is true for non-listed companies who for example may be looking for investment but there are no overarching incentives for SOEs to implement soft law arrangements.

(3) Perspective of the Regulator

Setting governance standards on a soft law basis makes it easier to update and amend standards when necessary, making them more fluid. For example, quasi-legal documents may be adopted by government departments or regulatory bodies whereas amending legislation can be a lengthy process that requires approval from the Oireachtas. The *UK Code* highlights that governance standards should be frequently updated as the challenges facing a company change regularly.[442] This also recognised in the *UK Stewardship Code* where:

"The FRC expects the content of the Code to evolve over time to reflect developments in good engagement practice, in the structure and operation of the market and the broader regulatory framework."[443]

However, it is questionable if the feature of being able to update standards will serve a purpose. For example, this feature of flexibility is not utilised in Ireland as there have been no amendments or additional provisions added to the *Code for State Bodies*,[444] when updating the standards a revised set of standards replaced the previous Code rather than annotating previous versions of the Code.[445] Similarly, the *Code of Practice* was revised in 2016 rather than amending the *Code of Practice* 2009. The opportunity to update the Code in 2009 from the 2001 version could have been taken by adding or removing provisions as there was considerable overlap between the two sets of standards introduced in 2001 and 2009. The Code in 2009 provides additional provisions to support principles contained in the 2001 Code, including the requirement for commercial SOEs to report to the Minister as

[442] Financial Reporting Council (UK) *The UK Corporate Governance Code* (2010) at 1 Listing Rule 5.
[443] Financial Reporting Council (UK) *The UK Stewardship Code* (2012) p. 3.
[444] The Department of Finance *The Code of Practice for the Governance of State Bodies* (Dublin 2001).
[445] The Department of Finance *The Code of Practice for the Governance of State Bodies* (Dublin 2009).

a going concern.[446] Along with this, the Code in 2009 contains new provisions on ethics, further details on remuneration and provisions on tax compliance for SOEs.[447] MacCarthaigh highlighted that provisions of governance on equal treatment of shareholders, transparency, setting performance targets and regards for meeting targets would strengthen the Code.[448] However, the majority of the recommendations were not included in the 2009 Code. The Code in 2009 was completely reformatted and styled, which mirrored the *Combined Code* in UK as it contained a general governance principle followed by detailed provisions on how to achieve the governance principle.[449]

Regulations that allow flexibility with implementation are user friendly and soft law offers more latitude for flexibility in its application. According to Hillgenberg soft law obligations are obligations which are difficult to implement due to their lack of specificity.[450] Ellis agrees and considers a soft law approach creates objectives rather than obligations.[451] Creating objectives rather than specific rules is an advantage for governance standards, as this allows the content to cover a wider scope. The phraseology of the *Code of Practice* 2009 reflects this lack of specificity as the principles are drafted in quite general terms "the board and management should accept accountability for the proper management of the organisation."[452] The lack of commitment to providing unequivocal requirements continued throughout the Code:

"The board should meet regularly, the board should satisfy itself that all obligations are identified, the Board should have procedures to monitor and manage political conflicts of interests."[453]

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[446] Ibid principle 2.8.
[447] Ibid principle 5, 7 and 15 respectively.
[448] MacCarthaigh, M. Committee for Public Management Research Report 9 *The Corporate Governance of Commercial State-Owned Enterprises in Ireland* (Institute of Public Administration Dublin 2009) p. 79.
[449] Financial Reporting Council *The Combined Code on Corporate Governance* (London 2008).
[450] Hillgenberg, H. "A Fresh Look at Soft Law" (1999) 10(3) *European Journal of International Law* 499 p. 500.
[451] Ellis, J. "Shades of Grey: Soft Law and the Validity of Public International Law" (2012) *25*(2) *Leiden Journal of International Law* 313 p. 317.
[452] Supra note 445 principle 1.
[453] Ibid p. 3 principle 2.2.

This was improved in the 2016 code which now requires the board to meet sufficiently regularly and have a formal schedule in place.[454]

This is the approach adopted in the *UK Code*:

"There should be a clear division of responsibilities, there should be a formal and transparent procedure for the appointment of new directors to the board."[455]

The UK sets desired results and it is up to the board for State bodies to ensure this happens, when the principles are examined there is a mix of vague and more specific principles:

"The governing body should decide how value for money is measured and make sure that it has the information it needs to review value for money effectively, including information about similar organisations, for comparison. It should use this information when planning and reviewing the work of the organisation."[456]

In terms of implementing governance provisions the standards included in the *UK Governance for Public Services*[457] are similar to Irish standards in the terminology used. However, UK standards demands SOEs to implement standards; 'the governing body has to,'[458] and 'governing bodies need to be clear.'[459]

Looking to the UK, while there are governance standards in place for public bodies, the commitment to improving governance for public bodies does not compare to codes that are available in the UK for listed companies. Standards that have been introduced are on a piecemeal approach with standards set for local government bodies and specific codes entities such as the NHS, rather than having a unifying document for State bodies. While there are standards for public bodies which have been commissioned by the government

[454] Supra note 413 at provision 1.7 p. 14.
[455] Supra note 455 at principle B.2.
[456] The Independent Commission on Good Governance in Public Services (UK) *The Good Governance Standard for Public Services* (2004) p. 8.
[457] Ibid.
[458] Supra note 456 p. 9.
[459] Ibid p. 11.

the more recent development in codes for public bodies is driven from the Audit Commission, an external auditing body along with professional bodies such as The Chartered Institute of Public Finance and Accountancy (CIPFA).[460] A distinguishing feature of standards set in the UK is they are predominately set for public bodies without distinguishing the class of public body.

(4) Perspective of SOEs

This lack of rigid rules is likely to be more welcomed by those implementing governance standards as they will have more freedom in how they apply and interpret principles, providing the opportunity to apply the principles in a manner that is more responsive to their circumstances. Soft law offers flexibility in terms of providing organisations the opportunity to adopt standards to best reflect their business.[461] Hillgenberg describes this as providing a means of mutual confidence building with the benefit of not being overburdened by hard law.[462] Such flexibility will allow organisations the opportunity to experiment with governance standards so that the organisation can benefit from implementing governance standards as they will be in conjunction with their own requirements. The features of freedom of control of implementation were clear from looking at annual reports for SOEs. SOEs have the ability to decide how they will observe governance principles and how they report this varies greatly across the SOEs examined.[463]

Giving organisations greater autonomy over the application of standards will provide an opportunity to apply the 'spirit of the code' which sees beyond the literal meaning of code provisions and should achieve a higher standard of governance as an organisation is likely to go further than implementing a minimum standard. The 'spirit of the code' serves as a means of bridging the gap of executing standards where standards lack detailed provisions

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[460] Chartered Institute of Public Finance and Accountancy (1994) *Corporate Governance in the Public Services Discussion Paper* (London 1994 CIFPA). Chartered Institute of Public Finance and Accountancy (1995) *Corporate Governance: A Framework for Public Service Bodies* (London 1994 CIFPA). See also CIPFA/SOLACE (2001) - *Corporate Governance in Local Government – A Keystone for Community Governance.*

[461] Hansen, J. "Catching up with the Crowd — But Going Where? The New Codes on Corporate Governance in the Nordic Countries" (2006) 3(3) *International Journal of Disclosure and Governance* 213 at 216.

[462] Supra note 450 p. 501.

[463] See section 5 of this chapter for further analysis.

on how the principles can be achieved. In endorsing this view the *UK Corporate Governance Code* expressly makes reference to the requirement of following the spirit of the Code, "attention needs to be paid to following the spirit of the code as well as its letter."[464] However, the updated *UK Corporate Governance Code* for 2014 does not reference the spirit of the code. The *UK Code of Good Practice Guidelines for Public Bodies* highlights the importance of following the spirit of the standards as well as the letter of the standards, this will allow "the Code to be a living document and will evolve in line with best practice."[465] By contrast, there is no express reference to the requirement of following the spirit of the code in *the Governance Code for State Bodies*.[466] However, *the Code of Practice* is intended to be a guideline for SOEs and in many respects the spirit of the Code can be followed by exceeding a minimum compliance approach through genuine buy-in:

"Directors and employees of State bodies and their subsidiaries should be guided by the principles set out in meeting their responsibility to ensure that all of their activities, whether covered specifically or otherwise in this document, meet the highest standards of corporate governance." [467]

It can be argued that following the spirit of code provides a "catch all" clause. Following the letter of the code would not cover every eventuality that an organisation may face so by taking into account the premise of the code, when a situation arises that is not covered by specific principles in a set of governance standards the board can overcome this by taking an approach that is in line within the spirit of governance codes. Wymeersch points out that:

"the code's provisions should not be considered as the sole answer to a given issue, but instead invite a board to reflect and find adequate answers to the issues identified. They

[464] Financial Reporting Council (UK) *The UK Corporate Governance Code* (2010) at 2. See further Garcia, S. Chen P. & Gordon, M. "The Letter versus the Spirit of the Law: A lay Perspective on Culpability" (2014) 9(5) *Judgment and Decision Making* 479.
[465] HM Treasury Cabinet Office (UK) *Corporate Governance in Central Government Departments: Code of Good Practice* (2011) at 3.
[466] Supra note 413.
[467] Supra note 413 p. 5.

should be viewed more as containing a process, a search for the optimal solution, rather than as a ready-made answer"[468]

While this offers a subjective approach to implementing governance due to the discretion at a board's disposal, it provides a board with independence to take necessary steps to ensure actions are consistent with the overarching theme within a set of governance standards. Deciding whether to implement regulation on a soft or hard law basis will impact on the supervision and enforcement of such regulation. It will be necessary to ascertain how these objectives can be achieved.

(5) Annual Reports of SOEs

In order to ascertain how soft law techniques are used by SOEs, an examination of their annual reports may prove useful. The *Code of Practice* does not operate on a mandatory basis SOEs are required to confirm annually their compliance with the Code which includes provisions on corporate governance and how SOEs meet their obligations. The requirements include an explanation when not complying with certain provisions,[469] ensure a balanced and true position is given in the report[470] and how the board are implementing their corporate strategy.[471] The board along with external auditors are required to confirm responsibility for preparing the accounts,[472] the board's attendance at board meetings throughout the year must also be disclosed in the annual report.[473]

Taking a sample of SOEs their annual report is examined below to identify how SOEs meet their governance obligations. The SOEs selected were four commercial SOEs from Transport section (CIÉ), communications (An Post), Energy and Natural Resources (Bord Gáis) and non-commercial SOEs: Enterprise Ireland and Bord Bia.

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[468] Wymeersch, E. "The Enforcement of Corporate Governance Codes" (2006) 6 *Journal of Corporate Law Studies* 113 p. 133.
[469] Supra note 413 p. 8.
[470] Ibid principle 6 p. 31.
[471] Ibid principle 1.15 p. 15.
[472] Supra note 413 principle 1.15 p. 16.
[473] Ibid provision 4.9 p. 26.

SOE	Annual Report – Corporate Governance Provisions
CIÉ	The Annual Report 2013 provided extensive detail on how it met its governance requirements, with focus on boards' responsibilities and lists the board members and how many board meetings they attended during the year.[474] The board met monthly. The Report outlines that the board support the principles in the *Code of Practice.*[475] The Report doesn't highlight governance principles that weren't implemented by the board.
An Post	The Annual Report 2013[476] provides concise details of governance with a focus on internal controls and managing risk. It acknowledges that the board aims to give effect to the *Code of Practice*.[477]
Bord Gáis	The Annual Report 2013[478] indicates that they comply with the *UK Code* and *Irish Annex*. The report details how they comply with the *UK Code* provisions and provides an explanation for some of the provisions of the *UK Code* they do not comply with due to their lack relevance and

[474] CIÉ Annual Report 2013 p. 44.
[475] Ibid p. 42.
[476] An Post Annual Report 2013 p. 38.
[477] Ibid p. 38.
[478] Bord Gáis Annual Report 2013 p. 50.

	applicability. It clearly outlines it commitment to the *Code of Practice* and highlights that policies are continually being updated to ensure compliance with it.[479]
Enterprise Ireland Annual Report 2013	The Annual Report 2013 simply provides that the board has implemented the *Code of Practice*. This is provided through a separate report annually to the Minster.[480]
Bord Bia	The Annual Report 2013[481] references the main provisions in the *Code of Practice*, however, details are not to the same extent when compared to the commercial SOEs annual reports.

Bord Gáis exceed compliance requirements by complying with the *UK Code* and Irish Annex to an extent that it appears the *UK Code* takes priority over the *Code of Practice for State Bodies*. Its annual report details changes in the *UK Code* and how Bord Gáis is adopting its practices in line with such changes.[482]

From the sample of annual reports selected, there does not appear to be any major governance breaches as all reports are in line with what is required from the *Code of Practice*.[483] While there are no obvious governance breaches in the SOEs annual reports selected above, it would be difficult to identify major governance failures from their annual reports. This is because the Code provision that can explain the most about the governance practices of the SOEs is within Provision 8, which requests the chairperson to provide the Minister with a report to the annual report which documents how the SOE has complied

[479] Ibid.
[480] Enterprise Ireland Annual Report 2013 p. 60.
[481] Bord Bia Annual Report 2013 p. 45.
[482] Bord Gáis Annual Report 2013 p. 50.
[483] Supra note 413.

with the *Code of Practice*.[484] This additional report was provided for the purposes of this research by Enterprise Ireland, which comprised a letter confirming to Minister Bruton that Enterprise Ireland was meeting their obligations under the *Code of Practice*.[485] The additional report sent by the chairperson of Bord Gáis to the Minister was requested from Bord Gáis but they refused to provide this information for the purposes of this research.[486]

If a board is addressing how compliance is met with the Code, it is for the Minister to ensure the perspective of the board is not biased and indicate compliance has been achieved by the board, as this is a subjective process.

The above outlines there are drawbacks in implementing governance on a soft law basis as annual reports are unable to establish if governance provisions are being implemented by SOEs. A consequence of having governance on a soft law basis is how SOEs tailor their involvement with governance standards varies significantly. For example, CIÉ and Bord Gáis appears to provide a robust statement annually on how its board mets its governance commitments while Enterprise Ireland and Bord Bia simply observe the *Code of Practice* without providing clear guidance to the extent of the application of governance standards.

However, in order to understand why soft law has been so popular for corporate governance standards it is necessary to identify some of the benefits of taking a soft law approach to regulation, primarily focusing on the flexibility associated with a soft law regime.

C. ENFORCEMENT AND COMPLIANCE ISSUES

For a regulatory framework to be effective, enforcement and compliance issues are central. This is the duty of the regulator to ensure that regulations are complied with and this can be challenging when the government is the regulator. Scott points out that often the government outsources this role to executive agencies to allowing a degree of

[484] Ibid principle 8 p. 39.
[485] Letter dated 2nd July 2014 from Enterprise Ireland to Minister Bruton.
[486] Request for this report was made to the Press Office 5 January 2015 (see Appendix).

separation.[487] In the context of SOEs, the relationship between the government with SOEs is central to successful regulatory compliance. The government takes on a supervisory function and SOEs are required to confirm their application with governance provisions. This means accountability issues require prescribing actions for both government departments and SOEs, a process-based model of regulation shifts the responsibility from the government to the board but this leads to potential pitfalls. The success of governance for SOEs can be measured by determining if SOEs have implemented the *Code of Practice* but as established earlier in the chapter SOEs annual reports do not instill confidence that SOEs are engaging with governance standards.

It is clear that there are limitations of soft law questioning if it is fit for purpose, as one of the main weaknesses of soft law is the inability to ensure enforcement and compliance, indicating the contradiction of terming it as law.[488] Therefore, if it is to be used in governance model long term solutions should be put in place to strengthen its application. Certain techniques have developed to address this issue, most notably the principles of comply or explain.

(1) Limitations of the Principle of Comply or Explain

There are widespread concerns highlighting the limitations of the principle of comply or explain and to some extent the limitations of the principle cannot be overcome as it provides SOEs ample opportunity not to comply with governance principles. Ultimately, this leaves a wide gap for those who do not intend to comply with governance standards, as a soft law basis largely depends on their self-enforcement to apply governance standards. This raises the question if each SOE should have its own specific governance framework in place, as opposed to the 'one size fits all' model currently in place. To overcome the problem of one set of governance standards applying to many organisations, the principle of comply or explain is included. A substantial benefit of including this principle in a model of governance standards is the autonomy it gives a board to decide on applicable governance principles to its entity. However, the credibility of this provision is seriously

[487] Supra note 421 p. 6.
[488] Zemanek, K. 'Is the Term Soft Law Convenient?' in Hafner, Loibl, Rest, Sucharipa-Behrmann and Zemanek (Kluwer Law International the Netherlands 1998) p. 843.

undermined if a board does not provide adequate reasons for not applying particular principles as this offers an opportunity for a board to comply only with the principles that are convenient to its agenda and principles which could act as safeguards are abandoned.

Providing detailed explanations with reasons for not applying standards also forces a board to scrutinise governance principles and to review their own decisions to satisfy themselves they are acting in the best interests of the entity. If an adequate explanation for not applying with standards is not provided this raises the issue if the standards can lead to a satisfactory level of governance. The quality of explanations for not implementing governance standards can be used as a benchmark to determine if a board has actively engaged with governance standards. Therefore, an explanation should not only set out why a code provision has not been followed but also what alternative measures have been taken to ensure the overall context of governance standards is fulfilled.[489]

A recurring problem is the quality of explanations for not complying with governance principles is at a low standard. Detailed reasons as to why principles have not been complied with have not always been given.[490] There is a growing trend of a lack of detail and recycled explanations for non-compliance with the code provisions to be produced each year, a problem which has been described as the "fungus of "boiler-plate."[491] In this regard, compliance with governance standards has been measured based on the principle of comply or explain. Grant Thornton assessed levels of compliance and quality of disclosures in Ireland when measuring compliance of Irish plcs with the *Combined Code*.[492] The report was prompted by need for better explanations to be provided for not complying with governance standards:

"It is not enough to simply say non-compliance suits one's business model: stakeholders deserve to know exactly why this is the case and what arrangements ensure that, despite non-compliance, the business and their interests are protected."[493]

[489] Grant Thornton *Corporate Governance Review* (Dublin 2011) p. 7.
[490] Financial Reporting Council (UK) *The UK Corporate Governance Code* (2012) p. 3.
[491] Ibid.
[492] Grant Thornton *Corporate Governance Review* (Dublin 2011). See also *Irish Stock Exchange Listing Rules - Continuing Obligations* Chapter 6 Listing Rule 6.8.3(7).
[493] Supra note 489 p. 2.

Grant Thornton took the view that a company is fully compliant with the Code where they have provided an explanation for every principle for which there was non-compliance.[494] The report concluded that only 26% of Irish plcs listed on the main securities market were fully compliant with the Code in 2011. However, Grant Thornton found that the amount of plc's that were fully compliant with the Code was decreasing each year, going from 51% in 2009 to 36% in 2010.[495] However, if this is the only basis for measuring compliance with governance standards, the basis is flawed. There are problems with the subjective process of a board having the freedom to provide explanations it considers suitable as this leaves the threshold of governance at a low level if the explanations are not scrutinised by any other parties. In their report, Grant Thornton found that while explanations for non-compliance were improving in 2010 there was still a significant decline in the quantity of companies complying with the *Combined Code.*[496] The *ISE / IAIM Report*[497] found that there was high level of companies complying with corporate governance standards. However, compliance is measured on companies providing reasons when not complying with governance principles.[498] This suggests that companies are not incentivised to provide adequate explanations for governance standards they do not implement as compliance is measured by simply providing explanations. It is apparent the comply or explain principle alone is insufficient to measure application with governance standards. It is unclear if providing better explanations for not applying standards will result in a better application of governance codes. It is recognised that fully complying with all governance principles would be a challenging task as the board would have to:

"encompass company law, the regulatory framework, the Listing Rules, the Combined Code on Corporate Governance ethical standards, corporate strategy and government policy."[499]

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[494] Ibid p. 8.
[495] Grant Thornton *Corporate Governance Review* (Dublin 2010) p. 12.
[496] Ibid p. 12.
[497] Report commissioned by the Irish Stock Exchange and the Irish Association of Investment Managers on the Compliance and Disclosure Practices of Irish Listed Companies. *Compliance with the Combined Code on Corporate Governance by Irish Listed Companies* (Dublin 2009).
[498] Ibid p.10.
[499] Ibid p. iii.

Therefore there may be reasonable explanations why a particular organisation found particular provisions not applicable to their current circumstances. Where there is a standardised set of principles, full adherence may be an unrealistic goal but to bridge this gap, adequate reasons for not implementing particular provisions must be provided. In comparison to the UK, 52% of listed companies were considered fully compliant with governance standards in 2010.[500] However, it is not clear if the quality of explanations has been to a standard that would merit a full application of principles.

The UK has also not escaped the problem of the poor quality of the explanations given for non-compliance. The *UK Code* describes this "as so often the preferred and easy option in sensitive areas but which is essentially dead communication."[501] Moore appreciates that to an extent, boilerplate explanations are acceptable as it would be an administrative burden to qualify each principle separately.[502] However, he foresees that companies who have full compliance with governance codes may not be fully appreciated as it may be construed as simply box ticking and the fact that there is genuine compliance with codes is overlooked.[503] Therefore, it becomes clear to ensure the credibility of the principle of comply or explain it is vital that the explanation is a meaningful accurate account of why the principle was not complied with, so it is necessary to establish how this can be achieved.

(2) Strengthening Regulation for SOEs

A lack of engagement with governance on a soft law basis undermines its credibility. Bruno and Claessens argue that a balance should be sought between optimal and strong governance so that managerial initiatives are not undermined.[504] While a board assumes responsibility for governance, robust checks and reviews will assist with strengthening governance for SOEs. Regulation for corporate governance will benefit from a revised approach to the principle of comply or explain by both requiring stronger explanations for

[500] Supra note 489 p. 8.
[501] Supra note 490.
[502] Moore, M. "Whispering Sweet Nothings: The Limitations of Informal Conformance in UK Corporate Governance" (2009) 9(1) *Journal of Corporate Law Studies* 95 p. 127.
[503] Ibid.
[504] Supra note 409 p. 462.

not implementing governance principles and then ensuring these explanations are monitored. To improve the quality of governance explanations, there are many solutions offered. The ISE / IAIM recommend that explanations for non-compliance with governance standards should:

"clearly reflect the contextual environment within which the company is operating;
An indication of how and when the company will be in a position to return to compliance with the relevant code provisions should be disclosed;
In circumstances where the company considers that non-compliance with a particular provision is in the best interests of the company, a robust justification for this opinion should be provided."[505]

The recommendations outlined above should aid in moving away from the 'boiler-plate' language of the explanations for non-compliance. If entities engage better with governance standard this should result in more meaningful explanations for not implementing standards.

The ISE have also provided guidance on the quality of the explanations. It is pointed out in *the Irish Annex* that implementing governance standards is not about using the Code as a template when reporting on a company's progress. It is stressed that explanations from organisations should not be in the form of recycled material, either from previous annual reports or taken from the Code:

"Issuers should provide meaningful, evidence-based descriptions of how they apply the provisions of the Code. The ISE encourages issuers to move away from the practice of recycling descriptions that replicate the wording of the Code's provisions and provide more informative disclosures that will provide shareholders with greater insight into the company and the circumstances in which it operates."[506]

[505] Supra note 497 p. 14.
[506] Irish Stock Exchange *The Irish Corporate Governance Annex* (2010) p. 1.

This again indicates that a practice may have been followed previously which merely reduced implementing corporate governance to a 'box ticking' exercise and that it was not giving an accurate report of the company,[507] and "box ticking takes no account of the diversity of circumstances and experience among companies."[508] By moving the disclosure requirements from a voluntary basis to a more substantial declaration, it may allow the principle to work better.

This raises the issue that if explanation are going to be reviewed this brings separate compliance issues including monitoring and enforcement. It appears there is agreement within different institutions that the quality of the explanations will be improved where they are monitored. The *European Commission's Green Paper on Corporate Governance* heavily criticised the explanations given when not complying with corporate governance standards and suggested the principle of comply or explain would work better if it was better monitored.[509] They suggest this role of monitoring should fall on securities regulators, stock exchanges or other authorities.[510] The FRC responded to issues raised and defended the principle of comply or explain and consider it to be a vital component of corporate governance principles but recognise problems exist with explanations given for non-compliance and suggest that there should be an improvement in the clarity of the disclosures given.[511] The FRC's report, which investigated the explanations given for non-compliance, drew on the research carried out by Grant Thornton in the UK which found 96% of FTSE 350 complied with the aggregate Code provisions applicable to them.[512]

However, compliance appears to be measured by a general disclosure of governance principles being applied, or an explanation being provided for not complying with particular governance provisions. A high level of compliance is likely to be influenced by

[507] See further Jackson, A. "Towards a Mutual Understanding of Objectives?" Attitudes of Institutional Investors and Listed Companies to Corporate Governance Reform" (2001) 9 *Corporate Governance: An International Review* 196 at 203. See also Di Pietra, R., Gebhardt, G., Mcleay, S., & Ronen, J. "Changes in standards setting and in the governance of standard setting: are they adequate responses to recurring financial crises and accounting scandals?" (2014) 18(3) *Journal of Management & Governance* 675.
[508] *Committee on Corporate Governance, Final Report ("The Hampel Report")* (1998) para 1.13.
[509] European Commission Green Paper *The EU Corporate Governance Framework* (Brussels 2011) p. 19.
[510] Ibid.
[511] Financial Reporting Council *What Constitutes an Explanation under Comply or Explain?* Report of Discussions between Companies and Investors (UK 2012) p. 5.
[512] Ibid p. 1.

the sanctions in place for not complying with the listing rules, which can result in suspension of share trading and delisting.[513] Rather than criticising the standards of explanations given, the FRC lists out what is expected from explanations not complying with corporate governance provisions:

"Explanations should be understandable as well as persuasive. Explanations should be relevant, specific and sufficiently informative, providing enough information to those shareholders who could not simply pick up the phone and talk to the company."[514]

The FRC point out that listed companies must state how they have applied the main principles of governance standards "in a manner that would enable shareholders to evaluate how the principles have been applied."[515] This indicates that the explanations must be to a standard that will give shareholders an informed opinion of the company in a language that can be understood by shareholders. Listing rules in Australia alter the comply or explain principle slightly by expecting all principles to be followed but 'if not, why not' explanation is required.[516] This approach places an expectation for companies to provide relevant reasons for not complying with particular provisions.

It is clear than the principle of comply or explain has substantial benefit to governance principles implemented on a quasi-legal basis. In order to avail of this principle it is necessary to have monitoring mechanism in regard to explanations provided, as without this the benefits of the principle cannot be utilised.

[513] Irish Stock Exchange *Main Securities Market Listing Rules and Admission to Trading Rules* (2014) at Listing Rule 1.6.
[514] Supra note 512 p. 6.
[515] Financial Service Authority *Listing Rules* (UK) at Listing Rule 9.8.6.
[516] ASX Limited Listing Rules (at 1 January 2012) at Listing Rule 4.10.

D. REGULATORY ISSUES FOR SOES

(1) Hard versus soft law: the advantages and disadvantages within a corporate governance framework

The outcome of what is required from a governance framework will impact on the governance model chosen. When deciding on a hard versus soft law framework there are many dimensions to consider but to whom SOEs are accountable to should be central to the process. A significant drawback of soft law regulation is there is no strict obligation to comply with rules and ultimately leaves too much discretion at the board's disposal. There is an argument that hard law regulation can result in a responsive and effective framework.

A framework that aims to address the accountability deficit will require consideration if accountability will be increased if governance standards are implemented on a legislative basis or if a quasi-legal, soft law, principle approach that has been popular for governance standards is sufficient. Introducing governance requirements on a legislative basis provides a solid foundation and generally sanctions are in place if laws are derogated from. However, rules on a legislative basis can be onerous, restrictive and place a significant burden on an entity. Implementing standards on a quasi-legal basis provides greater flexibility in terms of the content of the standards and allows entities to adopt the standards, making them relevant and specific to their entity. However, this may result in enforcement and implementation issues which undermine its credibility.

Many of the criticisms associated with recommending regulation on a legislative basis are not as relevant when regulations are implemented for SOEs. Concerns such as lack of expertise and costs for implementation[517] are not as prevalent for SOEs as government departments can assist boards and cost issues are diluted where legislation applies to all SOEs. It needs to be established what soft law can offer a regulatory model that hard law basis lacks. It is clear that soft law regulation is a popular choice for corporate governance standards.

[517] Supra note 425 p 386.

Considering whether a hard or soft law approach is more suitable for SOEs there are a number of factors to deliberate. Implementing governance on a legislative basis may result in the board taking a meticulous approach to compliance to ensure they are acting within legislative parameters where there are sanctions in place for non-compliance. There may be an inclination to take a soft law approach, as such structures are in place and the board are familiar with engaging with governance in this way. However, if recommending a governance model on a soft law approach, a suitable framework must be in place to ensure governance principles are followed. If implementing standards on a soft law basis there should be additional incentives to ensure application of standards such as increased reporting requirements. Such a quasi-legal, soft law framework brings a self-regulatory aspect as the onus is on SOEs to apply governance principles.

The flexibility that is associated with a soft law basis can serve as a means of incentivising applicability of standards as SOEs can take ownership and control over their governance standards. But the ramifications of this flexibility can result in a board not being fully aware of what is required to fulfil governance commitments, based on standards set in vague terms. If a quasi-legal framework is used mechanisms should be imposed, to curtail the likelihood of a board not implementing governance principles, aiming to improve effectiveness of standards on a soft law basis.

The rules versus principles debate has been a contentious issue,[518] for governance standards due to a principle-based approach being used where there are non-binding quasi-legal structures in place, whereas a rules based approach generally has the force of the law behind it. In order to be in a position to implement principled based governance, the standards have to be interpreted by the board but this may invite intrusion from government when assessing if governance principles are implemented. Drafting governance standards may benefit from a combination of both rules and principles in

[518] Martin, G. "Corporate Governance Guidance: Rules, Principles or Both?" (2012) 1 *Chartered Accountancy Ireland* 1. Available at https://www.charteredaccountants.ie/en/Members/Technical/Corporate-Governance/Corporate-Governance-Articles/Corporate-Governance-Guidance-Rules-Principles-or-Both----Gary-Martin/ Last accessed August 2017. Arjoon, S. "Striking a Balance Between Rules and Principles-based Approaches for Effective Governance: A Risks-based Approach" (2006) 68(1) *Journal of Business Ethics* 53; Sama, L. & Shoaf, V. "Reconciling Rules and Principles: An Ethics-Based Approach to Corporate Governance" (2005) 58(1) *Journal of Business Ethics* 177.

governance standards creating a hybrid model to achieve these results, as the two areas need not be mutually exclusive of each other to strive to achieve the same outcome. In order for principle-based provisions to carry merit a minimum, threshold of governance should be implemented in the provisions and this will also allow the board to establish if governance principles have been followed.

(2) The Principle of Comply or Explain in Governance Standards for SOEs

Previous versions of the Codes of Practice for State bodies do not include the principle of comply or explain.[519] For example, the principle is not specifically referenced In the *Code of Practice for the Governance of State Bodies* 2009[520] but there is an acceptance of the principle as boards are generally expected to comply with the Code but principles that will have a disproportionate effect on smaller SOEs may be excluded.[521]

The board along with the relevant Minister has responsibility for deciding if governance principles are going to have a disproportionate effect and so must judge if the particular provision should be implemented.[522] There is a requirement for SOEs to provide reasons for non-compliance in their annual report and it also must be set out if the SOE will be in a position to comply with the governance principles in the future.[523] This seeks to ensure explanations for not complying with governance principles are adequately addressed and so SOEs should not develop the same trend as listed companies for providing recycled explanations when not complying with governance standards.[524]

However, the opportunity was taken to include the principle in the Code update in 2016.[525] This was the first reference to the principle of comply or explain.[526] Any derogations from

[519] Supra note 445.
[520] Ibid.
[521] Ibid p. 1 principle 1.1.
[522] Ibid p. 1 principle 1.1.
[523] Ibid.
[524] Supra note 509 p. 3.
[525] Supra note 413 p. 8.
[526] Supra note 413 p. 8.

the Code are only justified where agreement is reached with the relevant Minister and clearly written explanations are provided.[527]

In providing a framework for increasing accountability, how the principle of comply or explain is dealt with and if it is what level of explanations should be provided for non-compliance is required. As the principle of comply or explain has found to be misused by entities, a firmer application of the principle is required. In order for the principle to be retained, a practice of engagement and complying with standards should develop rather than the principle operating only to identify disclosures when principles have not been followed. There is a move away from the flexible approach of comply or explain for credit institutions and insurance undertakings to a stricter comply or else principle.[528] This removes the entity's discretion and the standards must be obeyed. Where the provisions are not followed, there are sanctions and fines in place. In justifying a soft law approach, derogations that the principle of comply or explain brings may not be as big of an issue for SOEs as it is for listed companies. However, the supervisory role that the government has over SOEs should mean that a board should to explain why particular provisions[529] were not followed, bringing an element of independent judgement to soft law, moving soft law away from a tool of compromise and giving it a more solid basis.

However, taking into account the wide varieties of SOEs offering flexibility within the standards can accommodate a broader spectrum of SOEs but explanations for not applying governance principles have been found to be insufficient. Perhaps moving the emphasis to 'comply and cooperate' would serve to provide a greater focus on standards and where governance standards have not been followed the board must cooperate with non-executive directors (NEDs) and the relevant Minister so they are satisfied with the board's recommendation of principles that are not relevant to the particular SOE. This should help to overcome the difficulty of providing general and weak explanations for not complying with governance standards. In addition to cooperating with NEDs, where governance

[527] Supra note 413 p. 8.
[528] The Central Bank's *Corporate Governance Code for Credit Institutions and Insurance Undertakings* (2010) was introduced from January 2011 which moves away from the comply or explain principle to comply or else principle.
[529] Supra note 445 p. 1 principle 13.

standards have not been followed, the board may also benefit from liaising with NEDs on governance principles that have been complied with. This would improve transparency and move the board from only implementing the bare minimum standards to ensure relevance and accuracy and this would also result in better engagement between the board NEDs and the Minister. So while the principle of comply or explain has resulted in weaker application of governance standards, implementing safeguards such as the requirement to not only explain where principles are not enforced to actively cooperate with relevant parties should result in better application of governance standards.

(3) The merits of SOE-specific governance versus a catch-all governing Act/Principle for SOEs

In looking to increase accountability a review of having a unique set of principles particular to each SOE should be considered. A catch-all governing act presupposes that one model will fit all SOEs and this can give rise to concern due to the diverse sectors covered by SOEs. The principle of comply or explain is recognition that one size does not fit all, so this provides an 'opt out' of complying with all standards. Specific principles drafted for each SOE is more likely to give greater clarity to a board in applying corporate governance standards but this increases the administrative burden in drafting standards for each SOE. Deciding the threshold of governance standards will be an important aspect for either approach. If a minimum standard is set too low, this will result in poor governance.

There may be a good argument that each enterprise should be afforded their own set of governance principles as such standards may prove more beneficial to SOEs. There are two means to give effect to such a proposal. The first is at the time of establishing SOEs governance standards are drafted which will apply to the particular SOE. For this method to succeed standards will have to be drafted retrospectively for existing SOEs. One of the main concerns with taking such an approach would be the administrative burden surrounding such a task.

A second means of achieving this is to provide for general standards for all SOEs with specific guidelines on how to achieve such principles to be provided at the time of establishing SOEs. Such a proposal may be more favourable as it would only require one

set of governance standards for SOEs but the standards would be adopted to suit particular SOEs. This combined approach has been implemented worldwide with certain countries choosing to mix both options where general principles are provided and this is then qualified with further principles specific to individual SOEs. This approach has been taken in Canada and Australia. Distinct from this, deciding between these two options does not exist for listed companies as all companies are bound by the same Code,[530] therefore, governance derives largely from a single code of governance for listed companies but with supporting codes such as the UK Stewardship Code for investors.[531] It will be useful to compare *the UK Code* to Irish standards currently in place for SOEs. This will highlight the limitations of having a catch-all governing act, if a single code is justified to cover the spectrum of SOEs or if it is necessary for specific principles to be introduced for each SOE.

(4) How SOE Specific Governance and Catch-all Governance Act/Principles is achieved

As States have taken different approaches when drafting catch-all governance for SOEs or taking the opportunity for implementing governance specific to SOEs, approaches taken by other countries will be examined.

Canada makes an interesting use of corporate governance principles for SOEs. Rather than implementing a single stand-alone governance code, each SOE when established has governance standards included in their enabling legislation. This highlights two key features of governance standards for Canadian SOEs; their corporate governance framework is on a legislative basis and standards are specific to each SOE. In addition to this, extra governance principles are contained in the *Financial Administration Act* 1985 (FAA) which sets out further detailed provisions which focus on control and accountability, with the exception of SOEs of a cultural nature all SOEs are also bound by the provisions in the FAA.

[530] Financial Reporting Council (UK) *The UK Corporate Governance Code* (2012).
[531] Supra note 443.

Australia is an example where both approaches are taken as governance is provided on a catch all basis for SOEs on a national level and at a regional level different States have implemented additional governance requirements. For example, Queensland introduced the *Government Owned Corporations Act* 1993. At a national level Australia has introduced the *Better Practice Guides*[532] which is set by the Australian National Audit Office. The guides are unique in their format, as volume one contains general principles of corporate governance and volume two sets out more specific principles. The advantages of the two sets of standards is volume one contains a general principles, with volume two containing specific principles for particular entities and it recommended that the second set of principles should be updated when necessary.[533]

Volume one sets out general principles of public sector governance which mirrors other governance standards including those set in Ireland by requiring accountability, transparency and integrity from the board.[534] Volume two of *the Better Governance Guides* contains eight different papers giving guidance to the following public sector entities:

- "No. 1: Public Sector Governance and the Individual Officer
- No. 2: Potential Conflicts in the Governance of Commonwealth Authorities and Companies (CAC) Bodies
- No. 3: CAC Boards
- No. 4: Executive Boards in Financial Management and Accountability Agencies
- No. 5: Monitoring Board Performance
- No. 6: Conflicts of Personal Interest and Conflicts of Role
- No. 7: Cross-Agency Governance
- No. 8: Summary of Current Legal Requirements that may be Applicable to CAC and FMA Bodies"[535]

[532] Australian National Audit Office (ANAO) *Public Sector Governance: Better Practice Guide* Volume 1 and Volume 2 (2003).
[533] Audit Office of NSW *Australian Performance Report: Public Sector Corporate Governance: Corporate Governance - Volume Two: in Principle* (1997) p. 1.
[534] Audit Office of NSW *Australian Performance Report: Public Sector Corporate Governance: Corporate Governance - Volume One: in Principle* (1997) p. 8.
[535] Supra note 533.

Both volumes of the governance guides ensure that there are significant governance principles in place for SOEs. In contrast to this, New Zealand opted for enacting specific legislation for SOEs and so all SOEs in New Zealand are bound by the *State-owned Enterprise Act* 1986. This legislation aimed to bring uniformity within SOEs and cut down on regulatory procedure so that all newly formed SOEs would be bound by this Act.[536] New Zealand has focused on standardising governance rather than adopting a dual tiered approach to governance.

The UK introduced principles on a more general basis and refrained from implementing principles on a legislative basis. The *Nolan Principles*[537] are a key feature of governance for public bodies which were the result of a report commissioned by the Prime Minster in 1995. The *Nolan Principles* of good governance are "selflessness, integrity, objectivity, accountability, openness, honesty and leadership."[538] The principles are drafted on quite a general basis and offer little guidance on how the standards can be achieved.

The Good Governance Standard for Public Services (hereinafter the *UK Governance for Public Services*) was produced by The Independent Commission on Good Governance in Public Services in 2004 in an attempt at setting more substantial governance standards. The purpose of the standards was to facilitate public bodies to set a considerable standard of governance that would lead to "good performance, good stewardship of public money, good public engagement and, ultimately, good outcomes."[539]

Shortly after the *UK Good Governance in Public Services* was published, more substantial corporate governance principles were introduced with the *Corporate Governance in Central Government Departments: Code of Good Practice*[540] in 2005. The standards were extended to all arm's length bodies which covers "department's executive agencies, Non-

[536]Crown Ownership Monitoring Unit *A Treasury Internal Paper State-Owned Enterprises: History of Policy Development and Implementation* (New Zealand 1996). Available at http://www.comu.govt.nz/resources/pdfs/soe-pol-dev.pdf at 17.
[537] Supra note 456.
[538] Ibid p.13.
[539] Ibid at forward.
[540] HM Treasury Cabinet Office (UK) *Corporate Governance in Central Government Departments: Code of Good Practice* (2005).

Departmental Public Bodies and public corporations."[541] The standards of best practice of corporate governance include:

"effective leadership that has a clear vision for the Department. Effectiveness which challenges and scrutinises performance, accountability which is achieved through promoting transparency through clear and fair reporting and finally sustainability which is taking a long-term view about what the Department is trying to achieve."[542]

UK governance standards are divided into six sections which firstly outline the Minister's responsibility and Parliamentary accountability. After this, there is guidance for the role of the board and following this, guidance for board composition, board effectiveness, risk management and finally, there are standards specific for arm's length bodies. The UK has not streamlined governance for SOEs with the standards formed on a piecemeal basis without significant emphasis on a structures set of governance standards that exists in other countries. Public bodies in the UK are still required to implement the Nolan Principles.

Countries favour different methods in choosing governance for SOEs and it appears that implementing a dual structure of governance that combines a catch-all Act along with having specific principles for SOEs is a popular approach.

[541] Ibid p. 27. The standards were later updated in 2011 to allow the standards to better reflect the changes that had occurred in society. HM Treasury Cabinet Office (UK) *Corporate Governance in Central Government Departments: Code of Good Practice* (2011) at 3.
[542] Supra note 465 p. 5.

(5) How Governance Standards for SOEs can benefit from Standards in place for Listed Companies

To provide a more accessible framework of governance to SOEs, it is worth considering how governance standards for listed companies compare to governance standards for SOEs and determine what provisions could be included in a best practice model of governance. Governance standards in place for listed companies in the UK have been widely credited as a comprehensive suitable framework of governance standards. On this basis, the *UK Corporate Governance Code*[543] cannot be ignored when addressing a framework for Irish SOEs. Indeed many provisions will have equal applicability for the two types of entities and SOEs could benefit from the rigours of governance standards that are in place for listed companies. Although the driving force and motivations between the two categories of institutions can differ significantly, this does not impinge on the requirement of governance standards to contain common themes and goals. Listed companies may primarily have commercial motivations. As discussed in chapter 1 SOEs can be founded for a number of different reasons which can also include generating revenue but they will generally have a common goal of benefiting some aspect of society. For example, FÁS was not established with the aim of generating revenue but to get people back into employment by providing training so as integrate them into a corporate environment.[544]

Examining corporate governance standards of SOEs and listed companies, the different reports for the respective organisations will be reviewed; the *Code of Practice for the Governance of State Bodies*[545] sets the standard for governance of Irish SOEs, whereas listed companies in the UK must follow the standards set in the *UK Corporate Governance Code*[546] and the *Irish Corporate Governance Annex*.[547] An examination of how these reports are drafted will give a better understanding to the different features of governance contained within them and for the consideration of whether SOEs regulation can benefit from using principles that are in place for listed companies.

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[543] Financial Reporting Council (UK) *The UK Corporate Governance Code* (2014).
[544] FÁS was established under the *Labour Services Act* 1987.
[545] The Department of Public Expenditure and Reform *Code of Practice for the Governance of State Bodies* (Dublin 2016) see also the Department of Finance *The Code of Practice for the Governance of State Bodies* (Dublin 2001 & 2009).
[546] Supra note 543.
[547] Irish Stock Exchange *The Irish Corporate Governance Annex* (2010).

(6) A comparison between the Code of Practice for the Governance of State Bodies in Ireland and the UK Corporate Governance Code

TABLE A		
	Code of Practice for the Governance of State Bodies.	**UK Corporate Governance Code.**
The principle of comply or explain	Early versions of governance standards did not expressly mentioned the principle of comply or explain but rather there was an onus on SOEs to confirm compliance with Code to Minister.[548] The updated 2016 expressly references the principle.[549]	Comply or explain principle is used, and shareholders have a right to question the explanation given for non-compliance with standards.[550]
The requirement of complying with standards	State bodies are required to comply with the standards but there is no reference to following the spirit of the standards in 2016 or earlier versions.	It is noted that complying with the standards itself will not guarantee good governance the code will only be part of their governance regime.[551]
Structure of Codes	The 2016 Code is presented in the form of a guiding	The Code is presented in the

[548] Supra note 445 p.1.
[549] Supra note 413 p. 8.
[550] Supra note 455 p. 4.
[551] Supra note 455 p. 2.

	principle supported by provisions. The 2016 Code has a distinct board focus with heading dealings dealing with the role of the board, role of chairperson, role of board members, board effectiveness, codes of conduct, financial obligations, risk management, internal control and internal audit. Relations with the Oireachtas and the Minister and remuneration.[552]	form of a guiding principle with supporting provisions. The UK Code is presented through underlying principles of accountability, transparency, probity and focusing on the success of the entity over the longer term.[553]
Board Responsibility	The board is responsible for setting a strategic plan and to ensure financial accounts give a fair and accurate position of the SOE.[554]	Board responsibility is based on accountability, transparency, probity and focus on the sustainable success of an entity over the longer term.[555]
Board election	There are no standards on re-election of board members.	It is recommended that all directors of FTSE 350

[552] Supra note 413 p. 3.
[553] Supra note 455 p. 1.
[554] Supra note 413 provision 1.15.
[555] Supra note 455 p. 1.

		companies should be elected annually.[556]
Independence	Independence is not as stringent in the Irish standards but references that potential conflicts of interest should be managed by the board.[557]	Independence is a theme that runs throughout the UK Code and the importance of independence is evident.[558]
Non-executive directors (NEDs)	NEDs feature in Irish standards with a significant duty of becoming part of the audit committee.[559]	The role of NEDs is paramount in the UK Code and it suggests that the majority of the board should consist of NEDs.[560]
Remuneration	Remuneration set by the Minister for the board and remuneration for the chairperson is set in accordance with Government policy.[561]	Remuneration is set by a remuneration committee made up of NEDs.[562]
Stakeholders/ Shareholders	Earlier versions of governance standards contained limited reference to	The value of shareholders runs throughout the standards. The

[556] Supra note 455 at principle 7.2.
[557] Supra note 413 principle 5 p. 27.
[558] Supra note 455 principle B.1.1.
[559] Supra note 413 provision 7.12 p. 37.
[560] Supra note 455 at principle B.2.
[561] Supra note 413 principle 9 p. 52.
[562] Supra note 455 at principle D.1.1.

	the requirement to act in the interest of stakeholders.[563] However, the 2016 code require SOEs to serve the interest of taxpayers and other stakeholders.[564]	board must ensure the obligations to shareholders are met.[565]

It is clear that there are common themes between standards in place for listed companies and SOEs. This is recognised for the first time in the 2016 code where SOEs are required to implement the UK code and Irish Annex where relevant.[566] It would be reasonable to conclude that elements can be referenced from the *UK Corporate Governance Code* and the *Irish Annex* in drafting a best practice model. Depending exclusively on it would results in gaps in the framework and so, a wider source of material will also have to be considered as agency, accountability stakeholder and achieving value for money are key issues for governance for SOEs.

Numerous corporate governance standards for listed companies can equally apply to SOEs. In fact, MacCarthaigh points out that it is up to SOEs to provide benchmarks on standards for private companies.[567] The characteristics of corporate governance for both entities will generally aim for the same outcome. This was the view taken by the Institute of Directors and the National Standards Authority in Ireland (NSAI).[568] However, their report found that assessing corporate governance standards differs between listed companies and SOEs, indicating that SOEs require extra governance standards.[569] These extra requirements cover such issues as the following:

[563] Supra note 445 p. 4 principle 2.13.
[564] Supra note 413 p. 5.
[565] Supra note 455 at principle E.1.
[566] Supra note 413 p. 6
[567] MacCarthaigh, M. *The Corporate Governance of Commercial State-Owned Enterprises in Ireland* (Dublin 2009 IPA CPMR Research Report 9) p. xi.
[568] The Institute of Directors and the National Standards Authority in Ireland *SWiFT 3000: 2010 Code of Practice for Corporate Governance Assessment in Ireland* (2010) p. 6.
[569] The Institute of Directors and the National Standards Authority in Ireland *SWiFT 3000: 2010 Code of Practice for Corporate Governance Assessment in Ireland* (2010) at Principle 1. See further Dowdall, J. & Martin, G. "The Quiet Revolution - Corporate Governance in the Public Sector" (2011) *Corporate Governance Journal* Chartered Accountants Ireland. Boyle, R. & MacCarthaigh, M. "Fit for Purpose?

"The requirement to confirm compliance with the relevant Minister that boards generally do not have the power to nominate members of the board compliance with centrally determined rates of remuneration for many personnel. The adoption of public sector codes on procurement and disclosure of interest."[570]

Australia recognised a difference in corporate governance standards requirements for SOEs and for listed companies. The roles and responsibilities are often more clearly defined for listed companies, but there are more complex relationships between SOEs and the government. Hence, it is important to have specific corporate governance standards for SOEs, rather than go beyond mirroring the equivalent for listed companies. This was recognised by Australian National Audit Office (ANAO):

"Public sector governance has a very broad coverage, including how an organisation is managed, its corporate and other structures, its culture, its policies and strategies and the way it deals with its various stakeholders. The concept encompasses the manner in which public sector organisations acquit their responsibilities of stewardship by being open, accountable and prudent in decision-making, in providing policy advice, and in managing and delivering programs."[571]

The Auditor General pointed out that the basis for this difference comes from the requirement for SOEs to be more efficient and effective as they aim to serve the general public.[572] This is to reflect the difference in the mandate from being profit maximisation for listed companies and welfare maximisation for SOEs. SOEs in Australia have progressed to have separate governance standards for SOEs and for listed companies and identify the standards as 'public sector governance,' which has a strong commitment in

Challenges for Irish Public Administration and Priorities for Public Service Reform" (2011) *Institute of Public Administration* Dublin.

[570] Supra note 568 principle 1.

[571] Australian National Audit Office (ANAO) Australian National Audit Office (ANAO) (2003c) at 6.

[572] Australian National Audit Office (ANAO) *Australian Communications Authority's Business Planning Workshop, Better Practice Public Sector Governance* (2003) at 6. See further *Public Service Act* 1996. Preston *Public Sector Ethics in Queensland since Fitzgerald* (1999) Australian Society of Archivists Conference available from www.archivists.org.au/events/conf99/preston.html last accessed August 2017.

ensuring the organisation is run for the benefits of residents in the country. This was recognised by Osbourne by acknowledging:

"a plural state, where multiple inter-dependent actors contribute to the delivery of public services and a pluralist state where multiple processes inform the policy making system. As a consequence of these two forms of plurality, its focus is very much upon inter-organisational relationships and the governance of processes, and it stresses service effectiveness and outcomes."[573]

In New Zealand it was apparent that separate governance principles were required due to the implications of the government ownership of SOEs:

"The Government is increasing its focus on the SOE commercial portfolio to ensure that it is being managed as effectively as possible. Crown-owned commercial activities do not face the same market scrutiny as listed companies, but we believe it is important to replicate market disciplines as much as possible. We are increasing transparency in several ways including continuous disclosure requirements for SOEs, annual public meetings and publication of performance information."[574]

Policy is required which is:

"(i) clear with SOE boards about shareholding Ministers' expectations of the companies.
(iii) to provide shareholding Ministers with a greater understanding of, and therefore confidence in, the performance of SOEs, through enhanced benchmarking;
(iii) to develop appropriate capital structures which impose financial disciplines on SOEs while ensuring they have sufficient capital to make operational investment decisions without recourse to the Crown, and
(iv) to ensure that requests for capital are considered in line with the business needs of the SOE, while recognising the Crown's preference that major investments are considered relative to other demands for capital across the Crown by

[573] Osborne, S.P. 'The New Public Governance?' 2006 8(3) *Public Management Review* 377 p. 384.
[574] Crown Ownership Monitoring Unit *Annual Portfolio Report* (New Zealand 2010) p. 2.

incorporating SOE requests for equity for significant investments into the normal budget process."[575]

On a broader stage, OECD guidelines highlight the need of standards for SOEs to be set so as to ensure a balance is found between competing interests, such as the exercise of efficient ownership as opposed to the attainment of politically motivated social objectives but at the same time, not imposing undue political influence.[576] The OECD recognises that standards set for listed companies should also be considered when setting the standards for SOEs.[577] However, problems which may be a factor for listed companies, do not exist for SOEs and so guidelines should be in place for SOEs.[578]

[575] Crown Ownership Monitoring Unit *Owner's Expectation Manual for State-Owned Enterprises* (New Zealand 2007) p. 9.
[576] *Supra note* 175 at 3.
[577] OECD *Guidelines on Corporate Governance of State-Owned Enterprises* (2005) p.10.
[578] Ibid.

E. CONCLUSION

This chapter maps the merits of the regulatory model for corporate governance standards with an emphasis on hard law versus quasi-legal structures, the role of comply or explain and the benefits of implementing governance specific to SOEs or implanting a general act applicable to all SOEs. With a focus on distinguishing features of SOEs, a regulatory model must be robust to include the wide-ranging characteristics of SOEs. Regulation is a means of providing a specific set of rules with State influence and so a framework should contain clear and specific rules so that accountability can be ensured. Regulation based on an alternative approach to legislation has been seen traditionally as having a weak legal standing that can be undermined.

However, soft law regulation can be differentiated and with appropriate structures in place governance can operate well on a soft law basis. Notably, a significant drawback of soft law is its non-binding feature but being answerable to the government will assist in ensuring governance is applied so SOEs implement standards. To do this, the principle of comply or explain should be modified to ensure corporate governance standards can fulfil the role expected. Addressing the explanations given for not implementing governance provisions, a full and detailed disclosure needs to be given by a board as there is a fiduciary duty to the public to ensure their interests are served. It is questionable if hard law would overcome the 'box ticking' approach that often becomes routine to ensure the standards are met. Giving an entity the power and flexibility to decide to what extent they are going to implement governance standards may sustain an interest in the standards, as they decide for themselves which governance standards will apply to them. Soft law offers an interim support but without penalties for non-compliance with regulation, its enforcement is undermined. Therefore, a soft law framework should operate on a "comply or suffer consequences" basis, as it is unlikely that the same level of implementation of standards can be achieved on a soft law basis without some repercussions for non-implementation. As it is not possible to achieve hard law results from soft law measures, accountability provisions are required to ensure that SOEs engage with governance principles so that they comply and cooperate.

This chapter examined governance standards in other jurisdictions that use principles and rules based approach. A catch-all governing code is drafted in general terms so that it is applicable to all SOEs, but allowing flexibility for SOEs to achieve outcomes within the remit of their own autonomy. An alternative is to establish high detailed principles that can provide further detail on how governance can be achieved. Neither approach escapes the supervisory function that is required to ensure engagement with governance standards and this should come from the government or this role should be assigned to an overseeing authority such as an ombudsman. A catch-all code may be successful for SOEs but this will require a consultation period for SOEs and government to address their governance issues and identify potential areas of weaknesses. This should also prove useful for the board to ensure correct disclosure mechanisms are in place.

Ultimately, a successful application of governance standards can be attained provided there are appropriate structures in place. The following chapter will focus on the accountability models of corporate governance, both in terms of internal and external mechanisms by identifying who a board is accountable to and how accountability can be achieved. A central problem for a framework is how transparency and disclosure mechanisms can be employed as central norms to increase accountability. Central to this is identifying the government's role in accountability and stakeholders role for SOEs.

CHAPTER 4
STRATEGIES AND MECHANISMS FOR INCREASING BOARD ACCOUNTABILITY IN SOEs

A. INTRODUCTION

The success of corporate governance standards for SOEs is dependent on its accountability model. Accountability has been defined as "being called to account for one's actions."[579] A solid basis of accountability provides a means to ensure standards are implemented and upheld. This will require external scrutiny so a supervisory function to monitor and enforce standards is necessary. Chapter 3 focused on the regulatory model of governance with an emphasis on quasi-legal regulation but this chapter will address how a quasi-legal framework can work where there is adequate accountability structure in place. This will be centred on both the role and responsibility of a board and the relevant Minster. The creditability of a governance agenda hinges on a successful model of accountability to ensure a board is acting in the best interests of SOEs and being held to account for its actions but also for the State not neglecting their role in monitoring and ensuring governance standards are being followed and implemented. The 2016 *Code of Practice* requests an ongoing dialogue between government departments and SOEs to ensure SOEs are meeting their objectives.[580]

To achieve this Boyle suggests ex-ante specifications should be in place for a board along with ex post reporting arrangements, to ensure a high level of accountability.[581] Mouton highlights the importance of an accountability framework moving from a financial focus to operational and compliance measures to include provisions on risk management, the board and management to establish a suitable framework for SOEs.[582] This chapter seeks to address how increased accountability can be achieved in SOEs; this will require looking at

[579] Muligan, R. "Accountability: An Ever-Expanding Concept?" (2000) 78(3) *Public Administration* 555 p. 555.
[580] The Department of Public Expenditure and Reform *Code of Practice for the Governance of State Bodies* (Dublin 2016) principle 8 p. 14.
[581] Boyle, R. *Governance and Accountability in the Irish Civil Service* Committee for Public Management Research Report 6 (Irish Public Administration Dublin 1998) p. 34.
[582] Mouton, C. "Internal Control in State Bodies" (2011) 43(6) *Accountancy Ireland* 23.

the different levels of accountability, disclosure mechanisms that should be in place and how monitoring and enforcement are key issues on accountability.

In Australia, accountability of SOEs is a prevailing requirement in governance standards. As well as being responsible to government, SOEs are also accountable to institutions that include the Auditor-General Commonwealth Ombudsman, the Australian Securities and Investments Commission and the Administrative Appeals Tribunal.[583]

Corporate governance in New Zealand has been a useful comparator to examine. There are two well-founded concepts for SOEs in New Zealand. The first of these is that SOEs must be run as a successful business.[584] SOEs are expected to operate as if the State involvement is neither an advantage nor disadvantage to them.[585] Similar to companies without State involvement, there is mounting pressure for SOEs to be able to operate successfully. McKinlay points out that not only should SOEs operate in a similar way to a privately owned business, SOEs must also compete against private business,[586] aligning SOEs in New Zealand very closely to private sectors.

The second concept that is apparent in SOEs is the clear responsibility on the Minister to be responsible for SOEs. There is a dual ministry structure in place, where each SOEs in New Zealand has two shareholding Ministers; one is the Minister for Finance and the other is the relevant responsible Minister.[587] Monitoring functions are divided between the two Ministers but ultimately, the responsible Minister takes the lead shareholder role and is answerable to the Parliament for SOEs. The role of the Minister of Finance as SOE shareholder is to ensure the Crown's economic and financial objectives are met.[588]

The importance of accountability in governance standards is a well-recognised principle so that individuals are responsible for their actions and are scrutinised for the decisions they

[583] Australian National Audit Office (ANAO) *Public Sector Governance: Better Practice Guide* (2003) at 21.
[584] *State-owned Enterprise Act* 1986 New Zealand section 4.
[585] McKinlay, D. "Turn of the Century Change in New Zealand's Public Enterprises Public Finance and Management" (2002) 2(1) *Public and Finance Management* 30 p. 37.
[586] Ibid p. 31.
[587] Supra note 584 section 2.
[588] See further http://www.treasury.govt.nz/statesector/commercial/guidance/owners-expectations-manual/06.htm last accessed July 2017.

make.[589] Achieving accountability will not come from isolated actions but will be attained from a series of measures at different stages. Shaoul, Stafford and Stapleton promote a strong sense of accountability for governance of SOEs based on structures of internal governance, external accountability, member conduct and public access for stakeholders.[590] It is these aforementioned structures that will provide a solid basis of accountability and this chapter will focus on these principles by investigating the role of these principles in achieving accountability.

By examining internal structures of governance, this will primarily focus on the role of the board and its duties and responsibilities in enforcing governance standards as a board is central to the accountability process for SOEs. The chapter will then examine examples of internal mechanisms from different jurisdiction aimed at increasing accountability, this will be followed by an examination of examples of external mechanisms influencing accountability, which will highlight the interaction the government and relevant Minister have in overseeing accountability within SOEs. Numerous countries implemented overseeing bodies which have varying degrees of responsibilities of scrutinising the performance of the board. The relevant bodies that will be looked at will be Australian National Audit Office (ANAO); in New Zealand, the Crown Company Monitoring Advisory Unit and for Ireland, the Auditor and Comptroller General. Member conduct is also an important aspect of accountability as this highlights how a board should behave and also how a board will be monitored which should elevate the issue of conflicts of interest faced by the board. Public access will be addressed from reviewing the position of stakeholders and how their interests should be protected.

[589] Audit Office of New South Wales *Australian Performance Report: Public Sector Corporate Governance: Corporate Governance - Volume One: in Principle* (1997) p. 8.
[590] Shaoul, J. Stafford, A. & Stapleton, P. "Accountability and Corporate Governance of Public Private Partnerships" (2012) 23(3) *Critical Perspectives on Accounting* 213 p. 220.

B. THE BOARD OF DIRECTORS AND THEIR ROLE IN ACCOUNTABILITY FRAMEWORK

A board of directors is central to an accountability framework. A board is responsible for implementing corporate governance standards. A board is a driving force as it has control and responsibility for promoting the success of organisations governance.[591] When irregular activities come to light within a corporation, the first area that comes under scrutiny is the board of directors, to examine if they are a properly functioning board. It is therefore logical that the board becomes the central internal control for measuring how governance standards are utilised in practice. The role of a director is a substantial job in any circumstances but directors for SOEs have additional permutations to consider including having to factor in the requirement of serving the interests of the public, while having to report to government departments.

Edwards and Clough suggest a board should use a combination of hard and soft mechanisms for effective governance.[592] Hard attributes as defined by them are separation of the role of chairperson and CEO, small board size and appointing non-executive directors (NEDs). They consider soft attributes as clarity in the role of the board members, good working relationships between board members and regular evaluation, making hard features easier to measure.[593] A board is directly accountable to taxpayers/shareholders for the performance of SOEs and:

"The board's key purpose is to ensure the governance and prosperity of the body by collectively overseeing the board's affairs, whilst meeting the appropriate interests of its shareholders and stakeholders."[594]

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[591] Financial Reporting Council (UK) *Report: Review of the Role and Effectiveness of Non-Executive Directors* (*The Higgs Report*) (2003) p 5.
[592] Edwards, M. & Clough, R. *Corporate Governance and Performance An Exploration of the Connection in a Public Sector Context* 2005 Issues Series Paper No. 1 in for the Corporate Governance ARC Project University of Canberra p. 14.
[593] Ibid p. 12.
[594]See the Role of Board Members, appointments to State boards, available www.stateboards.ie/stateboards/questionnaire/intro/24.htm?lang=en last accessed August 2017.

(1) Functions of the Board

The responsibilities given to the board is one of the key issues to address in assessing how accountability is managed so a board is clear on what they have to do and how they this will be achieved. To do so there are two recognised elements to the board's responsibilities:

"performance, which will improve the overall performance and the delivery of the organisation's goods, services or programs and
Conformance, so that the requirements of the law, regulations, published standards and community expectations of probity, accountability and openness are met."[595]

Directors require ability, knowledge and understanding for governance standards to be implemented. The OECD provided guidance on what is expected of boards of SOEs in terms of their responsibilities.[596] The report identifies the board as being ultimately responsible for SOEs' performance and so they should be given a clear mandate on their role and duties.[597]

The *Code of Practice for State Bodies* 2016 stipulates the duties of the board of directors for Irish SOEs. Fiduciary duties and duties applicable to directors under the *Companies Act* 2014 have been included, aligning directors' duties with those for private companies.[598] The 2016 *Code of Practice* sets out duties which the board should implement and they include:

"Monitoring of performance – the Board shall receive regular reports from the State body's management team and Board sub-committees.
The Board shall advise and support the Chairperson, Chief Executive Officer and management.

[595] Supra note 583 p. 6.
[596] OECD *Guidelines on Corporate Governance of State-Owned Enterprises* (2005a) available at www.oecd.org/dataoecd/46/51/34803211.pdf at 47 last accessed August 2017.
[597] Ibid.
[598] The Department of Finance *The Code of Practice for the Governance of State Bodies* (Dublin 2009).

The Board shall satisfy themselves that financial controls and systems of risk management are robust and defensible.
The Board shall keep itself up to date and fully informed about strategic issues and changes affecting the State body and the environment in which it operates.
The Board shall ensure that on appointment to the Board, non-executive Board members receive a formal letter of appointment setting out clearly what is expected of them in terms of time commitment, committee service and involvement outside Board meetings.
The Board shall review the results of the Board performance evaluation process that relate to the composition of the Board and corporate governance generally.
The Board shall ensure that the principles and provisions set out in the Code of Practice for the Governance of State Bodies (and any other corporate governance codes that apply to the State body) are adhered to."[599]

Compared to the *Code of Practice for State Bodies* 2009 rather than providing the board with procedures on how to achieve their duties there is an overarching reliance on economic factors; any major expenditure must reflect the long term interests of the company and such expenditure should be subject to a performance measurement system to ensure such aims are achieved.[600] Other references to board responsibility include the board's obligation to monitor and manage potential conflicts of interest.[601] This is a substantial progression from the requirements provided in the previous Code in 2001, where board members were only required to remove themselves from conflicts of interests.[602] There are further provisions that require a board to report any inconsistences from standard practices within SOEs, bringing a watchdog element to their duties but it appears that current guidelines lack sufficient detail on board's duties.

Comparing board responsibility for Irish SOEs to other corporate governance codes highlights the lower requirements for Irish SOEs. Firstly looking at *the UK Corporate Governance Code,* it comprehensively sets out the board responsibility, with a similar

[599] Supra note 580 appendix A p. 58.
[600] The Department of Finance *The Code of Practice for the Governance of State Bodies* (Dublin 2001) p. 18.
[601] Supra note 598.
[602] Supra note 600 p. 18.

responsibility of setting the strategic and risk management plans but also requires that the board ensures their obligations to shareholders are met:

"The board's role is to provide entrepreneurial leadership of the company within a framework of prudent and effective controls which enables risk to be assessed and managed. The board should set the company's strategic aims, ensure that the necessary financial and human resources are in place for the company to meet its objectives and review management performance. The board should set the company's values and standards and ensure that its obligations to its shareholders and others are understood and met."[603]

The *UK Corporate Governance Code* clearly states that "no one individual should have unfettered powers of decision"[604] whereas Irish standards are somewhat more informally phrased: "excessive influence on board decision-making by one or more individual members should be guarded against."[605]

Looking to governance principles for UK government owned entities, there are examples to guide organisations to achieve high governance standards based on using comparators for efficiency and effectiveness to services provided by similar organisation. It is also suggested that feedback from users' experience will aid the board in its decision making process.[606] To aid the board in achieving their duties the Audit Commission in the UK has proposed ways of improving governance they include:

"achieving balance,
maintaining an outward focus,
sustaining a culture of accountability and
encouraging effective relationships between those in key governance positions."[607]

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[603] Financial Reporting Council (UK) *The UK Corporate Governance Code* (2010) Listing Principle A.1.
[604] Ibid principle A Leadership p. 6.
[605] Supra note 580 provision 1.4 p. 14.
[606] The Independent Commission on Good Governance in Public Services (UK) *The Good Governance Standard for Public Services* (2004) p. 8.
[607] Audit Commission *Corporate Governance: Improvement and Trust in Local Public Services* (London 2003) at 33.

Such goals can be achieved through a balanced approach to the decision making process where there is direction and control. It is clear from these principles that there is increased focus on methods for a board to ensure it has the most suitable environment so that good governance can more easily be a feature of SOEs. UK Standards for public bodies places responsibility on a board:

"Individual governors should be held to account for their contribution through regular performance reviews. The governing body should regularly review its performance as a whole. The review should involve assessing its ways of working and achievements and agreeing an action plan to put in place any necessary improvements."[608]

Neither Irish standards for SOEs nor *the UK Code*[609] place individual responsibility on board members, instead refer to a board's collective responsibility for promoting the success and effectiveness of the entity. Irish standards state "the board is collectively responsible for leading and directing the State body."[610] However, *the UK Code* goes further by holding the board "collectively responsible for the long-term success of the company."[611]

Looking to legislation in New Zealand it provides an outline of the duties of the board of directors by providing that:

"The directors of a State enterprise shall assist the enterprise to achieve its principal objective. All decisions relating to the State enterprise shall be made in accordance with its statement of corporate intent. The board of a State enterprise shall be accountable to the shareholding Ministers."[612]

[608] Supra note 606 p. 21.
[609] Supra note 603 principle A p. 6.
[610] Supra note 580 principle 1 p. 13.
[611] Supra note 603 principle A Leadership p. 6.
[612] *State-owned Enterprises Act* 1986 New Zealand Section 5.

The Crown Company Monitoring Advisory Unit (CCMAU) was established to monitor SOEs in New Zealand[613] and adds to the duties expected of the board:

- "Ensure compliance with statutory requirements
- Develop and review company policy
- Review and approve the company's capital investments
- Appoint a CEO and monitor the CEO's performance.
- Hold management responsible for meeting the targets set in the business plan." [614]

In a move to drive efficiency in New Zealand the *State Sector Act* 1988 established chief executives as the head of SOEs who have the responsibility of:

"(a) the carrying out of the functions and duties of the department
(b) the tendering of advice to the appropriate Minister and other Ministers of the Crown
(c) the general conduct of the department
(d) the efficient, effective, and economical management of the activities of the department."[615]

An important aspect of governance in Australia is the stewardship role of the board. Its importance is recognised and calls for financial sustainability and the efficient and effective management of resources, centre to this is leadership to ensure the best use of resources. [616]

(2) Duty to Disclose Information

Providing Ministers with relevant information regarding SOEs should be a key responsibility for the board and governance principles may be improved if directors have a duty to disclose information as there will be more transparency within SOEs. While SOEs

[613] See section D (2) below for further information of the CCMAU.
[614] Crown Company Monitoring Advisory Unit *Owners Expectations Manual for State-Owned Enterprises* (New Zealand 2007) p. 40.
[615] *State Sector Act* 1988 New Zealand section 32.
[616] Supra note 589 p. 8.

are established for the public interest, the public may not be treated as a priority by the board when sharing information about SOEs. However, SOEs in New Zealand are subject to a 'no surprise' policy which puts the onus on SOEs to inform the public of material changes within SOEs. SOEs are obliged to tell the public where there are changes in "matters that may have a material effect on their commercial value disclosed in their Statement of Corporate Intent."[617] SOEs must also produce explanations on financial reports.[618] Cullen sees the value that the 'no surprise' policy as adding to shareholder confidence and that the 'no surprise' policy should include no surprises on information that is both good and bad.[619]

A significant duty placed on the board in Irish standards is to ensure that a fair and true position is provided in the annual financial reports:

"The board has a duty to ensure that a balanced, true and understandable assessment of the body's position is made when preparing the annual report and accounts of the body and when submitting these to the relevant Minister."[620]

(3) Board Appointments

The appointment to a State board is an important task and should be transparent to prevent the possibility of board appointment based on political agenda over personal merit. Simpson advocates that citizens are both shareholders and stakeholders in SOEs and have an entitlement to be part of the board.[621] Members of the public can register their interest in becoming board members for SOEs in Ireland. Appointing board members based on their own credibility is a pledge made by government and have listed competencies required for board appointments. They require individuals who have an analytical strategic perspective

[617] Supra note 614 p. 67.
[618] Ibid.
[619] Cullen, M. 'Cullen at Induction Seminar for SOE Directors' (New Zealand Government 2003). Available at http://www.beehive.govt.nz/speech/cullen-induction-seminar-soe-directors last accessed August 2017.
[620] Supra note 580 principle 6 p. 31.
[621] Simpson, S. "Boards and Governance of State-owned Enterprises" (2014) (14)2 *Corporate Governance* 238 p. 240.

to understand and critique issues along with have integrity and focus on governance.[622] Keeping in line corporate governance principles board appointments should be based on previous experience and qualifications rather than on political appointment. However, political influence in board appointments has been a contentious issue in recent times. Taoiseach Enda Kenny admitted to ensure the election of Fine Gael candidate John McNulty in a Seanad by-election he appointed him to the board of the Irish Museum of Modern Art.[623] It is reported that less than 18% of positions for the appointment to State bodies advertised were filled by members of the public with the remaining positions being filled by Ministers own choice, between the period from 2011-2013.[624]

Different countries have varied their approach on board appointment. The Irish *IOD/NSAI* Report suggests that nominations for future members for the board should not be proposed by the current board members,[625] but suggests it is the responsibility of Ministers to appoint the board.[626] However, current principles allow board members to suggest possible candidates to the Minister thereby giving the board the opportunity to decide on the composition in the board,[627] but ultimately the decision is made by the Minister. In New Zealand, the process of board appointment of SOEs allows any individual to register their interest with the CCMAU. This gives the CCMAU the opportunity to screen potential board members and assess their suitability. This will result in a wide variety of candidates as potential board members but ultimately it is the Minister that selects the board for SOEs.[628]

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[622] See the Role of Board Members, appointments to State boards, available www.stateboards.ie/stateboards/questionnaire/intro/24.htm?lang=en last accessed August 2017.
[623] Carroll, S. Minihan, M. McGee, H. and O'Regan, M. "John McNulty withdraws from Seanad byelection race as Taoiseach says he let standards slip" *The Irish Times* 30 Sept 2014.
[624] Regan "Coalition breaking own rules on State Boards" Irish Examiner 30 December 2013. See also Brennan "Public still left out as state board jobs go to ministers' candidates" *Irish Independent* 23 February 2013.
[625] The Institute of Directors and the National Standards Authority in Ireland *SWiFT 3000:2010 Code of Practice for Corporate Governance Assessment in Ireland* (2010) p. 6.
[626] MacCarthaigh, M. "Managing State-owned Enterprises in an Age of Crisis" (2010) *UCD Geary Institute Discussion Paper Series* p. 15.
[627] Supra note 580 p. 12.
[628] Crown Company Monitoring Advisory Unit *Board Appointment.* Available at http://www.comu.govt.nz/about-comu/our-role/appointments/minister-decision/ last accessed August 2017.

(4) Board Refreshment

In Ireland, chief executives of State bodies are subject to annual re-election or in some instances a three year contract will be granted.[629] The Department of Finance has set out *Guidelines on Contracts, Remuneration and Other Conditions of Chief Executives and Senior Management of Commercial State Bodies*[630] which recommends chief executives be appointed on a 12 month rolling contract for a maximum duration of seven years.[631] Chief executives are responsible to the Minister and are appointed by the Minister.[632]

The *Code of Practice* 2016 recommends that board members should not serve more than two terms, but the length of each term is not quantified.[633] The board for CIÉ for example is appointed by Government on the recommendation of current staff for a four year appointment.[634] The lack of specifying board term highlights the more relaxed attitude that is taken to board refreshments as compared to the standards for listed companies in the UK. There is an argument to be made that there isn't the same gene pool available for the roles of directors as compared to what is available in the UK but where directors remain on boards for years, it can result in low standards of governance being followed year after year. Whilst a relaxed approach to board refreshment will not itself result in poor governance, the issue is not improved by the fact that requirements of independence of the board and non-executive directors are not as stringent as the requirements in the *UK Corporate Governance Code* as outlined below.

In contrast, the *UK Corporate Governance Code* stipulates the board for listed companies is to be elected by its shareholders "all directors of FTSE 350 companies should be subject

[629] The Department of Finance "New Pay Arrangements for Chief Executives of State Bodies" Press Releases 15 July 1999.
[630] The Department of Finance *Guidelines on Contracts, Remuneration and Other Conditions of Chief Executives and Senior Management of Commercial State Bodies* (Dublin 2006).
[631] The Department of Finance *Guidelines on Contracts, Remuneration and Other Conditions of Chief Executives and Senior Management of Commercial State Bodies* (Dublin 2006) at Principle 1.17 at 5. *State Services Act* 1988 Section 37 recommended that Chief Executives serve a term of five years but may be eligible for reappointment if they meet performance based objectives.
[632] *State Services Act* 1988 New Zealand Section 35.
[633] Supra note 580 provision 4.5 p. 25.
[634] CIÉ *Annual Report* 2013 p. 42.

to annual election by shareholders."[635] Companies of a smaller size should re-elect the board at regular intervals of no more than three years, it also recommends that the board of a smaller company should be elected by the shareholders.[636] The election process for the board features heavily throughout the *UK Corporate Governance Code* "there should be a formal, rigorous and transparent procedure for the appointment of new directors to the board."[637] There are clear standards set for the appropriate time before the board should be subject to re-election:

"All directors should be submitted for re-election at regular intervals, subject to continued satisfactory performance."[638] "Non-executive directors should not serve longer than nine years before re-election."[639]

(5) Board Remuneration

Board remuneration should not be overlooked as part of an accountability framework to ensure board members are receiving remuneration that reflects their duties and responsibilities. In Ireland, prior to the updated *Code of Practice* 2016, there was very little guidance for what the Minister should consider when setting remuneration. A report conducted by CIÉ highlighted that remuneration is set by the Minister for Transport and Tourism and Sport.[640] Ireland established a Review Body on Higher Remuneration in the Public Sector to advise the Government on the pay for higher level public servants.[641] Their report aimed to provide an insight as to how remuneration should be determined. It appears where there is a private sector, comparator remuneration will be based on the lower quartile of private sector salaries.[642] Public sector pay aims to stay in line with GDP and so when GDP declined by 3% in 2008 salary payments were adjusted and reduced accordingly. The report took samples from different public office holders and in the

[635] Supra note 603 Listing Rule B.7.1.
[636] Ibid.
[637] Ibid p. 6.
[638] Ibid listing Rule B.7.
[639] Ibid listing Rule B.7.1.
[640] Supra note 634 p. 44.
[641] See http://www.reviewbody.gov.ie.
[642] Department of Finance *Report 42 Review Body on Higher Remuneration in the Public Sector* (Dublin 2007) at 29.

context of SOEs, it only addressed CEO pay. The report recommended that the CEO of SOEs should have their pay reduced by 8% to €125,655.[643]

It is recommended that bonus pay is related to performance but should be suspended due to the economic climate.[644] This indicates that a reduction in remuneration only applies to bonuses and their base salary is unaffected regardless of how they perform. While there may be an incentive for chief executive to be rewarded for their performance as they are re-elected annually, other board members are not subject to the same procedure perhaps setting pay of their base salary in relation to their performance would incentivise their individual performance. Benz and Frey indicate their disagreement with remuneration being linked to performance, they call for fixed remuneration to allow directors focus on work content rather than compensation. This should prevent distortion of financial reports that seeks to inflate directors pay based on their performance.[645]

Guidelines for listed companies provide clarity on remuneration procedures. The *UK Corporate Governance Code* requires that no "director should be involved in deciding his or her own remuneration,"[646] and so remuneration is set by a committee of NEDs "The board should establish a remuneration committee of at least three, or in the case of smaller companies two independent non-executive directors."[647] As NEDs are required to be independent this should result in fairer approach as the committee will decide what the appropriate pay, based on the performance of the directors,[648] which reflects their ability to furtherance the long-term success of the company.[649] They should avoid paying a salary more than what's necessary:

[643] Ibid p. 33.
[644] Ibid p. 6.
[645] Benz, M. & Frey, B. "Corporate Governance: What can we Learn from Public Governance?" (2007) 32(1) Academy of Management Review 92 p. 93.
[646] Supra note 603 section D: Remuneration p. 7.
[647] Ibid listing Rule D.2.1.
[648] Supra note 603 p. 22.
[649] Ibid p. 22.

"Levels of remuneration should be sufficient to attract, retain and motivate directors of the quality required to run the company successfully, but a company should avoid paying more than is necessary for this purpose."[650]

In the UK, the role of deciding remuneration for the board of listed companies is a matter for NEDs. This is not the procedure set by the Irish guidelines as there is only a requirement for NEDs to be part of the audit committee. Instead of NEDs setting the remuneration, the *Code of Practice* 2016 clarified that government policy was to be implemented for board member fees and for the first time provides guidance on CEO pay and other board members:[651]

"The board of the State body will ensure that the fees paid to chairpersons and directors will be at the rates authorised by the relevant Minister" [652] and "chairpersons and boards of all State bodies are required to implement Government policy in relation to the total remuneration of board members" [653]

Current fee rates of remuneration are available from the Industrial Relations and Pensions Division of the Department of Public Expenditure and Reform.[654] Newly added requirements include:

"the Department of Public Expenditure and Reform to be consulted prior to the implementation of any pay proposals, which could have significant implications for: general Government pay policy; the State body's finances; charges for goods or services provided; and/or other areas of the public sector."[655]

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[650] Ibid p. 7.
[651] The Department of Public Expenditure and Reform *Code of Practice for the Governance of State Bodies* (Dublin 2016) Remuneration and Superannuation Guide Principle 1 p. 3.
[652] Ibid provision 2.4 p. 7.
[653] Ibid provision 2.1 p. 7.
[654] Ibid.
[655] Ibid provision 1.4 p. 3.

These requirements give less opportunity for excessive fees to be paid to board members, and the 'one person, one salary' rule introduced in 2011 prevents public servants already receiving a salary from receiving a board fee if they are elected to the board of an SOE.[656]

In New Zealand, appointed by the relevant Minister, it is the Chair and Deputy Chair of SOEs who determine directors' fees, thereby removing any possibility of directors setting their own fees.[657]

(6) Independent Directors

It is well accepted that NEDs play an important role on any board and are vital for good governance. The Higgs Report gives a detailed outline on the role of a NED:

"Non-executive directors should constructively challenge and contribute to the development of strategy. They should scrutinise the performance of management in meeting agreed goals and objectives and monitor the reporting of performance. They should satisfy themselves that financial information is accurate and that financial controls and systems of risk management are robust and defensible and are responsible for determining appropriate levels of remuneration of executive directors."[658]

"A board is strengthened significantly by having a strong group of non-executive directors with no other connection with the company. These individuals bring a dispassionate objectivity that directors with a closer relationship to the company cannot provide"[659]

The above highlights the strong recommendation of NEDs being both independent and capable of carrying out their duties. The calibre of NEDs is reference by their knowledge, reputation, experience and their ability to interact with other directors.[660]

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[656] Ibid provision 2.2 p. 7.
[657] Supra note 612 section 17.
[658] Supra note 591para 6.1 p. 27.
[659] Supra note 591 paragraph 9.6.
[660] Editorial "Non-Executive Directors: key characteristics" *Corporate Governance* (2003) 11(4) Blackwell Publishing 287.

Independent NEDs should remove the possibility of potential conflicts of interest in the decisions they make. This may be difficult in Ireland due to the number of people serving as NEDs being limited. However, the importance of independent judgment was viewed as a higher priority to listed, rather than unlisted companies as Long, Dulewica and Gay don't see a link between independence and NEDs performance as they consider NEDs being capable of performing their duties, regardless of their independence.[661] This raises a point, if the government need their own independent advisors who represent government's interest but the consequence of such is that independence is dissolved. If such procedures were in place, independent advisors should meet privately to discuss relevant business. It has been indicated that where former executives serve as NEDs, independence will be diluted.[662]

The *Code of Practice for State Bodies* 2016 gives key responsibilities for non-executive directors. These include – setting out their functions the recommended amount of NEDs on a board and requiring the Audit Committee to comprise only of NEDs.[663] The principles require NEDs to bring independent judgement for strategy, performance, resources, appointments and standards of conducts.[664]

Compared to the *UK Code,* it gives a detailed outline of how the board can ascertain the independence of its directors. It has been suggested that NEDs may act in the interests of particular shareholders that have a significant investment in the firm[665] and so the basis of their independence will be based on whether:

"the director has been an employee of the company with the last five years,
has within the past three years a material interest in the relationship with the company,
has received remuneration from the company,

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[661] Long, T. Dulewica, V. & Gay, K. "The Role of the Non-executive Director: Findings of an Empirical Investigation into the differences between Listed and Unlisted UK boards" (2005) 13(5) *Corporate Governance* 667 p. 675.
[662] Oehmichen, J. Schult, A. & Wolff, M. "Former Executives Serving as Non-Executive Directors: Resource Channels or Ineffective Monitors" (2014) 66(4) *Schmalenbach Business Review* 438.
[663] Supra note 580 provision 7.12 p. 37.
[664] Ibid principle 3 p. 20.
[665] Mura, R. "Firm Performance: Do Non-Executive Directors Have Minds of their Own? Evidence from UK Panel Data Financial Management" (2007) *Blackwell Publishing Limited* 81 p. 82.

has any close ties with the company,
has links with other directors,
represents a significant shareholder,
has served on the board for more than nine years."[666]

Such guidelines are welcomed as they cover the majority of situations in which independence could be questioned. The *Code of Practice for State Bodies* 2016 gives minimal recognition to independence that is required in the role of NEDs with the main provision simply advocating the independent judgement that should be brought to the board.[667]

A way of overcoming the problem of lack of direction is by introducing a code of conduct and a code of ethics as advocated by Lückerath-Rovers.[668] He sees the code of conduct as a means of facilitating both the NEDs and the stakeholders in so they can place trust in the professionals of the company and help by establishing a framework from which NEDs can operate and thereby increasing their efficiency.[669]

Other board members are requested to exercise independent judgement and carry out an annual evaluation to appraise their performance.[670] Independence for SOEs is a significant issue due to conflicts of interest that arise with governments having to balance their role as owner of SOEs, along with monitoring SOEs and representing the public interest. Edwards and Clough call for a clear distinction to be made between governance and management. Management run the organisation, while governance enables and oversees management.[671]

Agency theory is a well-founded principle of governance standards, which aims to reconcile issues that arise where those who run the organisation do not have the same vigilance as those who own the organisation, as the desired outcomes may vary between

[666] Supra note 603 p. 13.
[667] Supra note 580 principle 3 p. 20.
[668] Lückerath-Rovers, M., De Bos, A "Code of Conduct for Non-Executive and Supervisory Directors" (2011) 100 (3) *Journal of Business Ethics* 465 p. 469.
[669] Ibid.
[670] Supra note 596.
[671] Supra note 592 p. 3.

the principal and the agent. For the principal-agent relationship for SOEs to be managed on a wider number of issues will not only be solely based on economic decisions.[672] This raises the issue of who is the principle and who is the agent for SOEs. If citizens are considered the ultimate owners of SOEs and the board manages SOEs on behalf of the government, as ultimate shareholder then this adds another dimension to this relationship and gives rise to the third agency problem. Lioukas et el agree that because the government has a superior and supervisory role over SOEs, this infringes on the independence of SOEs and the government add another dimension to the agency relationship.[673]

Muligan outlines that accountability is a means of imposing control,[674] but by exerting control over SOEs independence is diluted, so appropriate checks need to be in place. In New Zealand, political interference is addressed by the Advisory Unit. They recommend there should be a clear level of independence between the government and SOEs, so that SOEs have control over their own actions. But SOEs cannot be completely independent as it is the governments' duty to ensure the public interest is met and resources are achieving value for money. Therefore, independence should be at arm's length, even though SOEs are owned by the government, there is a distinction between the styles of control exercised by the government over SOEs and exercised for government departments. This distinction in control will come from the board of directors who have the responsibility of ensuring proper management and functioning of an SOE and this board is appointed by the Ministers.[675]

Irish guidelines on this area echo the need for SOEs to have certain independence by providing that the board of directors of SOEs should be independent in exercising their duties and responsibilities. This primarily can be achieved by there not being any excessive influence on boards.[676]

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[672] Supra note 590 p. 217.
[673] Bourantas, D., & Papadakis, V. "Managerial Autonomy of State-Owned Enterprises: Determining Factors" (1993) 4(4) Organization Science 645 at 646. See Further Dharwadkar, George and Brandes "Privatization in Emerging Economies: An Agency Theory Perspective Source" (2000) 25(3) *The Academy of Management Review* 650.
[674] Supra note 579 p. 563.
[675] Supra note 614 p. 7 & 8.
[676] Supra note 580 provision 1.4 p. 14.

The competing interest of political investment and involvement is addressed by MacCarthaigh. He points out that there is a lack of clear guidelines on appropriate political involvement.[677] The formal structures that are in place advise the appropriate Minister instructs the board of directors and they must report back to the Minister. However, this structure is inadequate as it fails to identify how this relationship should work in more practical terms.[678] What is necessary for a governance framework is that it must be accepted that it is wider than the government.

Independence can also be improved with transparency. Shaoul, Stafford and Stapleton suggest public access will improve transparency and they suggest that a complaints procedure should operate such as an ombudsman, which should make SOEs more responsible to stakeholders.[679] Australian governance highlights that:

"transparency is required to ensure that stakeholders can have confidence in the decision-making processes and actions of public sector organisations, in the management of their activities, and in the individuals within them."[680]

In Australia, in an attempt to strengthen corporate governance and in particular monitoring SOEs, a *Continuous Disclosure Regime* was introduced in 2009 to allow information of material relevance to be released into the public domain.[681] This theory is based on the idea that those outside the management of a company are unaware if not all information is reported and therefore, may be at a disadvantage from this lack of information, so continuous disclosure rules would bring transparency in the way SOEs operated, to mitigate some of the challenges facing SOEs and it also adds another dimension for board evaluation. Talosaga, Heatley and Howell highlight material interest is easier to identify

[677] Supra note 626.
[678] Ibid p. 16.
[679] Supra note 590 p. 222.
[680] Audit Office of NSW *Australian Performance Report: Public Sector Corporate Governance: Corporate Governance - Volume One: in Principle* (1997) p. 8.
[681] Crown Company Monitoring Advisory Unit (NZ) website at http://www.comu.govt.nz/about-comu/our-role/monitoring/continuous-disclosures.

for plcs, as they consider it to be anything which will impact on the price of the company's shares.[682] Material information is defined by the CCMAU as:

- "the fundamental terms of each material transaction entered into,
- information that has a material impact on an SOE's estimate of current commercial value as shown in its *Statement of Corporate Intent*, and
- half-year and full- year financial results, plus a brief explanation, no later than 60 days after the end of the relevant period." [683]

The continuous disclosure rules for SOEs have a quasi-legal basis making it voluntary for SOEs to comply with the regime, although compliance is expected.[684] As SOEs are not subject to the same scrutiny as listed companies, the continuous disclosure rules were introduced as a supplement and as an incentive to improve performance of SOEs. The rules are necessary as it was found that SOEs were not performing as well as their equivalent private sector companies[685] and it is a fundamental feature of SOEs that they are effective and efficient companies.[686] The continuous disclosure rules operate for plcs listed on the New Zealand Stock Exchange but it is questionable if their use is equally effective for SOEs. This is due to the fact that investors in plcs are readily able to sell on their shares once unfavourable information comes to light which may impact on the share price, whereas with SOEs, the State is generally the only shareholder and so this is not an option.[687] It therefore emerges that the continuous disclosure regime is another mechanism for SOEs to report to the responsible Minister. While there is no doubt that transparency is a vital component for good corporate governance practices, it is hard to identify the impact the disclosure rules will make to improve the performance of SOEs to make it a successful

[682] Talosaga, T., Heatley, D. & Howell, B. "Can Continuous Disclosure Improve the Performance of State-Owned Enterprises?" (2011) *New Zealand Institute for the Study of Competition and Regulation* at 5. Available at http://www.iscr.org.nz/f648,18373/18373_Continuous_disclosure_Final.pdf last accessed August 2017.
[683]Crown Company Monitoring Advisory Unit (NZ) website at http://www.comu.govt.nz/about-comu/our-role/monitoring/continuous-disclosures.
[684] Crown Company Monitoring Advisory Unit (NZ) website at http://www.comu.govt.nz/about-comu/our-role/monitoring/continuous-disclosures.
[685] Supra note 682.
[686] Supra note 580 section 6.
[687] Ibid.

business. Independence can be increased by external agencies such as NewERA that add a supervisory function to governance which should scrutinise the actions taken by the board.

(7) Board Autonomy

If a board is going to have responsibility and be accountable for governance standards they also need to be given the autonomy to practice good governance. Providing a board with autonomy will require structured risk management procedures to be in place. Risk management identifies key risks and sets procedures on how to manage such risks.

ALARM[688] is a national forum in the public sector in the UK. They have published a report *Corporate Governance in the Public Sector – The Role of Risk Management*.[689] They point out that a risk management framework is necessary as it adds to the corporate governance document by improving strategic and financial management.[690] Rather than evaluating the effectiveness of Irish SOEs strategic plan the focus is for the board is to ensure the risk management policy set by the board is adequate:

"Each State body should develop a risk management policy and the board should approve the risk management framework and monitor its effectiveness. The board should review material risk incidents and note or approve management's actions, as appropriate."[691]

To see how a board interpret governance standards the NHS in the UK will be used as an exemplar. In the UK, guidance is given to the board of SOEs in the *UK Governance Code for Public Services.*[692] It is a useful report to review as there are extensive principles on board autonomy. To understand how *UK Governance Code for Public Services*[693] has been implemented in practice, the *Local Delivery Plan* of the NHS in Lanarkshire will be

[688] Association of Local Authority Risk Managers, as its parameters widened it is now known as 'Alarm, the public risk management association'.
[689] ALARM *Corporate Governance in the Public Sector – The Role of Risk Management* (2001) 10 Business Continuity planning is regularly reviewed and tested at executive level."
[690] Ibid p. 1.
[691] Supra note 598 principle 8.1.
[692] Supra note 606.
[693] Supra note 606.

examined together as it is based on the *UK Governance for Public Services*.[694] The main provisions dealing with accountability are as follows:

(i) Clear Policies for the Board to Follow

The first provision of *UK Governance Code for Public Services*[695] stipulates that a board's autonomy cannot be achieved without clear principles for the board to follow. Providing these principles will better equip the board to perform effectively within clearly defined boundaries. It also recommends that roles within the board are reviewed regularly to ensure they are keeping in line with the company's objectives, all of which result in better governance for citizens.[696]

The NHS in Lanarkshire implemented the above provisions by stipulating the board's performance is reviewed by the Cabinet and the Chief Executive's performance is reviewed by the NHS Board Chair. Therefore, there is a dual supervisory function coming from both government cabinet and from the Board Chair. The NHS established a governance team to discharge their duties, which comprises non-executive directors.[697] Each year a report setting out the terms of reference for the board is drafted so that each committee is clear on the governance objectives that are set.

[694]"Picture of Health Document" (NHS Lanarkshire 2005) Available at http://www.nhslanarkshire.org.uk/boards/governance/Pages/purpose-outcomes.aspx last accessed August 2017.
[695]Supra note 606 p. 7.
[696] Ibid.
[697] There are also a number of other committees which aid in achieving the governance standards, these include: Audit Committee, Clinical Governance Committee, Staff Governance Committee, Remuneration Sub Committee, Property Sub Committee, Equality, Diversity and Spirituality Committee, Acute Division Operating Management Committee, North Lanarkshire Community Health Partnership Operating Management Committee, South Lanarkshire Community Health Partnership Operating Management Committee.
NHS Lanarkshire Assessment of NHS Lanarkshire Governance Arrangements. Available at http://www.nhslanarkshire.org.uk/boards/governance/Pages/default.aspx last accessed August 2017.

The NHS drafted the *Patient Focus Public Involvement Strategy*, which dealt with board duties and responsibilities.[698] It sees the board meeting their responsibilities from the following governance principles:

"NHS Board members have overall responsibility for the quality of the Board's services, and for the quality of participation in service design and delivery.
NHS Board members are responsible for ensuring that their organisation meets statutory duties and for promoting good practice by providing leadership as well as challenge.
NHS Boards are required to have in place structures and systems which manage performance across their organisation, and which provide assurance to board members of the quality of participation in services.
The actions of NHS Boards are open to public scrutiny. Demonstrating a culture in which participation is encouraged, supported, and valued can be a positive way of developing or reinforcing public confidence in the Board's staff and services."[699]

(ii) Leadership from the Top

Achieving a high standard of governance is maintained through *UK Governance Code for Public Services*[700] by promoting values for the whole organisation and demonstrating good governance through behaviour.[701] It appears that there is an ethical constituent in the standards, as it is considered that setting an example that all staff will follow will set the bar for good governance:

[698] It is pointed out that the NHS Lanarkshire is patient focused and seeks to meet the needs of is patients. Fitzpatrick *NHS Lanarkshire Patient Focus and Public Involvement Strategy 2012-2016* (UK 2013) principle 2.1.
[699] Fitzpatrick *NHS Lanarkshire Patient Focus and Public Involvement Strategy 2012-2016* (UK 2013) p. principle 6.3.
[700] Supra note 606.
[701] Ibid p.13.

"A hallmark of good governance is the development of shared values, which become part of the organisation's culture, underpinning policy and behaviour throughout the organisation, from the governing body to all staff."[702]

The UK report appreciates the value in collective responsibility but also individual responsibility by including the principle of individual governorship. Those responsible for ensuring there is adequate governance should behave in a way that exemplifies effective governance.[703] Making their duties two-fold; to be accountable for one's own actions and for the board as a whole. Transparency is achieved by the NHS Lanarkshire by holding monthly board meetings in public. While this provides a great deal of transparency, this does not imply that the decision making process will be transparent. In managing risk, there is an Executive-level Risk Management Steering Group which is chaired by the Chief Executive.[704]

(iii) Board Members who have the Capacity and Capability to Serve

Developing the capacity and capability of the governing body to be effective,[705] points to the fact that there has to be a properly functioning board in order for good governance to exist:

"Public service organisations need people with the right skills to direct and control them effectively. Governing bodies should consider the skills that they need for their particular situation."[706]

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[702] The Independent Commission on Good Governance in Public Services (UK) *The Good Governance Standard for Public Services* (2004) at 13. It is stressed that the values should be over and above legal requirements for example, anti-discrimination, equal opportunities and freedom of information legislation.
[703] The report considers individual behaviour to be important as it will ensure that the organisation is running effectively and the public will have confidence in the organisation, this is what the idea of individual governorship is based upon. The Independent Commission on Good Governance in Public Services (UK) *The Good Governance Standard for Public Services* (2004) at 14. When compared to Irish guideline the provision reads that "The board is collectively responsible for the promoting and success of the State body." The Department of Finance *The Code of Practice for the Governance of State Bodies* (Dublin 2009) p. 2.
[704] NHS Lanarkshire Assessment of NHS Lanarkshire Governance Arrangements. Available at http://www.nhslanarkshire.org.uk/boards/governance/Pages/default.aspx last accessed August 2017.
[705] Supra note 606 p. 19.
[706] Ibid.

It is only people who have the skills and knowledge and have the ability to achieve good governance, who should be board members and it is useful for the board to be refreshed from time to time to allow for new ideas and opinions as this can strengthen governance to prevent objectionable practices coming commonplace:

"Governance is also likely to be more effective and dynamic if new people with new ideas are appointed regularly, but this needs to be balanced with the need for stability to provide continuity of knowledge and relationships."[707]

The NHS Lanarkshire considers it necessary for the board members to have an extensive skillset which include the following:

"Understanding of Government Health Policies, including how they impact locally.
The ability to work as part of a team, which has both Executive and Non-Executive Members.
The ability to analyse and review complex issues, weigh-up conflicting opinions and reach your own decisions.
Understanding of Strategic Planning.
Understanding of Resource Management.
Commitment to engaging positively and openly with patients and the public.
The ability to undertake effective public presentational/representational work.
The highest standards of integrity and honesty."[708]

From the above principles, it is important for staff to not only implement the principles but to also have a wider appreciation for the personal characteristics for implementing the principles.

[707] Supra note 606 p. 19.
[708] NHS Lanarkshire Assessment of NHS Lanarkshire Governance Arrangements. Available at http://www.nhslanarkshire.org.uk/boards/governance/Pages/default.aspx last accessed August 2017.

C. INTERNAL MECHANISMS OF ACCOUNTABILITY

If the success of SOEs is not based on profit maximisation and so financial performance is not a means of evaluating the success of SOEs, it is necessary to establish alternative criteria to review board performance. This chapter, rather than providing an exhaustive list, is going to take examples from different jurisdictions which demonstrate how accountability is attained. How a board is evaluated, can have a significant impact on the execution of corporate governance standards. For example, if the board is subject to rigorous reviews, it is more likely to be actively engaged with governance standards. It is suggested that SOEs will benefit from evaluations that are not solely based on annual reports.[709]

In Ireland, according to the *Guidelines on Contracts, Remuneration and Other Conditions of Chief Executives and Senior Management of Commercial State Bodies,*[710] the board must review the performance of the chief executive annually but it is left to the board to set the review procedure.[711] The board has the responsibility to constantly review its own operation and seek to identify ways of improving its effectiveness.[712]

In Queensland, it is clearly stated that it is the board of directors who are responsible to the Minister, for not only overseeing the running of the organisation, but also for the performance of SOEs.[713] Their governance standards set a higher standard for responsibility as the Minister sets targets for which SOEs' performance can be measured against, these targets are set in the Statement of Corporate Intent.[714] It becomes apparent that SOEs in Australia have an emphasis on efficiency and performance of SOEs, as these targets include both financial and non-financial basis.[715] The rationale for introducing such

[709] Sokol, D. "Competition Policy and Comparative Corporate Governance of State-owned enterprises" (2009) 6 *Brigham Young University Law Review* 1713 p. 1802.
[710] Supra note 630.
[711] Ibid principle 1.17 p. 5.
[712] Supra note 580 principle 4 p. 24.
[713] "The GOC's board will be accountable to the shareholding Ministers for the GOC's performance." The State of Queensland Australia *Government Owned Corporations Act* 1993 Part 5 Principle 3.
[714] The State of Queensland Australia *Government Owned Corporations Act* 1993 Part 5 Principle 3 Section 105.
[715] Supra note 714 section 122(1).

targets is to compensate for the absence of market regulation for SOEs.[716] This is a point highlighted by Martin and Dowdall, where they highlight that SOEs should seek value for money as they do not have a stock market price as an indicator to measure how they are performing.[717]

(1) Accountability Mechanisms for Boards Performance

Shaoul, Stafford and Stapleton argue that governance for SOEs will benefit from a critical evaluation of policy as accountability can be improved by cross examination and discussion forums.[718] If boards are responsible for their performance, they should be aware of what they are expected to achieve. Heath and Norman highlight concern that directors of SOEs may intentionally create deficits in SOEs so as to receive increased budgets in subsequent years.[719] To circumvent against this safeguards should be in place to ensure accountability from the board. To bring clarity to the area, some governments have opted for self-assessment for the board while other approaches taken have opted to implemented indicative policies with the board to define how they should achieve their role in advance of the financial year. Examples of the different strategies are outlined below.

In Ireland, commercial State bodies must implement a five year plan within the first six months[720] and non-commercial State bodies should have a three to five year strategic plan.[721] This plan must include objectives and targets which can be measured. Before implementation, this plan must be approved by the relevant Minister and any views provided by that Minister must be taken into consideration:[722]

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[716] Ibid part 5 principle 3.
[717] Martin, G. & Dowdall, J. "The Quiet Revolution - Corporate Governance in the Public Sector" (2011) *Chartered Accountants Ireland* 1 available at http://www.charteredaccountants.ie/Members/Technical/Corporate-Governance/Corporate-Governance-Articles/The-Quiet-Revolution---Corporate-Governance-in-the-Public-Sector--Gary-Martin-and-John-Dowdall/ last accessed August 2017.
[718] Supra note 590 p. 223.
[719] Heath J. & Norman W. "Stakeholder Theory, Corporate Governance and Public Management: What can the History of State-Run Enterprises Teach us in the Post-Enron era?"(2004) 53 *Journal of Business Ethics* 247 p. 257.
[720] Supra note 580 provision 1.16 p. 15.
[721] Ibid provision 1.17 p. 16.
[722] Ibid provision 1.18 p. 16.

"The board of a commercial State body should within the first six months of each year approve annual rolling five-year business and financial plans, encompassing strategy, planned investment and appropriate financial targets. Plans should reflect shareholders' objectives, as appropriate, and the strategic mandate of the body."[723]

In the United States, one way of ensuring accountability is through following ethical standards which are included in "*Sarbanes–Oxley Act* in 2002, rules established by the Securities Exchange Commission and incentives for ethical conduct outlined by the United States Sentencing Commission in 2004."[724] Although Ferrell believes that the shortfall of those ethical standards set is that they did not remove the incentives for misconduct.[725]

(a) Statement of Corporate Intent

A Statement of Corporate Intent (SCI) is an important feature of SOEs governance in New Zealand and Australia. A SCI is essentially a business plan setting out the objectives of SOEs and the board is bound by it. The information in a SCI is drafted by the board but is ultimately subject to approval by the shareholding Minister, who has the power to direct the board's SCI.[726] Following Ministerial approval the SCI is presented to the House of Representatives and once approved it is made available to the general public.[727] A high level of detail is required by SCI in New Zealand which include:

"the objectives of the group and the nature and scope of the activities to be undertaken:
the performance targets and other measures by which the performance of the group may be judged in relation to its objectives:
the information to be provided to the shareholding Ministers by the State enterprise during the course of those financial years.
any activities for which the board seeks compensation from the Crown." [728]

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[723] Ibid provision 1.16 p. 15.
[724] Ferrell, O. & Ferrell, L. "The Responsibility and Accountability of CEOs: The Last Interview with Ken Lay"
(2011) 100 *Journal of Business Ethics* 209 p. 215.
[725] Ibid.
[726] Supra note 612 section 13.
[727] Supra note 614 p. 16.
[728] Supra note 612 section 14.

The importance of an SCI should not be understated as this will define the role of the board and it is clear the content of an SCI will be the cornerstone of SOEs business. Not only will it be used for setting their objectives, it also will be used as a measure if SOEs are doing everything within their remit to operate as successful businesses. An SCI places a substantial burden on SOEs to ensure the objectives are met as there is a dual evaluation for SOEs as they are assessed prior to implementing SCIs and when the term ends to measure its success. Douglas describes SCIs as the principle means of accountability.[729] Corporate governance practices of SOEs are likely to improve as a result of such a detailed report as the SCI is used as a reference by both the Minister and board of directors as it aids the board in performing their governance role as they can refer to it to ensure they are operating within their perimeters and fulfilling the duties that is expected of them.

Similar to requirements in New Zealand, there is a requirement for Australian Government Owned Corporations (GOCs) to provide a Statement of Corporate Intent (SCI).[730] Similar to New Zealand, the basis for accountability for the board is through the SCI as it is a monitoring tool of the performance of SOEs and GOCs must also provide a SCI every financial year.[731] The State of Queensland Australia requires its GOCs to implement a SCI to include the following content:

"an outline of the GOC's objectives,
an outline of the nature and scope of the activities proposed to be undertaken by the GOC during the relevant financial year,
the GOC's capital structure and dividend policies,
an outline of the major infrastructure investments proposed to be undertaken by the GOC during the relevant financial year,
an outline of the borrowings made, and proposed to be made, by the GOC,

[729] Watson, A. "Neither Fish nor Fowl: Issues Arising from the Corporatisation of State Businesses in New Zealand" (1995) *International Company and Commercial Law Review* 344.
[730] See further Ryan, C. & Ng, C. "Public Sector Corporate Governance Disclosures: An Examination of Annual Reporting Practices in Queensland" (2000) *59*(2) *Australian Journal of Public Administration* 11 p. 20.
[731] Supra note 714 part 3 principle 14.

an outline of the policies adopted by the GOC to minimise and manage any risk of investments and borrowings that may adversely affect its financial stability,
an outline of the GOC's policies and procedures relating to the acquisition and disposal of major assets."[732]

In New Zealand, the Audit Office is reviews the SCI to ensure it contains sufficient information to meet the statutory requirements.[733] The SCI of Queensland highlights the requirement of substantial detail to be included in an SCI and in order to fulfil all the above requirements and would provide a considerable amount of detail. Compared to requirements of the SCI in New Zealand, there is a far greater amount of detail required and Queensland has particular focus on economic activities, something that does not feature in SCIs in New Zealand.

(b) Comprehensive Performance Assessment

In the UK, the Audit Commission examined ways in which local public bodies can improve services to ensure they are serving the best interests of the users and decided that the diagnostic tool of Comprehensive Performance Assessment (CPA) was suitable performance evaluator. It allows public bodies the power to self-assess their performance and their governance and rank it on a scale according to high performers, strivers, coasters, weak and poor performers.[734] CPA was later replaced by the Comprehensive Area Assessment in 2009.

Bovaird, Loeffler and Martin highlight flaws of CPAs and consider it an inadequate tool for measuring how institutions are engaging with corporate governance standards, as there is an emphasis on service improvement rather than on governance. They claim that "performance assessment procedures must assess the quality of governance as well as the

[732] Supra note 714 part 8 section 107.
[733] Supra note 729.
[734] The Audit Commission UK Comprehensive Performance Assessments. Available at http://www.audit-commission.gov.uk/inspection-assessment/cpa/pages/default.aspx last assessed last accessed August 2017.

quality of services."[735] CPAs are based on Performance Indicators but Bovaird, Loeffler and Martin have criticised Performance Indicators as they do not take into account areas of corporate governance for public bodies such as transparency, and they also omit details on the decision making process and how different groups of stakeholders are considered.[736] They note similarities with CPA's to the American system of using community score cards but find the community score cards superior as it gives better consideration to stakeholders.

The UK also uses Public Service Agreements (PSAs) to improve corporate governance of public bodies. PSA are target goals on performance that are set for public bodies. James has criticised the agreements as he claims the direct incentive effects of PSAs are weak and targets have been used by ministers as minimum pledges of performance rather than tools for stretching and improving performance.[737] He outlines how various forms of blame avoidance and blame shifting have occurred and the credibility of the PSA system is in danger of being undermined by frequent changes to targets and misrepresentation of performance in some areas.[738]

(2) Checklist for reviewing Governance

To assist government departments in complying with the *UK Code of Good Practice Guidelines*, the National Audit Office has provided a checklist so that those implementing governance standards can ensure they are interpreting it correctly.[739] The aim of the checklist is to provide the board with a useful starting point to assess their performance. The checklist also provides an opportunity to give a detailed explanation as to why the department has not complied with the code. Providing this checklist will offer a starting point for governance procedures for arm's length bodies and by following it, should install confidence in the government that the arm's length body has a high standard of governance

[735] Bovaird, Loeffler and Martin "From Corporate Governance to Local Governance: Stakeholder-Driven Community Score-Cards for UK Local Agencies?" (2003) 26(8) & (9) *International Journal of Public Administration* 1037 p. 1057.
[736] Ibid p. 1045.
[737] James "The UK Core Executive's Use of Public Service Agreements as a Tool of Governance" (2004) 82(2) *Public Administration* 397 p. 397.
[738] Ibid.
[739] National Audit Office UK *Corporate Governance in Central Government Departments: Code of Good Practice 2011 Compliance Checklist.*

in place. It is suggested that a board of directors should carry out their duties with extra vigilance during times of economic pressure and that they have an increased obligation to act in the interests of the creditors, even if temporarily this is not in the absolute best interests of the shareholders. This theory is reconciled with the company's obligation to act in the interests by the realisation that, if the organisation is not in a position to pay its creditors, the company will become insolvent.[740]

(3) Imposition of Personal Liability on Directors

In New Zealand, directors of SOEs can be personally held liable for their failings in their role as directors:

"(1) The duties of the members of a statutory entity are individual duties owed to the responsible Minister and the statutory entity.
(2) If a member does not comply with his or her individual duties, that member may be removed from office.
(3) A statutory entity may bring an action against a member for breach of any individual duty." [741]

Directors of SOEs can be sued for their actions under the Act on the basis that directors are independently engaged in trade, and can be sued for breaches of individual duties.[742] However, no liability will arise where the director acted in good faith which will provide cover against liability for many directors.[743]

OECD Guidelines specify a collective rather than individual responsibility of a board is favourable by including a provision making the board fully accountable to the owners.[744] While the board can be held responsible for their failings in New Zealand where they acted in bad faith, Queensland imposes criminal liability "an offence against this Act for which

[740] Daly *IBEC Corporate Restructuring Guidelines, Corporate Governance* (Irish Business and Employers Confederation 2010) p. 12.
[741] *The Crown Entities Act* 2004 New Zealand section 59.
[742] Ibid section 59(3).
[743] Ibid section 123.
[744] OECD *Corporate Governance of Non-Listed Companies in Emerging Markets* (Paris 2006) p. 17.

the maximum penalty of imprisonment is 2 years or more."[745] It is explicit that Ministers will not incur any civil liabilities for any acts or omissions in their role.[746]

Making directors accountable for their actions is one way to incentise directors to act in the interests of the company. Sternberg advocates that accountability is an essential feature of good governance, as the agent is accountable to the principle for an outcome and accountability presupposes legitimate authority.[747] In spite of this, Reynolds points out that it is not sufficiently clear whether the actions of directors should be in the interests of SOEs or the Government Minister who appointed him[748] and so undermining the value of accountability.

(4) The Role of Audits

The Audit Committee will also be an important agent in the role of accountability, in recognition of the board of directors having to delegate responsibility to the Audit Committee. The Audit Committee for SOEs comprises non-executive directors who have the responsibility of ensuring effectiveness of internal audits.[749] Research carried out by the Audit and Comptroller General identified the *Code of Practice for State Bodies* 2009[750] contains only basic provisions and does not have the high level detailed provisions that are required to attain good practice standards.[751]

It is essential that any State body with more than 20 employees to have an Audit Committee who has duties that:

• ensures that at least one member has an adequate financial expertise.

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[745] Supra note 714 section 160(1).
[746] Supra note 714 section 83.
[747] Sternberg "The Stakeholder Concept: A Mistaken Doctrine" (1999) *Foundations for Business Responsibilities* 1 p. 20.
[748] Reynolds, I. "Public Sector Corporate Governance" (2009) 3 *Accountancy Ireland* 51 p. 53.
[749] Supra note 598 principle 10.
[750] Supra note 598.
[751] Comptroller and Auditor General *Special Report Effectiveness of Audit Committees in State Bodies* (Report number 87 Dublin 2014) p. 29.

• monitor and review the effectiveness of the State body's internal audit activities and ensure that it is achieving value for money.
• meet four times a year and receive information on audit items relating to their areas of responsibility when these are identified.
•The internal Audit Committee must also make external auditors aware of the corporate governance issues and report to the Board Audit Committee.[752]

While these standards reflect what has been set for SOEs, listed companies *the UK Code* goes further and requires the committee to confirm the integrity of the financial statements made by the company. Rather than liaising with the external auditors, *the UK Code* requires the internal audit committee to ensure their independence. They also have the power to remove external auditors. Common features to both codes are that they require an internal audit committee to ensure the effectiveness of the internal audit function and make recommendations to the board.

A report carried out Grant Thornton *Corporate Governance Review* found only 43% of audit committees complied with the provision that one in every three on audit committee should have financial experience, indicating that over half of audit committees are made up of NEDs without the relevant financial experience.[753]
Full disclosure must be provided so as to ensure a full and accurate picture is reported.[754] SOEs must report to Ministers as they have a responsibility in overseeing that standards are followed, including the *Code of Practice for State Bodies* 2009. However, where the guidelines are lacking is in relation to what measures Ministers must take if there has not been compliance with government policy. This is a major issue and will be dealt with in the later chapter on the case study of FÁS.

[752] Supra note 598 p.13.
[753] Grant Thornton *Corporate Governance Review* (Dublin 2011) p. 25.
[754] Supra note 625 p. 6.

D. External Mechanisms of Accountability

This section looks at examples on how external mechanisms can improve accountability. Examples from other jurisdictions will also be reviewed.

(1) The role of the Minister

Hogwood and McVicar identify the five levels of ministerial responsibility:

"Redirectory responsibility, requiring that ministers redirect queries to the appropriate person dealing with a particular case or issue.
Informatory responsibility, requiring the minister to keep parliament informed of what is happening in their department.
Explanatory responsibility, requiring the minister to make further explanation, particularly in cases of once-off shortcomings or wrong doings.
Amendatory responsibility, where a minister is convinced that more than an explanation is required, requiring correction, amendment or reparation.
Sacrificial responsibility, where a minister accepts an obligation to resign."[755]

However, there may be significant disparities between what Minsters are responsible for and what they are accountable for. The Minister, as head of the department, carries significant duties and the role of the relevant Minister is undoubtedly a key feature of the external mechanisms of accountability in governance standards as the Minister is separate from the board and SOE but has a supervisory role over governance for SOEs. The IOD/NSAI standards for SWIFT accreditation require SOEs to satisfy the relevant Minister that corporate governance standards are followed.[756] This is reiterated by the Code for State Bodies:

[755] Judge, D. Hogwood, B. & Vicar, M. "The "Pondlife" of executive agencies: Parliament and Informatory Accountability" (1997) 12 (2) *Public Policy and Administration* 95 p. 97.
[756] Supra note 598 p.1, introduction. See also The Institute of Directors and the National Standards Authority in Ireland *SWiFT 3000:2010 Code of Practice for Corporate Governance Assessment in Ireland* (2010) p. 6.

"State bodies and their subsidiaries are required to confirm to the relevant Minister that they comply with the up-to-date requirements of the Code in their governance practices and procedures."[757]

This indicates that while Ministers may have a supervisory role over the board, the Minister has a role in seeing that SOEs have suitable governance standards in place. In Queensland, legislation casts significant responsibility on the board to keep the shareholding Minister informed of the activities of SOEs:

"there is no limit to the matters of which the board is required to keep a shareholding GOC of a prescribed GOC subsidiary informed, or limit the reports or information that the board is required, or may be required, to give to a shareholding GOC."[758]

What is particularly unique to UK standards for public bodies is the clear unequivocal responsibility that is put on Ministers who are responsible for SOEs and it is the leading principle in the standards:

"The Minister in charge of the department is responsible and answerable to Parliament for the exercise of the powers on which the administration of that department depends. He or she has a duty to Parliament to account and to be held to account, for all the policies, decisions and actions of the department, including its arm's length bodies."[759]

The UK also places responsibility on Ministers for SOEs' performance and also for the use of their resources.[760] Including extra requirements for use of their resources, places an onus on the arm's length body to be efficient and it is a measure to ensure money invested in the entity is being used as it was intended. Such measures should secure organisations that will achieve its aims and serve the stakeholders. This requires clear sanctions for arm's length bodies who do not meet their performance targets.[761]

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[757] Supra note 580 p. 5.
[758] Supra note 714 section 122(2).
[759] HM Treasury Cabinet Office (UK) *Corporate Governance in Central Government Departments: Code of Good Practice* (2011) Principle 1.1 p. 13.
[760] Ibid principle 6.3.
[761] Ibid principle 6.7.

A distinct approach taken by both New Zealand and Australia is the dual ministry model where dual responsibility for SOEs is divided between two government departments. This responsibility is generally divided between the Minister for Finance and another Ministerial department who are most suitably matched to monitor SOEs:

"Where two or more Ministers are responsible for different functions of a department, the Minister responsible for the relevant function of the department shall be the appropriate Minister."[762]

The *New Zealand State-owned Enterprise Act* 1986 refers to the Ministers as "shareholding Ministers" and "responsible Minister."[763] A responsible Minister is defined as "the Minister for the time being responsible for that State enterprise."[764] Shareholding Minister comprises both the Finance Minister and the responsible Minister.[765] Responsibility is proportioned between the Minister for Finance and the responsible Minister for SOEs, as both departments are responsible to the House of Representatives for the performance and functions of SOEs, with the dual responsibility reflected in the ownership as both departments owning half the shares in an SOE.[766] However, the responsible Minister generally takes a more active role in managing SOEs.[767]

Australia's *Commonwealth Authorities and Companies Act* 1997 provides for a dual Ministry model. The State of Queensland has opted to follow a dual Ministry model of governance, where a GOC Minister and a portfolio or shareholding Minister, are both responsible for SOEs.[768]

There are benefits of a dual ministry model as monitoring aspects of SOEs could improve where two government departments monitor SOEs and each department can provide

[762] *State Senior Act* 1998 New Zealand section 2.
[763] Supra note 580 section 2.
[764] Ibid.
[765] Ibid.
[766] Ibid part 1 section 8.
[767] Supra note 614 p. 8.
[768] Supra note 714 section 78.

expertise on their area. Vagliasindi indicates that a dual ministry model can alleviate potential agency issues of government being both owner and administrator for SOEs by separating the roles over two departments will reduce potential conflicts of interest that may arise.[769]

However, a dual ministry model can be problematic as responsibilities are divided between two departments, which may result in neither department having a full and accurate insight into SOEs. A way of overcoming such difficulties is for the departments to correspond with each and establish advance planning and outlining specific outputs from each department to prevent instances of duplicating duties but this may give rise to overlapping of resources.

The OECD considers an advantage of a sole ministry is that it leaves no ambiguity over who has responsibility for SOEs and recognises that dual ministry may cause conflicts of interest.[770] This conflict becomes prevalent where there is proximity of ownership and regulation, where the same Ministerial branch is responsible for industrial policy and ownership functions of SOEs.[771]

Irish guidelines for SOEs do not stipulate if it is the overseeing Minister for the SOE or the board of directors who are ultimately responsible for failings in corporate governance standards of SOEs. While the Minster is responsible for the overall performance of SOEs, it appears that the Minister is not accountable if corporate governance standards are not implemented. This conclusion was reached when the then Minister for Trade Enterprise and Employment Mary Coughlan, who was the Minister FÁS was accountable to during the scandal, did not suffer any consequences for any omissions of duties she may have been responsible for**.**[772] The *Code of Practice for State Bodies* points out that it is the board and management who are accountable for the proper management of the organisation.[773]

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[769] Vagliasindi M. "Governance Arrangements for State Owned Enterprises" *Policy Research Working Paper World Bank Washington DC* (2008) p. 6.
[770] OECD *Comparative Report on Corporate Governance Enterprises* (2005) p. 33.
[771] Ibid p. 18.
[772] Quinlan "How the FÁS Scandal Unfolded" *Irish Independent* 23 November 2008.
[773] Supra note 580 p.5.

Legislation in New Zealand is clear that the Minister is responsible to Parliament if they fail in their duties to SOEs:

"The shareholding Ministers of a State enterprise shall be responsible to the House of Representatives for the performance of the functions given to them by this Act or the rules of the State enterprise."[774]

(2) Overseeing Bodies to monitor SOEs

The second element of external mechanism of accountability is the role that overseeing bodies have in the governance of SOEs. Many countries engage an overseeing body to monitor SOEs. The Australian National Audit Office (ANAO) has a supervisory role over SOEs in Australia, in what appears to be similar to what SOEs are subjected to by the Comptroller and Auditor General in Ireland and by the Crown Company Monitoring Advisory Unit in New Zealand.

(a) Ireland - Comptroller and Auditor General

The Comptroller and Auditor General in Ireland is a means of providing external review of government agencies. *The Comptroller and Auditor General (Amendment) Act* 1993 extended the duties ensuring value for money was within the remit of the Comptroller and Auditor General.[775] The Public Accounts Committee (PAC) also plays a role in ensuring public money is spent ensuring value for money. NewERA was introduced in 2011, however, it only provides advice to the government on corporate governance and does not monitor SOEs.

(b) New Zealand - Crown Ownership Monitoring Unit (COMU)

In New Zealand the Ministers role in monitoring SOEs is greatly aided by the influence of the Treasury and a branch with the Treasury Unit set up for monitoring SOEs known as the

[774] Supra note 612 section 6.
[775] *The Comptroller and Auditor General (Amendment) Act* 1993 section 5.

Crown Ownership Monitoring Unit (COMU). The COMU's predecessor is Crown Company Monitoring Advisory Unit (CCMAU) and the organisations offer perhaps one of the more significant insights to how overseeing the board can develop governance with SOEs.

The CCMAU was established in 1992 as a branch of The Treasury where initially it was intended to monitor health services but their role expanded over time due to the increased public interest in SOEs' performance. The CCMAU monitors SOEs once the following conditions are satisfied:

"(i) Is the ownership interest material?
(ii) Are the ownership and purchase/other interests sufficiently well-defined and separable from each other to make separate ownership monitoring valuable?
(iii) Is there value monitoring the entity specific interest separately from the Crown's balance sheet interest?
(iv) Do the benefits of monitoring aspects of the ownership interest centrally outweigh the costs?"[776]

Therefore, the CCMAU decision to become involved in monitoring SOEs will be based on the Crown having a clear separation from SOEs, so the CCMAU can strive to make SOEs more cost effective, tying back to the requirement for SOEs to be self-sustaining enterprises. There are four teams within the CCMAU that report to the shareholding Minister comprises the following:

1. Sector Monitoring teams, who analyse business reports and advise on strategic issues.
2. Financial Analysis unit who analyse individual SOE financial reports.[777]
3. Appointments and Governance team, who advise the Minister on the appointments of board members of SOEs.

[776] The Treasury State Services "Commission Report of the CCMAU Review Team: Phase II - Scope, Form and Location" (2000) p. 3.
[777] The financial reports are used a means of measuring performance. All financial decisions are taken by the Treasury and the Minister.

4. Sector Performance and Balance Sheet team who advise the government on the overall performance of the Crown's SOEs. [778]

The CCMAU is a key component in managing relationships between government and SOEs as it acts as an agent for the shareholding Minster to the board of directors. The CCMAU updates Ministers on the performance of SOEs but all financial decisions remain the responsibility of the Treasury and the Ministers. McKinlay sees the role of the CCMAU as adding a valuable dimension of monitoring SOEs which will provide an effective tool for monitoring their effectiveness of delivering government policy.[779] While the CCMAU primarily works on behalf of Minsters, SOEs also gain from this as they will be aware of what is required from them to fulfil their duties increasing communication between the two entities. This is beneficial as soon as the CCMAU becomes aware of difficulties within SOEs the shareholding Minster can take a proactive approach in solving problems. Ministers can request updates on SOEs on specific matters where necessary. There is clearly a great emphasis on monitoring SOEs in New Zealand. Along with allocating two Ministers supervisory functions for an SOE there is the added layer of the CCMAU:

The CCMAU has the functions to:

- "monitor the government's investment in Crown entity companies,
- assist with the appointment of directors to Crown entity company boards,
- provide performance and governance advice to shareholding Ministers."[780]

This extra link between government and SOEs can create an increased promise of good governance as the CCMAU has regular contact with SOEs.[781] The CCMAU provided guidance on the requirements of SOEs and highlighted the importance of SOEs being successful, efficient and productive companies, a requirement that does not feature in the

[778] The Treasury Crown Ownership Monitoring Unit *Owner's Expectations Manual Crown Ownership* (New Zealand 2012) p. 16.
[779] Ibid p. 50.
[780] State Services Commission New Zealand *Crown Entities: A guide for Ministers* Available at http://www.ssc.govt.nz/node/6382 last accessed August 2017.
[781] Supra note 614 p. 14.

Irish codes. The Advisory Unit expands on this by adding that SOEs must be more productive when compared to entities that are not SOEs.[782] It may be difficult to determine if this objective is being fulfilled as there may not be a comparable entity to SOEs or the function of an SOE may not be profit driven, and therefore, it is questionable if efficiency can be measured.

(c) Australia - Australian National Audit Office (ANAO)

The ANAO is the national auditor for the Parliament of Australia.[783] The ANAO provides a mechanism of bringing accountability for government and SOEs in Australia. The Auditor General is completely independent from government and so takes no direction from them. The key functions include:

"auditing the financial statements of Commonwealth entities, Commonwealth companies and their subsidiaries;
conducting performance audits, assurance reviews or audits of the performance measures, of Commonwealth entities and Commonwealth companies and their subsidiaries, other than government business enterprises;
providing other audit services as required by others and
reporting directly to the Parliament on any matter or to a minister on any important matter."[784]

[782] Supra note 614 p. 8.
[783] *Auditor-General Act* 1997 Australia.
[784] Ibid section 2.

E. ISSUES ASSOCIATED WITH STAKEHOLDERS AND SHAREHOLDERS

(1) Code Provisions dealing with Stakeholders

In addressing how a board and government is accountable for stakeholder interests it is of assistance to examine how they have been dealt with in the *Code of Practice for State Bodies* and compare this to other corporate governance codes. The *OECD Guidelines on Corporate Governance of State-owned Enterprises* deals with the treatment of stakeholders.[785] The OECD guidelines highlight both the governments and SOEs obligations to stakeholders. They recommend that governments should respect the rights of stakeholders and that SOEs should report on their relations with stakeholders.[786] Additionally it is recommended stakeholders should have the right of redress where they consider their rights have been violated.[787] The OECD requires large SOEs to report on stakeholder relations[788] and this was endorsed by the *Code of Practice for State Bodies* 2016 which requires effective and timely communication with stakeholders.[789]

The *UK Governance for Public Services* affirmed the value of stakeholders where it highlighted that not only should stakeholders be considered but that they should be engaged in the process and, of equal importance, the body should be accountable to other stakeholders.[790]

The UK Audit Commission team investigated corporate governance principles in the public sector and extended the definition of corporate governance to emphasise the importance of stakeholders:

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[785] OECD *Guidelines on Corporate Governance of State-Owned Enterprises* (Paris 2015). For further discussion on stakeholders see OECD *Corporate Governance of State-Owned Enterprises: A Survey of OECD Countries* (Paris 2005) p. 37.
[786] OECD *Guidelines on Corporate Governance of State-Owned Enterprises* (Paris 2015) p. 48.
[787] Ibid.
[788] Ibid.
[789] Supra note 580 provision 2.3 p. 18.
[790] Supra note 606 p. 23.

"The framework of accountability to users, stakeholders and the wider community, within which organisations take decisions, and lead and control their functions, to achieve their objectives."[791]

To build a relationship between the government and stakeholders, trust is recognised as a feature of public corporate governance standards in the UK as this will result in better corporate governance standards.[792] It is a difficult task for SOEs to win trust as stakeholders may not feel their interests are appreciated by SOEs and as a result of this public confidence in SOEs may not be very forthcoming.[793] The *UK Governance for Public Services Code* is presented in a manner that reflects the value of stakeholders by focusing on results for the citizens and from transparent decision making. If the board acts in the best interests of citizens this will improve the public confidence in the public body and it will also allow the corporate body to connect with citizens.[794] While it is not always clear what the right decision to make should be, it is highlighted that if decisions are made in a transparent manner in which reasons can be given for why a particular course of action is taken then this will lead to good governance.[795] The *Kay Review* was carried out to assess how UK quoted companies performed and how well governance was implemented.[796] The report stressed the importance of trust and confidence and regards integrity as paramount for UK listed companies and recommends that:

"All participants in the equity investment chain should observe fiduciary standards in their relationships with their clients and customers. Fiduciary standards require that the client's interests are put first, that conflict of interest should be avoided, and that the direct and indirect costs of services provided should be reasonable and disclosed. These standards should not require, nor even permit, the agent to depart from generally prevailing standards of decent behaviour. Contractual terms should not claim to override these standards."[797]

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[791] UK Audit Commission *Corporate Governance: Improvement and Trust in the Local Public Service* (2003) p. 4.
[792] Ibid p. 8.
[793] Supra note 607 p. 35
[794] Supra note 606 p. 7.
[795] Ibid p. 4.
[796] The Kay Review of UK Equity Markets and Long-term Decision Making: Final Report July 2012.
[797] Ibid principle 5.

Deighton-Smith recognises the importance of transparency in governance as it promotes trust by allowing stakeholders access information in understandable language to assess the quality of actions and decisions.[798] It is argued that transparency is increased through a consultation process known as *Regulatory Impact Analysis* (RIA) which will allow stakeholders to get involved in the development of new regulation.[799] There is a provision for RIAs as part of the legislative process in Ireland.[800] Deighton-Smith argues that if the results of the RIA are published this will improve transparency as a useful method of engaging shareholders as this is active consultation with stakeholders.[801]

The process of engaging with stakeholders was used when implementing when the FRC were revising the governance standards for listed companies implementing *the UK Code* in 2010.[802] A similar process was used by the ISE when deciding if *the UK Code* should be annexed to the Irish standards.[803] The principle of engaging stakeholders and making accountability real places a duty on State bodies to give stakeholders the opportunity to be involved and it ensures the board is accountable and will act in the interests of citizens. This raises the question to what extent or what proportion the board of SOEs should act on advice of the stakeholders but nevertheless ensuring the interests of stakeholders in State bodies.[804] Branston, Cowling and Sugden argue that the engaging stakeholders can only happen if information is available to them so that they can have an education and an understanding of the issues.[805]

Legislation for SOEs in Australia provides for community service obligations which ensure the interests of the community are considered by SOEs:

"The community service obligations of a GOC are obligations to perform activities

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[798] Deighton-Smith, R. "Regulatory Transparency in OECD Countries: Overview, Trends and Challenges" (2004) 63(1) *Australian Journal of Public Administration* 66 p. 68.
[799] Ibid p. 67.
[800] Department of An Taoiseach "Review of the Operation of RIA" (2008).
[801] Supra note 798 p.68.
[802] Financial Reporting Council (UK) *Consultation on the revised UK Corporate Governance Code* 2009.
[803] Irish Stock Exchange *Consultation Paper Consultation on changes to the ISE Listing Rules relating to Corporate Governance* (2010).
[804] Supra note 606 p. 4.
[805] Branston, R. Cowling, K. & Sugden, R. "Corporate Governance and the Public Interest" (2006) 20(2) *International Review of Applied Economics* 189 p. 206.

that the GOC's board establishes to the satisfaction of the shareholding Ministers
(a) are not in the commercial interests of the GOC to perform
(b) arise because of a direction, notification or duty to which this section applies
(c) do not arise because of the application of the principles of corporatisation of Strict accountability for performance or Competitive neutrality."[806]

The board's responsibility to stakeholders was not reflected in the Irish standards as the *Code of Practice for State Bodies* 2009 omitted any provisions on stakeholders. The updated *Code of Practice* 2016 made limited references to stakeholders but acknowledged they should be considered and communicated to.[807] The *Code of Practice* maintained a focus which sought value for money to be achieved and this ensure the best interests of stakeholders:

"State bodies should serve the interests of Government as shareholder, the taxpayer, and all other stakeholders, and pursue value for money in their endeavours, including managing risk appropriately. State bodies should act prudently, ethically and with transparency as public entities and should conduct their activities consistent with their statutory responsibilities."[808]

This provided little incentive for the board to implement Stakeholder theory. Rather than providing guidance there was more a vague requirement for SOEs to spend their money with good cause and presumably to pricing structure for goods and services provided. Achieving value for money is important, but it only has a narrow focus on stakeholders' interests. The *UK Governance for Public Services Code* highlights it is necessary that public money is spent in the best interests of the taxpayer and that the services work in line with the public interest.[809] While SOE's spending activity is it an important aspect of governance this alone will not ensure SOEs are considering and improving stakeholder interests. As highlighted previously it is important that stakeholder interests and economics are not completely interlinked, stakeholder interest should not be centred solely on

[806] Supra note 714 part 8 section 112.
[807] Supra note 580 provision 2.3 p. 18.
[808] Supra note 580 p. 5.
[809] Supra note 606 forward.

economic reasons or it will be unlikely that their interests will be accounted for. This moves responsibility to the government to give clear guidance as to what are the objectives of SOEs and how SOEs add value to the stakeholders and thereby enforce Stakeholder theory.

Perhaps it would be useful to shift some focus from how governance standards can be improved by a change in the attitude towards corporate governance to recognise not only the role of stewardship a board plays but also the stakeholder and shareholder. While there may always be an implicit element of following corporate governance standards to favour stakeholders substantive provisions are omitted from the Irish standards which does not give any guidance to a board and is a weakness in Irish standards. As provisions dealing with stakeholders are limited in the Code of Practice, this shift responsibility to stakeholders to ensure their interests are protected.

(2) Stakeholder activism

An important issue in the context of SOEs is stakeholder engagement and how non-shareholder stakeholders can influence SOEs. If stakeholders are those who have a stake and an interest in SOEs they have motivation as they will be affected by the outcome. For example, Irish Water is an example how stakeholders can influence the actions of an SOE. The introduction of domestic water charges was met with hostility and stakeholders were successful in suspending water charges for domestic homes. This shows how persistent stakeholder involvement can bring change.

Shareholder activism is common for listed companies as there is a presumed responsibility on shareholders of ensuring standards are upheld.[810] However, there is a recognised problem of shareholder passivity where shareholders are disinterested in assuming an active role in the organisation while shareholders are receiving a return on their investment they may not be concerned in whether the organisation has a good standard of corporate governance or not.[811] Ideally it should be a reciprocal relationship between stakeholders

[810] Financial Reporting Council (UK) *The UK Stewardship Code* (2010).
[811] See further Stratling, R. "How to Overcome Shareholder Apathy in Corporate Governance: The Role of Investor Associations in Germany" (2012) 83(2) *Annals of Public & Cooperative Economics* p. 143.

and SOEs, where SOEs act in the interests of stakeholders but stakeholders must engage and support SOEs. Cools questions stakeholders' involvement in getting involved with organisations they have invested it. It is suggested that shareholders do not have the same expertise as directors and are immersed in organisations to be able to make independent judgements.[812] It is often only when there is a downturn in the company that shareholders have an interest in corporate governance rather than participating on an ongoing basis. The EU has highlighted the lack of shareholder engagement due to a variety of reasons that include cost of engagement, uncertainty of engagement and lack of interest.[813]

During the financial crisis shareholder activism was credited as being a major component of good corporate governance practices. The *Stewardship Code*[814] was a result of the *Walker Review*[815] which encouraged institutional shareholders to take more responsibility with their voting rights for the benefit of all shareholders. In order for institutional shareholders to fulfil this duty it is recommended that there is increased engagement by institutional shareholders and one of most significant information to communicate is material changes in the share register.[816] Other incentives for institutional to shareholders increase their involvement is to have engage with investee companies and consider and challenge explanations for departure from *the UK Corporate Governance Code*.[817] The Merseyside Pension Fund Committee[818] implemented *the Stewardship Code* and set out how they intend to implement the code, which will be the responsibility of asset managers to enforce *the Stewardship Code* by monitoring their investee companies and they must intervene where necessary. They indicated that they will work collaboratively with other

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Bolodeoku, I. "Corporate Governance In The New Information And Communication Age: An Interrogation of the Rational Apathy Theory" (2007) 7(1) *Journal of Corporate Law Studies* p. 109. Chizema, A. "The Empowerment of Shareholders: A Conceptual Perspective" (2011) 36(4) *Journal of General Management* p. 23.

[812] Cools "The Dividing Line between Shareholder Democracy and Board Autonomy: Inherent Conflicts of Interest as Normative Criterion" (2014) 2 *European Company and Financial Law Review* 258 p. 266.

[813] European Commission Green Paper *The EU Corporate Governance Framework* (Brussels 2011) p. 11.

[814] Supra note 810.

[815] Walker *A Review of Corporate Governance in UK Banks and Other Financial Industry Entities Final Recommendations The Walker Report 2009.*

[816] Ibid recommendation number 14.

[817] Supra note 810 p.4.

[818] Merseyside Pension Fund is the 5th largest fund in the UK Local Government Pension Scheme. It has assets under management of £4.6 billion. Available at http://mpfmembers.org.uk last accessed August 2017.

institutional shareholders such as the Local Authority Pension Fund Forum (LAPFF) to increase their influence on investee companies.[819]

(3) The influence of public interest on corporate governance standards

Stakeholders can use the influence of public opinion to their advantage when persuading SOEs to enforce standards that protect their interests. Public outcry will often be the impetus for setting new policies in Ireland. Often corporate governance standards are updated where there is a corporate crisis as the power and influence that comes with the role of director can give rise to abuse of this position.[820] Policy is frequently made in reaction to scandals which are well publicised. The scandals that often lead to public outrage that result in the introduction of corporate governance standards very often carry an element of corruption.

It can be argued that a large portion of law-making is political and as a result politicians can be more easily swayed and influenced by public perception so they are seen to be making decisions that are popular with the people who have elected them to their public office. By extension of this there is an argument to be made for public perception influencing governance standards and enforcement of them, after all it is the public who are the ultimate owners of SOEs and therefore it is not unreasonable that their interests should be considered. Introducing policy in response to public perceptions can create unforeseen problems that are based on events which precede its introduction as they may have narrow limitations and may later serve only specific situations.

In this respect it would be useful to have an independent committee akin to the UK Financial Reporting Council investigating where the shortfalls are in corporate governance standards for SOEs and setting out how they can be addressed. Perhaps it would also be useful for the board of SOEs to have a point of contact so they have the opportunity to

[819] Merseyside Pension Fund Statement of compliance with the U.K. Stewardship Code for Institutional Investors. Available at Available at http://mpfmembers.org.uk last accessed August 2017.
[820] Bruner "Corporate Governance Reform in a Time of Crisis" (2011) 36(2) *The Journal of Corporation Law* 309.

discuss how they are implementing the Code of Practice and also to be assured that they are providing adequate explanation where code provisions do not apply to that SOE.

The New Economy and Recovery Authority (NewERA) established in 2011 has moved the corporate governance functions for the following SOEs the ESB, Bord Gáis, EirGrid, Bord na Móna, Coillte to this authority. It is unclear why these particular SOEs were chosen however, they are five of the largest commercial SOEs in the State so this may be an influential factor. It is yet to be determined how NewERA will impact the corporate governance of SOEs as there has been very little impact reported to date. The establishment of this authority may be an indication that better governance can be achieved by moving the control of enforcement of governance from the respective government departments to a centralised body. This also may explain why the government refrained from updating the governance standards as updated standards on their own may not bring better enforcement of corporate governance. In June 2013 the government indicated that they will implement NewERA on a legislative basis.[821] NewERA was put on a statutory footing in 2014, however, it only acts in an advisory capacity to the government.[822]

(4) Corporate Social Responsibility

Brennan and Solomon highlight a change in accountability in governance procedures that are moving from shareholder centred to govern a wider ambit which include accountability for stakeholders and towards an inclusion of corporate social responsibility (CSR).[823] Shaoul, Stafford and Stapleton agree that the unitary stakeholder approach does not fit well with governance standards for entities owned by the government. CSR is defined by the EU Commission as the responsibilities of enterprises for the impact of their actions.[824] CSR is described as a business responsibility to its stakeholders:

[821] See National Treasury Management Agency "New Economy and Recovery Authority" Available at http://www.ntma.ie/business-areas/new-economy-and-recovery-authority/ last accessed August 2017.
[822] *National Treasury Management Agency (Amendment) Act* 2014.
[823] Brennan, N. & Solomon J. "Corporate Governance, Accountability and Mechanisms of Accountability: An Overview" (2008) 21(7) *Accounting, Auditing & Accountability Journal* 885 p. 892.
[824] See http://ec.europa.eu/growth/industry/corporate-social-responsibility_en last accessed August 2017.

"the social responsibility of business encompasses the economic, legal, ethical, and discretionary expectations that society has of organisations at a given point in time"[825]

The role of the stakeholder in CSR has developed over different stages. CSR has progressed from companies' "obligation to work for social betterment" to the "the capacity of a corporation to respond to social pressures" and more recently the shift to "the notion of moral correctness in actions taken and policies formulated."[826] Including moral obligation expands the nature of the stakeholder as the organisation is advised to consider a wider audience. In addition to the growing issue of what a stakeholder comprises as there is a greater appreciation of the stakeholder to be concerned with the activities of an organisation where its actions will have implications on them. The pension fund levy perhaps is an example of this. This initiative introduced by the government in May 2011 where a tax of 0.6% is charged on assets under management in pension funds and pension plans approved under Irish tax legislation for the next four years.[827]

CSR does not form part of the governance framework for SOEs. It was omitted from the *Code of Practice* 2009 and was not included in the updated Code in 2016. Governance standards in New Zealand impose a corporate social responsibility on SOEs with a requirement for services provided by the State to be "better-integrated, people-focused service delivery."[828] The effect of this is that the duties of SOEs in New Zealand are widened to encompass their CSR duties but perhaps their duties are qualified by the requirement to adhere to CSR where whenever it is viable to do so. However, this provision may not add substance due to the Treasury considering this requirement for SOEs to be successful businesses as performing their CSR obligations.[829]

[825] Carroll "A Three-Dimensional Conceptual Model of Corporate Performance" (1979) 4(4) *Academy of Management Review* 497 p. 500.
[826] Branco, M. & Rodrigues, L. "Positioning Stakeholder Theory within the Debate on Corporate Social Responsibility" (2007) 12(1) *Electronic Journal of Business Ethics and Organization Studies* 5 p. 11.
[827] Department of Finance Pension Fund Levy – Questions & Answers section.
[828] Duncan, G.& Chapman, J. "New Millennium, New Public Management and the New Zealand Model" (2010) 69(3) *Australian Journal of Public Administration* 301 p. 303.
[829] Supra note 614 p. 33.

CSR should not be omitted from governance for SOEs as it implies that "businesses share responsibility for societal conditions"[830] and that "companies voluntarily integrate social and environmental concerns in their operations and interaction with stakeholders."[831] Jackson sees CSR as businesses acceptance of conforming to what behaviour society expects from it and so will take into account the impact of the actions of the organisation.[832] In return the organisation will benefit financially from improving relations with its stakeholders as it strengthens the resources and capabilities available to them, which are considered a useful means of differentiating an organisation from its competitors,[833] making CSR and the stakeholder a two-way relationship.[834]

[830] Jackson K. "Global Corporate Governance: Soft Law and Reputational Accountability" (2010) 35 (1) *Brooklyn Journal of International Law* 41 p. 52.
[831] Supra note 826.
[832] Supra note 830 p. 53.
[833] Supra note 826 p. 9.
[834] Supra note 826 p. 13.

F. CONCLUSION

Accountability is central to any governance framework and this chapter explores key measures and mechanisms for increasing accountability in SOEs which will be useful for drafting a framework for SOEs. In order to address the issue of accountability different mechanisms are engaged throughout different jurisdictions but indisputably the role of the board and how it engages with governance standards, along with ensuring the board is monitored is central to accountability. This chapter reviewed the role of the board along with its duties and how it works to implement governance standards. It addressed enforcement issues such as monitoring the board, which will give a supervisory function to incentivise compliance for standards on a soft law basis. The chapter examined tools in place to measure the performance and progress of the board. A popular approach was Statement of Corporate Intent for measuring the success of the board's ability to implement governance is to contain the board within the remit of statements of how they intend to enforce governance standards.

Standards can widen the parameters of the duties of the board by recognising that corporate governance principles should not be framed around the board but there is a wider responsibility to stakeholders. Increasing accountability can be sought by giving clear responsibility and direction to a board. If a board has autonomy it should be able to engage with governance standards. Listed companies are accountable to shareholders whereas with SOEs a board is accountable to the relevant Minister but perhaps its accountability should also be towards the stakeholders as it is essentially in their interest their actions are taken. To achieve accountability towards shareholders may require greater transparency in the board's actions. Stakeholders have a stake in SOEs and so will be affected by their success and failure and so a best practice model of governance should ensure their interests are protected. Setting standards only on the operation of the board will result in corporate governance that has a very narrow focus. It is clear as distinct from Irish standards there is much more emphasis on the value of the stakeholder. There is a requirement for governance arrangements to ensure that the legitimate interests of stakeholders are properly and appropriately considered.

It is clear that member conduct of the board and Ministers will have an important role for accountability for SOEs as relevant characters and procedures are central to establishing accountability. SOEs have another element of accountability as the board is accountable to the government. By using a combination of internal and external controls a suitable accountability framework can develop.

The following chapter is going to examine a case study of corporate governance of an Irish SOE. One of the biggest corporate governance scandals of an SOE is FÁS to date and the following chapter will assess how the accountability regime in place did not work as intended.

CHAPTER 5:
BOARD ACCOUNTABILITY - THE FÁS WAY: A CASE STUDY

A. INTRODUCTION

Prior chapters examined the various components required to attain a suitable level of accountability in SOEs. To understand the workings of corporate governance standards in SOEs, FÁS will be examined as a case study. This will help establish how FÁS interacted with corporate governance standards in place at that time, which was the *Code of Practice* 2001. The FÁS controversy, based on misappropriation of funds and reckless spending, was brought to light in 2008. At that time the then Director General stated that the board had broken no rules or regulations.[835] Exploring the events that took place in FÁS is a fitting way to examine how corporate governance principles operate in practice. It also provides a review of how agency issues are increased in SOEs due to the tri-partite relationship of citizens, politicians and the board. The attention on the events in FÁS was instrumental in bringing corporate governance of SOEs into the media attention, making it an excellent model of governance to examine. It is possible to argue that the FÁS saga inspired a reform of corporate governance standards, as the scandal was brought to light in 2008 and the code was updated in 2009.

In addressing the substantial governance issues associated with FÁS, firstly this chapter will give a background into FÁS and its role as a significant SOE in Ireland. The chapter will examine the FÁS controversy and governance issues associated with FÁS, in particular agency issues of individual board members and accountability of FÁS. This raises the question of boards and specifically NEDs role during the scandal. The final section of this chapter will examine corporate governance standards in the FÁS case and the update in governance standards from the Code of Practice in 2001 and 2009. This will build on the previous chapters, which established the key features of governance and highlighted the importance of a suitable regulatory model for a governance framework. Central to this is the issue of the effectiveness of governance on a quasi-legal basis, which examined if governance has significant standing where it is drafted on a soft law basis. As

[835] Radio 1 interview with Director General of FÁS Rody Molloy on 'Today with Pat Kenny' 24 November 2008.

governance standards for FÁS was drafted on a soft law basis, the real impact of this will be studied. There are several governance issues surrounding FÁS. The agency issue of the board, which resulted in a lack of controls over spending and travel protocol and also there were issues with the procurement process. An equally significant governance feature is the level of accountability that comprises a governance model and so the elements of this will be reviewed.

Examining breaches in corporate governance of FÁS is relevant, as the following chapter provides a framework for increasing board accountability in SOEs and these recommendations will be based on governance issues raised by the FÁS scandal.

(1) The Background and Role of FÁS

The organisation was established under the *Labour Services Act* 1987. At that time unemployment was high and FÁS was introduced as a measure by the government to address the problem of rising unemployment. The essential function of FÁS was to train, provide for employment schemes and assist people secure employment.[836]

During the late 80's and early 90's the EU was preparing for a more streamlined market between EU countries. Ireland was falling behind other EU countries in terms of employment and growth and so in order to improve employment prospects for Irish residents £4 million was allocated to FÁS.[837] Throughout the 1990's unemployment fell quite substantially[838] and so FÁS adopted its objectives accordingly. It did so by advancing it policies so as to upskill and to further educate those already in employment and it also established programmes for early school leavers. FÁS offered places on apprenticeships, traineeships and community employment schemes. Once unemployment began to rise again, FÁS adopted so as to tailor its practices to suit the market. In 2008 FÁS implemented a restructuring programme which contained three main provisions which

[836] *Labour Services Act* 1987 section 4.
[837] Dáil Debates Questions Industrial Training Programme 27 March 1990.
[838] See "Ireland and the EU 1973-2003 *Economic and Social Change"* Central Statistics Office Website available at http://www.cso.ie/en/media/csoie/releasespublications/documents/statisticalyearbook/2004/ireland&theeu.pdf last accessed August 2017.

aimed to assist those who had become unemployed to secure further employment, to manage the reduction in the apprenticeship scheme and also to ensure that the qualifications provided by FÁS were meeting the appropriate and highest standards.[839] FÁS also expanded its functions by providing a Special Initiative for Travellers. According to FÁS's 2008 Annual Report 74% of its participants progressed after their training to either employment, further training or starting their own business.[840]

It is clear that FÁS was fulfilling its key objective of retraining and upskilling individuals in seek of employment and FÁS was operating as a key SOE in Ireland. The SOE was introduced at a time that required intervention from the State and it improved the prospects for many people in Ireland and so the fundamental basis for the organisation is not called into disrepute. The organisation changed focus when unemployment became less of dominant issue with the organisation shifting its focus to providing training to allow people to upskill and retrain. In 2004 FÁS provided training in Competency Development Programme (CPD) to increase the transferable skill levels of low skilled workers.[841] However, this funding was expensive as between the period from 2005 – 2008 approximately €111 million was paid out for this training.[842] Ross and Webb challenged the retention of the organisation when half the training courses were empty during a time when unemployment was high in 2009.[843] When FÁS was dissolved in 2013 and replaced with SOLAS, the key objective of SOLAS is providing training and apprenticeships. This helps defend the reason why FÁS was retained during a period of full employment.

[839] Dáil Debates Joint Committee on Enterprise Trade and Employment 2 July 2008 at 2.
[840] See FÁS *Annual Report* 2008 p. summary.
[841] The Special Report No.73 of the Comptroller and Auditor General: *Internal Control and Governance in FÁS* (2009) p. 74.
[842] Supra note 841 p. 74.
[843] Ross, S. & Webb, N. *Wasters* (Penguin Books Ireland 2010) p. 71.

(2) The FÁS Controversy

The scandal unfolded in the media through an investigation published by news reporters Shane Ross and Nick Webb for the Sunday Independent on 23 November 2008. Their investigation uncovered the spending practices regarding foreign travel significantly breached of *the Code of Practice* 2001 for FÁS. The scandal highlighted how value for money was not achieved. This happened because:

"authorisation limits were breached when certain transactions were being initiated. There were deficiencies in the conduct of tender processes as when goods and services were being acquired, payments were made in the absence of supporting documentation. Confirmation orders for purchases already effected were issued in many instances. The system of risk management adopted by the Board in 2005 did not function effectively."[844]

Notable disregard for achieving value for money was in the area of foreign travel, business expenses and the use of credit cards. The excessive spending is detailed further below.

(i) Foreign Travel

€5.7m was spent on travel and other expenses in 2007.[845] With €640,000 of FÁS's budget was spent on transatlantic travel only during a four year period.[846] FÁS did not have a written foreign travel policy in place prior to 2009.[847] This is despite the fact that the Department of Finance issued procedures to be followed for foreign travel.[848] During an investigation carried out by the Comptroller and Auditor General, FÁS claimed they did not receive the circular on foreign travel. However, the policy was implemented in particular instances.[849] Investigations into travel arrangements in FÁS found that reasons for the use of business travel were not provided.[850]

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[844] Supra note 841 p. 9.
[845] Lavery & Neville "Fury grows over 'outrageous' FÁS spending on US junkets" *The Evening Herald* 25 November 2008.
[846] Collins & Keena "Molloy Resigns as Chief Executive of FÁS" *The Irish Times* 26 November 2008.
[847] Supra note 841 p. 13.
[848] Department of Finance Circular *Foreign Travel Policy* E105/10/97.
[849] Supra note 841 p. 32.
[850] Supra note 841 p. 35.

(ii) Business Expenses

FÁS used €1.7 million of its advertising budget using an alternative website for advertising jobs, even though their own website was adequate to do the task necessary at a much lower cost to the organisation. FÁS spent €600,000 on television commercials that were never used.[851] FÁS spent €48 million on adverting between 2002 and 2008, which could not be explained by the board.[852]
The investigation into expenses found that FÁS spent €35,000 on tickets for sporting and musical events.[853]

(iii) Credit Cards

FÁS spent €980,000 on credit cards from the between 2002 and 2008.[854] There was a lack of documentation for purpose of the expense but certain expense items were on limousine, payment of gratuities and payment of alcohol.[855] The lack of controls over credit card expenditure have been identified:

"in many cases, the documentation of the business purpose of the expenditure and of the recipient of the services was deficient, particularly in the case of meals and hospitality. The quality of documentation supporting expenditure by some cardholders was poor and original receipts were often not provided. There was evidence of extravagant expenditure that appears to have gone unchallenged."[856]

The FÁS scandal highlighted there were insufficient safeguards against excessive spending as it uncovered how public funds could be spent within a State body without being

[851] Phelan Irish Independent "Key figure at centre of FÁS scandal to tell all" *Irish Independent* 9 October 2009.
[852] Supra note 843 p. 65.
[853] Supra note 841 p. 44.
[854] Supra note 841 p. 41.
[855] Ibid p. 42.
[856] Ibid p. 47.

questioned or answerable for their actions. In response to this the Comptroller and Auditor General suggested that:

"FÁS could benefit from a fundamental review of its control regime. Recognising that the cost of control must be proportionate to its desired benefits, such a review should take account of an assessment of the risks which the organisation must address by means of fully functioning controls the imperative that the control regime underpin organisational effectiveness, the capacity of FÁS to respond to the demands of the client base it serves and the need to promote a positive culture of service and personal initiative."[857]

During the FÁS scandal serving board members were Rody Molloy Director General and Greg Craig director of corporate affairs. As Director General Mr Molloy was responsible for carrying out, managing the general administration and business of FÁS.[858]

The day after the media reported the story Molloy gave an interview in which defended the actions and spending[859] but the following day Molloy resigned as Director General on the 25 November 2008 following public outcry. However, when he resigned he was permitted to retain his luxury company car and was given a €1.1 million golden handshake.[860] It later emerged that the government did not seek legal advice prior to granting Molloy his demands for retiring from his post early.[861] Greg Craig was temporarily suspended following an internal investigation but was later reinstated after which he resigned.[862] Peter McLoone was head of the board of FÁS during the scandal.

It can be argued the State was ill equipped to deal with the scandal. It appears the Department was aware of the activities within FÁS, as the internal audit in 2006 identified breaches in government policy for achieving value for money and this was reported by the Comptroller and Auditor General.[863] Ministers were also associated with excess spending

[857] Ibid p. 29.
[858] Supra note 836 section 6.
[859] Supra note 835.
[860] Supra note 851.
[861] Quinlan "How the FÁS scandal unfolded" *Irish Independent* 29 September 2009.
[862] Supra note 851.
[863] The Special Report No.10 of the Comptroller and Auditor General: *General matters arising on audits: Non-commercial state sponsored bodies* (2008).

as they took holidays at the expense of FÁS with the then Minister Mary Harney taking the government jet on a FÁS trip to Florida costing €80,000.[864] Sean Gorman, the secretary general of the Department of Enterprise, Trade and Employment was part of the €2,255 spent by FÁS on tickets and drinks at a Robbie Williams concert.[865] It may difficult for Ministers to objectively curtail the practices of the board when the government themselves were benefiting from the excessive spending in FÁS. It highlighted that the government did not act on behalf of the public and securitise the spending by FÁS officials.

The FÁS controversy emphasised the lack of controls over governance standards being implemented in the SOE.[866] A poor reporting regime with a lack of accountability, the existence of conflicts of interest and with little monitoring of the board were identified by the Comptroller and Auditor General. FÁS was dissolved in 2013 and replaced with SOLAS to take over functions of providing training and assisting jobseekers find employment.

B. AN EXAMINATION OF THE KEY CORPORATE GOVERNANCE STANDARDS OF FÁS

Based on the events in FÁS the Code of Practice 2001 failed to provide structures, systems and processes that provide direction control and accountability. The FÁS scandal uncovered weaknesses in the corporate governance code; accountability provisions were inadequate as there was very little monitoring or enforcement of governance standards and provisions on value for money were completely ignored. This is accepted by the Comptroller and Auditor General who pointed out that:

"The examination found that FÁS had a governance structure that is consistent with its governing legislation and with the Code of Practice for the Governance of State Bodies. It had also a plan of internal control, which, if fully implemented, would have provided sufficient assurance that its transactions were processed in a safe and regular manner.

[864] Malony, Smyth & Brennan "Revealed: sky-high cost of FÁS Florida trip" *Irish Independent* 28 November 2008.
[865] Supra note 843 p. 55.
[866] Supra note 841.

However, failure to fully implement elements of the plan of control exposed FÁS to the risk of losses."[867]

(1) Failure to achieve value for money

FÁS failed to achieve value for money. This has been defined as:

"Value for money is a term used to assess whether or not an organisation has obtained the maximum benefit from the goods and services it both acquires and provides, within the resources available to it."[868]

Therefore, value for money does not mean the least amount of money has been spent but rather there is maximum efficiency and effectiveness for the money spent. This is recognised by the Department of Finance when they endorse criteria for achieving value for money based on economy, efficiency and effectiveness.[869] Economy is acquisition of resources in the right quantity and of a quality no higher than is needed for the job so doing things at a low cost.[870] Efficiency is a comparison of outputs to inputs. It refers to the extent to which the objectives of a policy are achieved so doing things the right way.[871] Effectiveness is defined in terms of the extent to which the objectives have been achieved and the planned benefits delivered, whether results are positive or negative.[872]

The *Code of Practice* 2001 provisions for travel stated that SOEs should:

"introduce controls to prevent fraud including adequate controls to ensure compliance with prescribed procedures in relation to claiming of expenses for business travel" [873]

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[867] Supra note 841 p. 9.
[868] Erlendsson "Value for Money Studies in Higher Education" (2002) Available at http://www3.hi.is/~joner/eaps/wh_vfmhe.htm Last accessed 13 August 2017.
[869] Department of Finance "Value for Money and Policy Review Initiative, Guidance Manual" Value for Money and Policy Reviewers' Network, Central Expenditure Evaluation Unit, (2007) Department of Finance.
[870] Ibid p. 33.
[871] Ibid.
[872] Ibid p. 34.
[873] Department of Finance *Code of Practice for the Governance of State Bodies* (Dublin 2001) appendix B p. 26.

Governance standards at that time provided extra guidelines on State procedure for travel, procedures for procurement and disposals of assets by third parties.

Regarding the procurement process a requirement was in place for competitive tendering and value for money in spending and it was the responsibility of the board to ensure that good procurement processes are followed.[874] Despite this, FÁS's former executive Greg Craig stood by their decision to use the alternative website *Jobs Ireland*, rather than their own for advertising job vacancies as he claimed this website would attract skilled workers worldwide. He has also commented that it was with the full support of the board.[875]

The activities carried out by FÁS are inconsistent with an SOE that should achieve value for money. McDonough outlines that SOEs can achieve value for money through productive and allocative efficiency.[876] Productive efficiency requires SOEs to use the least amount of resources and allocative efficiency so that a maximum benefit can be produced.[877] This raises the question of the board's actions during this time as the board is fully accountable for adhering to the governance regime**.**

(2) Lack of Board Accountability

"The purpose of accountability is not to prevent the government from governing, but for public officials to account for their stewardship."[878] During the most substantial breaches of corporate governance the board comprised a chairperson and 16 ordinary members appointed by the Minister for Enterprise, Trade and Employment.[879] The board composition of FÁS from 2002 to 2008 comprised:

"four employers' representatives,

[874] Ibid principle 4 p. 4.
[875] Supra note 843 p. 63.
[876] McDonough, D. "Corporate Governance and Government Owned Corporations in Queensland" 10(2) (1998) *Bond Law Review* 272 p. 282.
[877] Ibid.
[878] Finn, P. "Public Trust and Public Accountability" (1994) 3(2) *Griffith Law Review* 224 p.234.
[879] Dáil Debates Joint Committee on Enterprise, Trade and Employment 4 December 2008 p. 3.

four trade unions' representatives,
one person representing youth interests,
two representatives of the Minister,
one representative of the Minister for Finance,
one member representing educational interests, appointed by the Minister following consultation with the Minister for Education and Science,
one member representing social welfare interests, appointed by the Minister after consultation with the Minister for Social and Family Affairs,
two FÁS employees."[880]

Griffith points out to achieve a satisfactory level of accountability this will sometimes require intrusion into the affairs of public bodies.[881] This will have to be balanced with responsible government to prevent excessive interference into SOEs. This balance may be achieved by preventing the government's involvement in the day to day running of SOEs and so its monitoring functions are not undermined.

An essential aspect of accountability within SOEs is that integrity is not compromised, and while the State has a central role in the accountability process the government has to entrust part of this role to the board. It has been noted that the integrity of financial statements depends on the characteristics of the board and the audit committee.[882] This is accurate in the case of FÁS, despite the publicity surrounding FÁS the wasteful spending practices only came into the public domain after the media requested the internal report under the *Freedom of Information Act*.[883]

However, it was not the first time that their corporate governance practices have been called into question. The internal audit of FÁS revealed breaches of the procurement process as far back as 2002.[884] What is interesting about the breaches found in the internal audit in 2002 is that the then Director General of FÁS did not report these inconsistencies

[880] Supra note 841 p. 47.
[881] Supra note 878 p. 235.
[882] Zalata, A. & Roberts, C. "Internal Corporate Governance and Classification Shifting Practices" (2016) 31(1) *Journal of Accounting, Auditing & Finance* 51 p. 54.
[883] Committee of Public Accounts (4 December 2008).
[884] Supra note 863 p. 18.

to the Minister for Enterprise, Trade and Employment or Auditor General as corporate governance practices requires. Corporate governance standards stipulated that once the internal audit reveals any inconsistencies, the board should report them to the relevant public authorities[885] and to the Comptroller and Auditor General within six months.[886] The chairperson of the board is responsible for the body's system of internal financial control.[887] The chairperson of each State body is obliged to provide the Minister with annual report and accounts of the body affirming that all appropriate procedures for financial reporting, internal audit, procurement and asset disposals are being carried out.[888] However, the Auditor General did not become aware of these issues for two years. Instead the Director General decided to conduct his own investigation into the matter.[889] The motive for conducting this second report remains unclear. The department had uncovered these variable patterns in the spending of their budget,[890] and so it would appear futile to carry out another report. The matter perhaps would be dealt with more appropriately, using with the external supervisory functions of the Auditor General. However, the former Director General has defended his actions by stating that he sought to revise their internal procedures.[891]

Insisting that proper procedure was followed the Auditor General claimed that he sent all completed reports to the Comptroller and Auditor General.[892] He later stated out that internal audits are not for public viewing as they contain information that if released into the public domain could be damaging to the organisation as he considered without viewing the whole audit, the media could take it out of context and give a distorted impression of reality.[893] The reason given to explain such a remark is that he claims that, by their nature, internal audits give a robust and critical insight to the organisation, making it necessary for

[885] FÁS is accountable to the Minster for Enterprise, Trade and Employment. Its accounts are reviewed by its internal audit department, the Comptroller and Auditor General.
[886] Supra note 873 principle 10.
[887] Ibid principle 10.2.
[888] Ibid.
[889] Supra note 863 p. 18.
[890] Ibid.
[891] Ibid.
[892] Dáil Debates Joint Committee on Enterprise, Trade and Employment 2 October 2008 p. 4.
[893] Ibid.

them to be adopted before released into the public domain and he criticises how this process could not happen because of the *Freedom of Information Act*.[894]

This questions the usefulness of an internal report if given once issues are raised they can be ignored by the board. It is not surprising that stronger action was not taken by the board once the internal report was presented to them and so once inconsistencies of practices are brought to attention in the internal audit, the board of directors may not be the best people to address the problem. Keena indicated that once this internal audit was presented, Molloy's anger was not directed to the fact that there was reckless expenditure of money, but it was directed at the auditors and he strongly criticised their report. However, any issues he had with the audit were refuted and the audit committee rejected and they stood by its accuracy.[895] But if internal audits are carried out correctly, they are a very good means of monitoring SOEs, as the internal audit identified a lot of the malpractices carried out by the organisation and internal audits are useful as they will make recommendations on how to improve any areas they consider open to misuse. But internal auditing is only effective once all the records are made available to the audit committee and an issue of this nature was found with FÁS's records. It was alleged that financial records for the period from January 2005 to August 2006 were not available to the audit committee. FÁS's board later stated that these problems were resolved and the committee had access to all records.[896]

There was a perceived impression of good governance as the board did not flag any internal issues on the governance within FÁS. The structure of governance in place gave the perception of standards being implemented but this was only visible compliance. One of the main shortcomings in the governance code in place at that time was in regard to the internal report. The *Code of Practice* 2001 required the board to confirm annually to the Minister that appropriate internal financial controls were in place.[897] The actions of FÁS completely undermined this principle as their annual reports confirmed compliance with this governance provision but it is clear this was effectively only lip-service. There were

[894] Ibid.
[895] Keena "High-Flyers at FÁS Are Brought Down To Earth" *The Irish Times* 26 November 2008.
[896] Oakley "FÁS Financial Practices to Come under New Scrutiny" *The Irish Times* 7 September 2008.
[897] Supra note 873 principle 10.2.

several governance issues that were disguised by the board and they chose not to report them and this allowed their practices to continue uninterrupted. It has to be questioned why practices of the Director General were able to continue for so long without interference. Corporate governance standards that were in place did not have functional capacity to stop the activities, but what was in place should have circumvented incidents if governance codes had been strictly adhered to. Corporate governance standards provided better accountability provisions than what was implemented by the board. This indicates that the agency problem between the board and Minister needs to be addressed.

C. FACTORS WHICH LEAD TO THE FÁS SCANDAL

(1) Agency Theory

Traditionally Agency theory focuses on the relationship between the principal and agent, where the agent performs tasks on behalf of the principal.[898] However, in SOEs complexities are added to Agency theory as there is a dual principal agency relationship. This relationship has been characterised by Cuervo-Cazurra et al.[899] SOEs are owned by citizens of the country who as principals task politicians on behalf of the State to achieve the social and economic objectives of SOEs. As citizens have no contractual mechanisms with politicians, objectives and interests do not always align. Politicians as principal task managers of SOEs based on their interest, and managers act as agents for politicians.[900] Therefore, Agency theory in SOEs needs to extend to range of principal agent sets of relationships that exist.

Examining the problems that arose in FÁS, the agency issues of individuals and the pursuit of their own objectives was instrumental to the scandal. There is an expectation that agents will act in the best interests of the principal and not pursue their own interests. However, this will not be achieved by depending on goodwill of a board and so checks and mechanisms need to be in place to ensure this happens. If corporate governance codes are

[898] Meckling, J. "Theory of the Firm: Managerial Behaviour, Agency Costs and Ownership Structure" (1976) 3 *Journal of Financial Economics* 305.
[899] Cuervo-cazurra, A., Inkpen, A., Musacchio, A. & Ramaswamy, K. "Governments as Owners: State-owned Multinational Companies (2014) *45*(8) *Journal of International Business Studies* 919 p. 919.
[900] Ibid p. 931.

going to protect interests of shareholders, a board must recognise the authority provided by standards. A balance must be achieved between the right to monitor and the right to control, as there cannot be undue political interference into the running of SOEs. By creating SOEs, the State is accepting of a loss of control but the actions of agents must be monitored.

Essentially, as Agency theory focuses on the separation of management and control, the owners should be a central point of concern. Corporate governance should incentivise systems and monitor to protect shareholder interests and this authority must be exercised by the board from the point of protecting shareholder interests. With SOEs, there is a competing set of dealings, as a board has to maintain relationships with several groups that are affected by its decisions and so Stakeholder theory embraces a wider group who are impacted directly and indirectly by the actions of SOEs. For SOEs, the shareholder is the State but the actions should be in the best interests of stakeholders, blurring the distinction to the traditional shareholder/stakeholder roles. For SOEs, citizens have no say in the election of board members for SOEs.

FÁS had two codes of conduct in place when the scandal broke; the Code of Business Practice for Directors[901] and a Code of Ethics for employees.[902] However, board behaviour of FÁS indicated that they were disregarded, as self-interest was central to actions and decisions made and that shareholders cannot rely on boards to do what shareholders expect.

In the context of SOEs, it can be argued that shareholders expect funds to be spent in the best interests of citizens, value of money to be achieved and for SOEs to add value to the Irish State, not retract from it. SOEs should be expected to fulfil the State's social and economic reasons for establishing the entity so there will be development goals along with economic goals.

[901] Supra note 873.
[902] *The Code of Practice for Employees* 2003.

(2) Soft Law Issues highlighted by the FÁS saga

FÁS failed in the application of governance standards. While the Code does not have a legislative basis and SOEs are only required to implement governance standards that are relevant, it is clear for the analysis above, that governance provisions applies to FÁS but the board completely chose to disregard them,[903] indicating that accountability provisions were insufficient. While the then Director General claimed they were not in breach of any rules, they clearly did not implement the *Code of Practice for State Bodies* 2001. This illustrates that where a board does not implement governance standards, there is nothing holding them accountable. Predominately, issues that arose were in the context of the inability to prevent excessive spending, travel protocols and procurement process, were breached as outlined earlier in the chapter.

The problems associated with implementing governance on a soft law basis were brought to the forefront in the FÁS saga. As outlined in previous chapters, it is difficult to ensure governance will always be implemented when essentially the key element of its application is the dependence on goodwill of the board on their desire to implement governance principles. Without penalties or repercussions for not implementing governance codes execution of principles may move down the list of priorities for the board. This then becomes a contentious issue, as the ramifications for not implementing governance standards manifests in different areas.

It is undoubtedly the manner in which FÁS spent money that drew media attention and highlighted the lack of control over the boards spending. FÁS spent over €10million on advertising and had credit card limits of over €76,000 for senior executives.[904] FÁS set up an alternative website for jobseekers at a cost of €1.7 million which essentially duplicated the functions of their own website.

The persistent reckless spending which included spending on items, which did not have a direct link to the SOEs function, caused a major public backlash. Determining what is

[903] Supra note 873 principle 10.2.
[904] Drennan "FÁS bosses will not face lash for lavish expenses" *Irish Independent* 8 February 2009.

acceptable expenditure is a subjective undertaking and so while certain expenditure went outside the ambit of reasonableness, it may not be too far removed from standard practice for boards of major entities. However, governance standards required SOEs to be careful with spending, being economical as possible.[905] It is apparent FÁS enjoyed complete freedom and disregarded a need for efficiency in their co-ordination of the corporate governance code. It was evident that FÁS's former Director General, Mr. Rody Molloy, was spending the budget in a manner not within the spirit of good corporate governance.

As outlined above, FÁS adopted and made changes to suit the economic climate but the budget allocated to FÁS did not reduce, while the rate of unemployment fell FÁS's budget grew and reached one billion euro.[906] However, when questioned at the time on the amount of money the organisation received, the former Director General Mr. Rody Molloy rigorously defended the use and allocation of their budget. Molloy gave a loose breakdown of the billion euro budget. He claimed that €216 million was spent on training people for employment, €358 million was spent on Community Employment (CE) schemes,[907] which are schemes for long termed unemployed people to seek part-time employment through different forms of community work.[908] €219 million was spent on apprenticeships. While the breakdown gives an insight into what FÁS is spending its money on, the figures do not add up to a billion euro. Tracing the remainder of the budget emerged at different stages over the years; €5.7million was reportedly spent on travel and subsistence in 2007.[909] Molloy later admitted that such expenditure was not appropriate.[910]

It identifies that there is a conflict of interest due to the close proximity of a board being accountable to a government who does not question the spending it is providing funding for. An SOE is essentially fulfilling functions that have been provided by the Department, who is also responsible for funding and monitoring the SOE. This leads on to address how there was a lack of monitoring within FÁS.

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[905] The Department of Finance *Code of Practice for the Governance of State Bodies* (Dublin 2009) principle 15.
[906] Supra note 840 p. summary.
[907] Dáil Debates, Committee of Public Accounts 2 October 2008.
[908] Citizens Information www.citizensinformation.ie.
[909] Dáil Debates Committee of Public Accounts 6 November 2008 p. 3.
[910] Supra note 883 p. 6.

(3) Monitoring Issues

The board did very little to address governance problems within the SOE. Regarding the reckless expenditure of money, the board was aware of the procedures that were followed and it appears that they approved of the decisions made on the expenditure made.[911] Clarke points out that it is not uncommon for board members not to challenge the actions of executives.[912] This is true in the FÁS saga as Greg Craig, a member of the board of FÁS, stated that the board was aware of the way the procurement process was carried out and approved of it for years, despite the fact that this was in breach of procedure.[913] This highlights the problem when governance standards are implemented on a soft law basis without a strong accountability regime. The board suffered no consequences and were not monitored and contributed to the excessive spending escalating to the level it reached. In 2008, the board of FÁS took steps to address the procedure practices within the organisation and requested that:

"the board has approved a revised set of procurement procedures that include a requirement for managers to make annual declarations of compliance.

Training workshops have been held to increase the level of awareness of those procurement procedures.
Policies relating to the use of credit cards and revised procedures governing foreign travel were adopted by the Board during 2009 and the use of credit cards curtailed."[914]

This research indicates that the board did not always fulfil their duties as directors in accordance with corporate governance standards in place and directors' alignment of their interests was flawed. Looking to how the board actually fell short of their commitment to achieve value for money happened on many occasions, as outlined above. It is the board's duty to ensure effective leadership within a framework of prudent controls that meets the

[911] Keena "FÁS Official gives his side of the story to PAC" *The Irish Times* 9 January 2009.
[912] Clarke "Lessons Learned - The Corporate Governance Code for Credit Institutions and Insurance Undertakings" (2011) 33 *Dublin University Law Journal* 172 p. 177.
[913] Supra note 911.
[914] Supra note 841 p. 9.

values and obligations of the company, so the board is making the decision to steer away from accepted governance principles. Therefore, it is clear that the Director General of FÁS was aware that he was in breach of corporate governance whilst carrying out his uncontrolled spending. Molloy issued a code of ethics for FÁS in 2003 which contained provisions on achieving value for money. It stressed that employees or their family were not to benefit from the organisation in any unsuitable manner.[915]

The internal audit carried out by FÁS confirmed that their employees were recommending contractors for work that had to be carried out, indicating that contacts were being awarded to the benefit of certain companies and individuals associated with the organisation. This was a breach of the procurement process as they were not obtaining the best value for contracts, rather they were given to people connected to the organisation. By the board accepting this, it bolsters the opinion that the board was not operating with the best interests of stakeholders in mind.

The chairman of the board of directors took responsibility for the practices of the organisation and Molloy resigned as Director General of the organisation. It was necessary for Molloy to step down as director general as there was no basis for the claim that he did not realise that he was in breach of regulations. To date, the board have received no penalty for activities carried out by the board. After the scandal Sauls, a non-executive director and chairman of the audit committee of FÁS, guaranteed the competence of the board going forward.[916] He claims this for the reason that there is a clear separation of powers between the audit committee, the internal function and the executive management.[917]

It is also necessary to examine the role NEDs had to play during the FÁS malpractices. The function of NEDs is to act as independent watchdogs to ensure organisations are conforming to standards set down, such as the internal audit process, the suitability of arrangements to eliminate risks that might arise, and analyse reports of particular

[915] Barrington & Burke "Molloy Introduces Ethics Code of FÁS before Resignation" *The Sunday Business Post* 21 December 2008.
[916] Committee of Public Accounts (6 November 2008). The board comprised a chairperson and 16 ordinary directors.
[917] Ibid p. 6.

concern.[918] NEDs as part of the board have always played an important role in maintaining high standards of corporate governance standards as they "constructively challenge the performance of management and are required to satisfy themselves with the integrity of financial statements."[919] The importance of NEDs is evident as they bring an objective view to the board. The definition the role of NEDs has been described as providing two functions: firstly, to monitor decisions made by the executive directors and secondly, to add value to the board and the company with their own input.[920] These two functions are recognised in the *Code of Practice* 2001 which asked NEDs to "bring an independent judgement on issues of strategy, performance and standards of conduct."[921] However, this is heavily dependent on NEDs actually performing their duties as expected.[922] The OECD highlight the importance of NEDs as they do not represent particular stakeholders but are there because they contain certain skillsets and competencies to the board.[923]

So how did the board of FÁS interpret the requirements of NED as determined by the *Code of Practice*? It is suggested that there should be two to three NEDs on the board, depending of the size. What is categorised as an independent NED is open to question. There is really nothing in the Code to clarify this other than there being no conflict of interest. However, Mallin points out that there is no need to doubt their independence if their role includes working with an organisation to further its objectives.[924] But the growing responsibility placed on NEDs to highlight and prevent any irregularities can only be assured if the NEDs work with the executive directors to have a full understanding of the internal workings of the organisation. The board structure of FÁS at the time of the governance scandals met their requirements set out in the *Code of Practice*; there were three NEDs on the board and the Audit Committee was composed of three NEDs.[925] But it is clear that there is little to suggest that NEDs attempted to curtail the board's activities.

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[918] Financial Reporting Council *The Combined Code on Corporate Governance* (London 2008).
[919] Financial Reporting Council (UK) *The UK Corporate Governance Code* (2014) Listing Rule A.4.
[920] Mallin, C. *Corporate Governance* (OUP New York 2007) p. 132.
[921] Supra note 873 p. 16.
[922] Liu, Wang & Wu "Removing Vacant Chairs: Does Independent Directors' Attendance at Board Meetings Matter?" (2016) 133(2) *Journal of Business Ethics* 375 at 375.
[923] OECD *Boards of Directors of State-owned Enterprises: An Overview of National Practices* OECD Publishing (Paris 2013) at 49.
[924] Supra note 920 p. 132.
[925] FÁS *Annual Report* 2009.

The Comptroller and Auditor General investigated the malpractices of the board of FÁS and they exposed the following:

"Authorisation limits were breached when certain transactions were being initiated. There were deficiencies in the conduct of tender processes when goods and services were being acquired. Payments were made in the absence of supporting documentation. Confirmation orders for purchases already effected were issued in many instances. The system of risk management adopted by the board did not function effectively."[926]

This highlights governance failures across a number of areas. The board was able to manipulate standard operating procedures in line with its own agendas and the board was able to do so without intrusion or question. Based on the foregoing, this thesis recommends that an independent monitoring body is required for overseeing governance functions of SOEs. NewERA has been established to assist and provide advice to the government but only in relation to the following State bodies; ESB, Ervia, Irish Water, EirGrid, Bord na Móna, and Coillte. However, chapter three focuses on how other jurisdictions have overseeing bodies dedicated to monitoring SOEs. For example, in New Zealand the Crown Ownership Monitoring Unit (COMU) and acts as an agent for the government and assists with the supervisory role of the government. Expanding the role of NewERA in a similar respect to the COMU would really advance the level of monitoring of SOEs in Ireland.

(4) Lack of Enforcement of Corporate Governance Standards

Griffith sees compliance as a means of establishing internal mechanisms to detect and prevent violations of law. However, the scope of compliance is greater than enforcement of rules and regulations, but containing a control function aimed at minimising misconduct.[927]

Griffith recommends putting disclosure policies in place will provide the opportunity to understand what works in compliance.[928] Governance standards are of little value if the

[926] Comptroller and Auditor General *Special Report Internal Control and Governance in FÁS* 2009 p. 9.
[927] Griffith, S. "Corporate Governance in an Era of Compliance" (2016) 57(6) *William & Mary Law Review* 2075 p. 2082.
[928] Ibid p. 2139.

enforcement programme underpinning it is not implemented effectively. The issue of enforcement of corporate governance is well recognised and Griffith sees the problem as governance arrangements should be agreed with shareholders and managers as current compliance methods are outdated.[929]

In privately owned companies, there is control by the market leading to enforcement of the codes, as well as shareholders acting as vigilant watchdogs over their money. However, the same supervision is not always present in SOEs. Even though much of the same code provisions apply to both entites circumstances, the same initiatives do not transfer into SOEs. Therefore, by drawing on what works for private companies it is necessary for the activities of SOEs to be improved and closely monitored. The Minister was ultimately responsible for overseeing expenses in FÁS under its establishing legislation:

"members of the staff shall be paid, out of the moneys at the disposal of An Foras as the case may be, such remuneration and allowances for expenses incurred by him as An Foras, as the case may be, with the consent of the Minister and the Minister for Finance, may determine."[930]

This indicates that the Minister is responsible for setting both remuneration and more importantly the expenses incurred by FÁS. It is clear that this was ignored as details of first-class flights for board and their family, luxury holidays, golf trips and spa treatments were paid by FÁS.[931] The Labour leader at that time suggested the past three Ministers for Trade and Enterprise should accept responsibility for the failings in FÁS.[932]

A better method is required for the Minister to ascertain how the board have implemented governance standards. Providing an annual statement to the Minister indicating that governance codes have been implemented without further guidance notes is insufficient. To strengthen both the monitoring and accountability regime, additional structures should be in place, which will be addressed in the following chapter.

[929] Ibid p. 2079.
[930] Supra note 2 section 7(2).
[931] Supra note 845.
[932] "Government urged to take responsibility for FÁS scandal" *Irish Independent* 26 November 2008.

(5) A review of the updates in Code of Practice for the Governance of State Bodies from 2001 to 2009.

TABLE B		
	Code of Practice for the Governance of State Bodies 2001.	**Code of Practice for the Governance of State Bodies 2009.**
The principle of comply or explain	SOEs are expected to comply with the Code but principles that are "not appropriate or fully relevant, where agreed with the Minister do not have to be applied.[933]	Comply or explain principle not expressly mentioned but an onus on SOEs to confirm compliance with Code to Minister.[934]
Structure of Codes	The Code lists 12 provisions, which includes dealing with internal audits, remuneration and directors' fee and reporting arrangements. A framework for best practice is provided in the appendix.	The Code is presented in the form of a guiding principle supported by provisions. The Code takes a narrower focus by setting out the report under the headings of the board of directors, remuneration, risk management, accountability, internal control and internal audit. Relations with the Oireachtas and the Minister

[933] Supra note 873 p. 1 & 2.
[934] Supra note 905 p. 1.

		Specific Procedures to be followed by State Bodies.
Board Responsibility	The board is responsible for providing the Minister with a balanced and understandable assessment of SOEs.[935]	Board responsibility is increased by setting a strategic plan and to ensure financial accounts give a fair and accurate position of the SOE.[936]
Risk Management	The 2001 code requires a board to have a risk management policy in place.[937]	The updated code introduces guidelines on Risk Management Policy.[938] This includes establishing a Risk Committee, ensuring competencies of the board and seeking external advice.[939]
Annual Reports	State bodies were required to prepare annual reports.[940]	Annual reports were required to be published. Updated requirements meant the details of board fees were to be disclosed along with expenses paid to the board.[941]
Board election	The only requirement is for NEDs should be	There are no standards on re-election of board members.

[935] Ibid p. 15 principle 1.
[936] Supra note 905 p. 4 principle 2.12.
[937] Supra note 873 principle 1 p. 15.
[938] Supra note 905 principle 8 p. 11.
[939] Supra note 905 principle 8 p. 12.
[940] Supra note 905 principle 5.8 p. 6.
[941] Supra note 905 principle 7.7 p. 11.

	involved in board appointments.[942]	
Independence	Directors are required to report conflicts of interest.[943]	The Code restates that interests of directors should be disclosed and potential conflicts of interest should be managed by the board.[944]
Non-executive directors (NEDs)	The 2001 code requires at least three independent NEDs on the audit committee.[945]	NEDs feature in the 2009 standards reemphasising the 2001 provision with a significant duty of becoming part of the audit committee.[946]
Remuneration	A remuneration committee should be in place. Remuneration for the chairperson is set in accordance with Government policy.[947]	The code restates that remuneration is set by the Minister for the board and remuneration for the chairperson is set in accordance with Government policy.[948] The Code refers to the "*Guidelines on Contracts, Remuneration and other Conditions of Chief Executives and Senior Management of Commercial*

[942] Supra note 873 p. 16 principle 1.
[943] Ibid p. 17 principle 3.
[944] Supra note 905 p. 3 principle 2.7.
[945] Supra note 873 p. 12 principle 19.
[946] Ibid p. 12 principle 10.
[947] Ibid p. 9 principle 9.
[948] Supra note 905 p. 9 principle 7.

		State Bodies" (2006), for guidance of remuneration.
Stakeholders/ Shareholders	The board is required to reflect the shareholders objectives and strategic mandate.[949]	There is limited reference to the requirement to act in the interest of stakeholders.[950]
Value for money	"introduce controls to prevent fraud including adequate controls to ensure compliance with prescribed procedures in relation to claiming of expenses for business travel" [951]	"Whether commissioning public services or providing them directly, State bodies have a duty to strive for economy, efficiency, transparency and effectiveness in their expenditure."[952]
Travel Policy	The only reference to business travel is to ensure compliance with prescribed procedures.[953]	A new section of guidelines in relation to travel are provided in the Code, with a framework appended to the Code.

The table above highlights how code provisions were dealt with in the 2001 and the 2009 Code of Practice for State bodies. Key updates relevant to this thesis dealt with provisions on the board of directors, travel policy and audits which are explored further below.

[949] Supra note 873 p. 10.
[950] Supra note 905 p. 4 principle 2.13.
[951] Supra note 873 appendix B p. 26.
[952] Supra note 905 principle 15.
[953] Supra note 951.

(i) Provisions dealing with the Board

The 2009 code places additional guidelines on expenditure and how it should be monitored by the board. This was to be done from the introduction of performance measurement system to assess the effectiveness of major items of expenditure, which should be reported to the board.[954]

Written Codes of Business Conduct was required to be circulated to all directors and staff of State Bodies should:

"refer those people to the need to comply with relevant legislation and regulatory requirements and should identify relevant provisions regarding conduct/conflicts of interest in the State Body's governing legislation,

make clear that certain obligations to the body regarding, in particular, the non-disclosure of privileged/confidential information, continue after a person ceases to be a director or employee

recommend the avoidance, for a reasonable period, of further employment where potential for conflict of interest arise."[955]

(ii) Travel Protocols

Policy objectives for travel were more adequately defined. The 2001 code only prevented fraud, whereas the 2009 code required efficiency and effectiveness.

The 2009 Code contained guidance on travel policy, it perhaps can be considered one area of the standards that provides clear unequivocal standards and its key relevant provisions included:

[954] Supra note 952 provision 2.5 p. 3.
[955] Supra note 873 appendix II.

"State bodies should also be cognisant of the need to achieve economy and efficiency in their expenditure on official travel and should have a policy in place that covers both foreign and domestic travel."[956]

The 2009 code made the board responsible for ensuring travel policies were complied with:

"The board of the State body should satisfy itself that the principles of its travel policy are adhered to and is effective in insuring that the State body is fully complying with the policy."[957]

The Code stated that travel policy limits excessive spending and requires maximum use to be made of public transportation. Air fare should be selected on the criteria based on the most cost-effective overall and business class can only be considered in exceptional circumstances and the use of premium rates can rarely be justified.[958]

(iii) Audit Requirements

If the board act as stewards for SOEs, one of best methods for accessing the performance of SOEs is the internal audit:

"The internal audit function should serve the best interests of the State. In order to demonstrate that due professional care has been taken in performing its work, it is necessary to have comprehensive records of activity showing that the work has been performed in accordance with accepted standards of best practice."[959]

Provisions for the audit committee were increased in the 2009 Code and the update required the board to satisfy itself that:

[956] Supra note 873 appendix IV.
[957] Supra note 905 appendix IV.
[958] Ibid.
[959] Supra note 905 appendix III.

"at least one Committee member has recent and relevant financial experience,
the Committee monitor and review the effectiveness of the State Body's internal audit activities,
any internal audit/audit items that relate to the Board's areas of responsibilities should be communicated to the Board as soon as identified."[960]

[960] Supra note 905 principle 10 p. 13.

D. CONCLUSION

It is clear that the governance framework in place could not prevent or curtail the malpractices that occurred in FÁS. The events in FÁS highlight that accountability provisions require strengthening.

From an examination of FÁS and the governance issues in place, it is evident they were not adhered to, most notably regarding achieving value for money and travel arrangements. The *Code of Practice* 2001 had guidelines, albeit limited in their scope, in place that would have reduced many of the corporate failings in FÁS if accountability provisions worked as effectively as intended. While the board must report to the Minister annually on their performance, this does not provide assurance that governance issues have been dealt with, thus highlighting the issue of enforcement with existing governance standards. This indicates that what will be critical for governance to be successful is monitoring by the government, suggesting that accountability is the basis for corporate governance for SOEs.

In line with a move to increase implementation of governance standards, interventions from overseeing bodies should increase the desire of the board to engage with governance standards. If a board expects additional queries from an external body, this should reconcile the board's annual implementation of governance with what is required from the governance code. To aid the board, risk assessments should be carried out which highlight potential weaknesses in a governance model for SOEs.

Focusing on and addressing the agency issue of the board should also help prevent malpractices of a board. One method of being able to improve this is by making directors accountable for their actions. Moving the responsibility onto directors should result in a board making calculated decisions that are in the best interest of SOEs so that they will be able to defend any decisions made. It is clear that existing framework is ticking the right boxes but it is clear that it needs to be strengthened. Learning from the FÁS saga, moving forward, a government could withhold a portion of SOEs annual budget until it is satisfied changes are made for the future year and they have better procedures in place to ensure

compliance with governance standards. This is a way of availing of penalties that may be more closely aligned to hard law but still retaining the characteristics of soft law.

To regain trust in SOEs, there should be a credible system of internal control that is monitored by the government. The FÁS scandal triggered a shift on the focus of corporate governance standards for SOEs, the lack of control over both spending and the procurement process was highly criticised. This chapter has focused on the shortcomings of governance standards relative to FÁS and highlights potential dangers where a lack of effective management is in place and highlighted weakness in the *Code of Practice* 2001. This should be addressed by strengthening accountability and enforcement mechanisms, which will be focused on in later chapters.

It is clear that the main controversy surrounding FÁS was the manner in which it was able to spend money without restrictions or curtailments. It found that while it was the board's duty to report fully on the governance of the organisation, this was not done on many occasions. There was a lack and unwillingness by the board to ensure prudent and ethical allocation of resources. What is interesting about the FÁS saga is that the board claimed there were no illegal activities within the black letter of the law but they have fallen short and there were breaches within the spirit of the law. This conceivably highlights the limitations of corporate governance. The incidents that occurred should have been detected and stopped at a much earlier stage, but this was not the case because the 2001 Code lacked any real force to ensure compliance as accountability provisions are too weak. After taking a look at the case study of FÁS, was a matter of bad governance practices or a matter of governance not being good enough to prevent the activities? It was found that provisions had a fundamental flaw: they aimed to prevent certain practices but could do little to remedy a situation once breaches occurred. The problem appears perhaps that there are few repercussions for a CEO who does not follow corporate governance to a high standard.

Confidence has been lost in the corporate governance for SOEs but this does not have to be detrimental for all SOEs. Corporate governance is pivotal for SOEs, but perhaps it is time to raise the bar on corporate governance, it is time to put penalties in place for not

complying with corporate governance standards and copper fasten accountability practices and it is up to the State to set the example.

It is common for organisations to want to maximise their independence and minimise their accountability but there should be a better balancing of interests. By the government setting up boards and committees, they should not consider their duty discharged, and use it as a vehicle for not taking accountability for the mismanagement that has occurred. What becomes even more surprising is that the Comptroller and Auditor General found that the governance structure of FÁS was consistent of what was required from *The Code of Practice for the Governance of State Bodies* 2001. This raises questions as to what value corporate governance standards can add when FÁS directors were liberally spending money on personal luxury items and there was no breach of corporate governance standards.

This questions the model of governance after the scandal. While it may be difficult for a government to ensure there is adequate governance of SOEs, perhaps there should be key indicators in place that can warn Ministers when governances is not being met. Perhaps the standards should move to a mandatory basis to improve corporate governance standards in SOEs and to prevent something of the scale of FÁS occurring again, particularly in SOEs that have a poor record of compliance. A questionnaire, along with the Code, can be used in aiding the board in achieving a high standard of governance provided enforcement and accountability is achieved.

A common theme that leads to corporate crisis is a lack of accountability and insufficient audits, where internal audits were carried out and the results were hidden by the board. To circumvent such problems arising in the future, the standards have included what can be considered comprehensive guidelines to ensure accountability and accurate auditing. Such guidelines ensure that each department sets out the roles of their accounting officers and places the responsibility on the preparation of appropriation accounts rather than placing the responsibility on the board.[961] This is in line with the same reasoning as to why it is

[961] Supra note 905 p. 12.

only NEDs who should sit on the audit committees of State bodies,[962] as it would go against the principle of an audit if the executive directors were auditing themselves, and auditing allows NEDs to continue with the supervision duties even though the standards only require one out of three of the audit committee to have relevant financial experience.[963]

This chapter has focused on the board of FÁS and how corporate governance standards were implemented. It is clear the Code of Practice 2001 was insufficient to establish good governance as there is too little accountability and enforcement provisions within these standards. Therefore, the following chapter will address how to strengthen accountability governance provisions for boards of SOEs to provide an overall better standard of governance.

[962] Ibid p. 13.
[963] Ibid.

CHAPTER 6
A FRAMEWORK FOR ADDRESSING THE ACCOUNTABILITY DEFICIT IN BOARDS OF SOEs

A. INTRODUCTION

This thesis highlighted that previous versions of the *Code of Practice* failed to provide an adequate governance framework which resulted in an accountability deficit. The *Code of Practice* 2001 and 2009 contained basic standards and it is necessary to construct a framework model that can be used for SOEs, that contains principle-based standards that establish broad rules but provides specific treatment on implementing these rules. This requires having standards in place that are detailed enough so a board will know how to implement them. There should be a move away from the checklist only mindset to governance and to strengthen this, there should be a more formal move towards implementing standards. There should be a move to establishing fundamental principles that set the presumption that standards will apply. Taking this approach, government departments should be clear on which governance principles have been implemented by a board.

This thesis has found board accountability is a key governance mechanism central to a successful framework model for SOEs as it pushes a board act in the best interests of an SOE and ensures a board is responsible for its actions. Accountability delivers so many mechanisms that become the driving force of a successful governance regime. Accountability brings responsibility, answerability and sets parameters for a board to do act within permitted criteria. A greater emphasis on transparency provides better access to information on SOEs.

If there are adequate accountability structures, this infers that a board is being actively monitored. Monitoring a board insinuates the threat of repercussions for board members who do not fulfil their duties. Therefore, there must be structures in place when board members fall short of their objectives. Governance standards must contain principles that deal adequately with accountability and transparency, that result in a unified board approach with individual board responsibility. The requirement of being able to enforce

governance standards is a contentious issue, as governance for SOEs operates on a quasi-legal basis, with no sanctions for not enforcing governance standards. In light of reviewing the flaws in the governance framework for SOEs, the aim of this chapter is to set out how better provisions on accountability can influence and is critical to the corporate governance regime for SOEs.

With the dual agency issue, accountability for SOEs takes another dimension which the *Code of Practice* remains silent on. Dual agency in SOEs is the responsibility of the relevant Minster to monitor the board of SOEs for the government as regulator and behalf of citizens as ultimate owners of SOEs. A government takes on the responsibility for supervising how SOEs are operating and will distinguish board accountability from SOE accountability. The key objective of SOE accountability in this context is to achieve efficiency, value for money and avoiding conflicts of interest.

A fundamental issue to address in an overhaul of accountability measures for boards of SOEs is how accountability standards will be implemented by SOEs, and this thesis offers key methods for reforming existing governance standards. This will stem from good management and deployment of resources. A robust accountability framework will require two controls; which is essentially two checks to ensure implementation of governance standards. This could be delivered through an overseeing body acting on behalf on the government which scrutinises the board's application of standards and also by the board providing the relevant Minister with a questionnaire confirming the application of governance principles.

The *Code of Practice for State Bodies* was updated for the fourth time and a revised Code was introduced in September 2016. The Code is influenced by the *Companies Act* 2014 and the *UK Corporate Governance Code* 2016. With a revision of governance standards, the updated Code finally gives recognition to the accountability regime that is required from a governance framework for SOEs. As highlighted all throughout this thesis, a strong emphasis on board accountability will be the deciding factor for a successful governance framework. The relevant provisions will be discussed below but it remains to be determined how the newly introduced provisions will be adopted by SOEs.

B. INCREASING BOARD ACCOUNTABILITY WITHIN SOES

(1) Code of Practice for State Bodies 2016

It is evident from the *Code of Practice for State Bodies* introduced in September 2016 that the approach taken on board accountability has been completely reformed, adding to governance requirements and strengthening the accountability framework. Reviewing the *Code of Practice for State bodies* 2016 firstly to note the government department issuing the standards has moved from the Department of Finance to the Department of Public Expenditure and Reform. The change in governmental department is relevant as new provisions now require the Department of Public Expenditure and Reform to carry out critical reviews for the ongoing business relevant for SOEs, with a requirement for the results of the review to be published.[964] This is a clear indication that the government is moving SOEs in line with organisations that should be effective and efficient as they now have to defend their standing.

The standards have now been separated, identifying core principles and then it provides further provisions based on the core principle. This is a useful methodology as it highlights central principles that should make it more difficult for SOEs not to endorse. For example, one of the core principles holds the board collectively responsible for the sustainability of the SOE; this is then followed with provisions on how the board can achieve this.[965]

Focusing on the regulatory model of governance, the updated Code retains its quasi legal standing and was not implemented on a legislative basis. However, as illustrated in chapter three of this thesis, a quasi-legal framework can have a strong impact where appropriate controls are in place. The updated Code seeks to close this gap between hard and soft regulation by inserting a new take on the principle of comply or explain to the standards.[966] While this principle has been widely criticised and found to undermine credibility where

[964] The Department of Public Expenditure and Reform *Code of Practice for the Governance of State Bodies* (Dublin 2016) principle 8.14 p. 43.
[965] Ibid principle 3 p. 20.
[966] Ibid p. 8.

explanations for non-compliance are not satisfactory, the updated Code has a new take on the principle. The *Code of Practice* 2016 is the first time the principle of comply or explain has been expressly mentioned in governance standards. Previous versions of the Code did not make express reference to this principle, instead SOEs did not have to implement governance provisions that would have a disproportionate effect on them. The *Code of Practice* 2016 retains the provision to allow SOEs the choice not to implement governance principles that will have a disproportionate effect. However, the 2016 Code goes further by requiring significant derogations to be agreed in writing with the government department.[967] Including this requirement places more emphasis on the principle than how it has been traditionally implemented. There is now an onus to let the Minster know in advance about principles that will not be implemented and seek permission for this. This is a welcomed approach as this provides the Minister with the opportunity to be aware in advance of governance principles that are not going to be implemented. This is in line with recommendations made in chapter two of this thesis, calling for this principle to operate on a comply and co-operate basis to improve better engagement with governance standards. By working together and giving better disclosures of their governance regime, this moves to narrow the accountability deficit. While the comply and co-operate principle may have the potential to undermine a boards autonomy, provided boards act within the parameters of governance standards, they will have freedom and scope to act as they consider necessary. The principle is reinforcing a system of being accountable for their actions.

A distinction has been made between commercial and non-commercial SOEs, in the principle of comply or explain. While non-commercial SOEs are only required to let the Minister know if governance provisions are not being implemented, commercial SOEs are required to take all reasonable steps to ensure governance provisions have been followed or the Minister has been notified on their governance arrangements.

It is disappointing that the *Code of Practice* 2016 did not go further and review if the board complied with this requirement on an annual basis or if there were standards not

[967] Ibid p. 7.

implemented by the board but not informed to the Minister. It is a lack of follow through within the Code that could undermine its potential. The language of the Code has been drafted in a tone that does not demand a higher level of adherence as the same undemanding language has been retained. There is only a requirement that the board *should* act prudently, ethically and transparently.[968]

However, board accountability provisions have been strengthened and while previous versions of the Code bundled provisions on accountability, within audit requirements these principles have been separated in the Code.[969] Having separate principles on accountability should move to increase answerability within SOEs, however, code provisions are heavily influenced by audit requirements. The Code interlinks provisions with audit and accountability, largely due to ensure SOEs are achieving value for money but accountability encompasses more than this. SOEs may not be taking advantage of their position with spending money but this does not ensure SOEs are operating in the best possible way. Accountability provisions should ensure fairness, transparency and efficiency on both financial and non-financial transactions. This would provide a set of priorities for the board but allow for reasonableness within the context of individual SOEs.

In recognition of the weak board accountability regime in previous Code versions, the updated Code has completely reformed accountability structures and the new measures have strengthened governance provisions particularly through the Performance Delivery Arrangements (PDA) requirements. As outlined in chapter four, New Zealand and Australia implements a Statement of Corporate Intent and this is something that has been introduced in the revised Code. The Performance Delivery Arrangements (PDA) requires the Minister and SOE to devise a three year plan which they agree on goals and objectives to ensure there is efficiency and effective management of SOEs.[970] Monitoring of the PDA also specified in the Code and a minimum of one meeting per annum, is required with the Department to review the review the PDA.[971]

[968] Ibid p. 5.
[969] Ibid p. 33.
[970] Ibid p. 67.
[971] Ibid p. 42.

The Code now requires board members to attend 100% of board meetings and their attendance at board meetings should be taken into account for re-election of board members.[972]

The Code makes a board accountable for the effectiveness and sustainability of an SOE.[973] This is a substantial increase in a board's responsibilities compared to responsibilities with the 2009 Code. However, the 2016 Code could have taken this a step further. Chapter three outlines how SOEs in New Zealand are required to operate as a successful business as their principle objective.[974] This obligation moves the responsibility firmly on SOEs to operate the best they can so they prosper. Associating performance of SOEs with its turnover will provide a basis for measuring how efficient SOEs operate. There is a large gap between a requirement to be successful and operate effectively, but fundamentally it is a measure of increasing accountability.

(2) Could the Code of Practice 2016 gone further to strengthen accountability provisions?

This thesis has found it's the board's approach to governance that needed to be altered. Robust accountability provisions are required and this was recognised in the updated *Code of Practice* 2016. However, the updated Code has failed to address the dual principal agency issue that arises in SOEs. As outlined in previous chapters, SOEs are owned by citizens of the country who act as principals and task politicians on behalf of the State to achieve the social and economic objectives of SOEs. Politicians act as principal task managers of SOEs, and managers act as agents for politicians.[975] Therefore, Agency theory in SOEs needs to extend to range of principal agent sets of relationships that exist.

The Code omitted provisions dealing with Ministerial accountability. The updated Code failed to appreciate the importance of such a requirement to provide a complete framework for accountability. It is necessary to establish an ownership policy that outlines the

[972] Ibid principle 3.9 p. 23.
[973] Ibid principle 1 p. 13.
[974] *State-owned Enterprise Act* 1986 New Zealand section 4.
[975]Cuervo-cazurra, A., Inkpen, A., Musacchio, A. & Ramaswamy, K. "Governments as Owners: State-owned Multinational Companies (2014) *45*(8) *Journal of International Business Studies* 919 p. 931.

Ministers role in the corporate governance framework and sets out how the Minister is to implement their duties and responsibilities.

The influence of providing complete procedural aspects to accountability have been omitted but are critical for implementing governance standards, and this thesis recommends three strands for a successful accountability regime. Firstly, there should be a planning section with a governance committee, so a board has a consultation process to allow an opportunity to establish its governance regime, which will also set out the board's duties and responsibilities. Secondly, there is an implementation section so a board applies governance standards so they will act in the best interest of the SOE, and thirdly, there should be an effective review of the board's performance so a complete accountability regime is in place. This framework is outlined in the following section.

C. A FRAMEWORK FOR ADDRESSING THE ACCOUNTABILITY DEFICIT IN SOES

(1) PLANNING SECTION - Establish a Governance Committee

The planning process of the governance process should not be overlooked and an effective way of ensuring better governance is through the establishment of a governance committee. The OECD recommends developing an ownership policy for the board, where a clear mandate is given to the board.[976] If board members are going to take ownership on an individual basis for implementing governance standards, a forum to allow the board to become involved in a consultation process on their governance provisions should be established. The board should set out how they intend to establish their governance objectives for the year and this should be followed by a consultation with the Minster. This will also allow the expectation from the Minister to be made known to the board.

[976] OECD *Accountability and Transparency: A Guide for State Ownership* (France 2010) p. 13.

(i) Statement of Corporate Intent

Looking at examples of corporate governance codes from different jurisdictions, there are different characteristics on accountability and enforcement. For example in New Zealand the Statement of Corporate Intent (SCI) is key. Board members of SOEs in New Zealand issued a Statement of Intent to the government setting out how they will address governance issues.[977] The SCI has to be provided to the shareholding Minister annually and the focus is on allocation of funds.[978] In addition to this, a board must supply reports to the Minister with financial statements on a half yearly and yearly basis. These reports must contain:

"information as is necessary to enable an informed assessment of the operations of the State enterprise and its subsidiaries, including a comparison of the performance of the State enterprise and subsidiaries with the relevant statement of corporate intent."[979]

The information that is required highlights the link a SCI will have throughout the year and SOEs are required to explain why they departed from it during the year. It becomes apparent, in terms of accountability in New Zealand, there is a definite requirement for SOEs to continually report to the Minister; they must set out how they expect the SOE to operate during the year through the SCI and how this is carried through must be explained during half yearly and yearly reports. The persistent reporting back to the Minister clearly shows boards are accountable to the Minister and with such a strong focus on conformity and transparency and thereby limit the risk of governance failures. The board is both individually and collectively responsible to the Minister and failure to exercise its duties can result in members being removed from the board.[980] In New Zealand board members are required to provide an annual Statement of Corporate Intent (SCI) containing key objectives and financial forecasting for the SOE.

[977] *State-owned Enterprises Act* 1986 New Zealand section 5.
[978] Ibid part 4.
[979] Ibid part 4, principle 15.
[980] *The Crown Entities Act* 2004 New Zealand section 59, principle 58.

While the *Code of Practice* 2016 introduces a similar concept of Performance Delivery Agreements (PDA), a reference to budget spending did not receive the equivalent treatment. The allocation of funding is something to be agreed in advance with the government and for this reason should be provided annually. This should help reduce soft budget constraints and curtail unapproved expenditure, as the government will be better informed. SOEs would benefit from the Department of Public Expenditure and Reform being involved in the supervision of spending. Griffith highlights the need for increased government involvement, in that it may be necessary for the government to dictate how entities should comply with standards by imposing specific requirements and structures.[981] This is considered the difference between the government setting regulations for entities to follow and being part of a compliance regime.

(ii) Working on better engagement with governance principles

A consultation process should contribute to a departure from the 'boilerplate' approach to governance as boards will be given the opportunity to participate in setting the objectives of a governance framework before embarking on its implementation, thereby legitimising the approach to governance. Ultimately, it is important there is a review process of a governance framework for SOEs. If standards are not working as expected, the approach needs to be reconsidered in recognition that a "one size fits all" approach may not work for all SOEs. This should help deal with special circumstances where further Ministerial assistance is required. This would also allow the board an opportunity to voice concerns over what is accepted to be reasonable and allow the board to discuss implementation of principles. This would allow the board to ensure they are operating within their terms of reference as well as taking into account stakeholders. This should also assist the board on being clear on what reports they have to provide or produce and how they deal historic issues of governance if standards have not been implemented in the past and how they intend to address this going forward.

[981] Griffith, S. "Corporate Governance in an Era of Compliance" (2016) 57(6) *William & Mary Law Review* 2075 p. 2078.

Recommendations

- It is recommended to establish a governance committee, and draft a strategic plan for implementing governance standards, this should also provide the government with the intended allocation of budget for the year which should be approved by the Department of Public Expenditure and Reform. The board is required to ensure there is effective internal control within SOEs, the board should disclose deviations from the strategic plan.
- To ensure the alignment of interests and bring clarity it is recommended that the board and Minister are required to consult with each other and provide an induction when new board members are elected. A consultation should occur at the start of the financial year with a meeting with the government department and the option should be available for either the board or the Minister to call more meetings throughout the year as deemed necessary. This should help bring to light specific governance problems and an opportunity for solutions to be found.
- It is recommended that potential areas of weaknesses should be proactively identified at the consultation stage and if the board is not going to apply particular governance provisions this should be made known to the Minister along with a detailed explanation. This should help result in better transparency by having stronger disclosure regime which is on a similar basis to mandatory disclosures.
- Principles that are implemented by the board should also be disclosed to the Minister. This will ensure that where the board makes the assumption they are implanting governance provisions the Minister knows this and can ensure they are doing so correctly.

(2) IMPLEMENTATION - Application of Governance Standards

Having robust provisions on how governance standards can be implemented and applied is interconnected to a successful model of governance. If guidelines lack specific mandates on how governance should be implemented it becomes increasing difficult to expect a board to adhere to governance standards. Essentially, accountability will be improved if a board is aware of what its role is and the board co-operate with the government in achieving their obligations. Transparency is important and so information should be communicated to stakeholders as ultimate owners of SOEs.

(i) Alignment of the boards' duties and responsibilities

An issue to address is who is responsible for ensuring compliance with governance standards and setting the level of compliance along with what constitutes non-compliance and details that needs to be reported. The application of governance standards requires each member of the board to take ownership for achieving a high level of governance standards. The attitude of the board should reflect this and if the board adopted an approach that each member acts as owner of the SOE, this may deal with the agency issue of individual board members.

(ii) Comply and Co-operate

Governance standards on a soft law basis is a feature for making governance principles more easily accessible and implementing as the mandatory obligation that is required for compliance is alleviated. Introducing governance standards that are rules based, rather than principle based, may reinforce an obligation to comply with standards. By their characterisation rules leave less room for interpretation than a principle based approach, so the expectation is SOEs will follow the rules with little departure. The corollary of this is that a rules based approach hampers the ability of SOEs to infer the 'spirit' of governance provisions so if rules do not fit for SOEs, they will not implement the principles.

The benefits of drafting governance on a legislative basis can be availed of where there is a significant accountability mechanism in place. It is clear that perhaps one of the most influencing factors of implementing governance on a legislative basis would be to have the force of the law to ensure the board implements governance standards. To a large extent this can be availed of if there are adequate accountability mechanisms in place. This will require a strategic plan to be implemented. This should include a principle based on comply and co-operate so that the Minister reviews the performance of SOEs and resolutions are adopted where the board have not implemented governance standards correctly. The board should provide accounts to external auditors so that financial statements are prepared based on true and accurate information.

The functions of a soft law model are better suited and recommended for SOEs as it allows for more flexibility to allow SOEs implement governance standards in the best way for the SOE and it is less burdensome both on SOE and government but provisions should be included where governance standards have not been followed. Effectively, what is required is an overview of the approach taken by the board on implementing governance standards. If governance provisions do not apply for legitimate reasons, this is acceptable, provided this is communicated in advance to the Minister. Ultimately, it is the flexibility that is offered from soft law provisions that make it attractive but this should not be at the expense of accountability where the board co-operate with the Minister.

(iii) Transparent decision making

A governance model that contains disclosure provisions should increase transparency as the board will be required to draw the Minister's attention to particular events. A board has a duty to provide this information to the Minister and so open communication channels should be in place for these reporting requirements. It is expected that increasing transparency will at least allow the information to be available to interested stakeholders. However, as stakeholders do not have a duty to engage with a governance framework, they rarely will do so without a vested interest. An examination of annual reports of SOEs reflects that governance issues are not addressed in great details and there is little engagement with standards, leaving stakeholders little motivation to play any role of governance.

Contradictory interests can arise in SOEs and this raises the issue of whether a governance model should be shareholder or stakeholder focused. This problem was noted by Sokol as he outlines the interests of managers and directors may not align with those of citizens as ultimate shareholder of SOEs.[982] As citizens do not have ownership rights, Sokol suggests the principal agent relationship is between the government and the taxpayer, rather than the government and the SOE, as citizens ultimately own entity.[983] So while SOEs are for the

[982] Sokol, D. "Competition Policy and Comparative Corporate Governance of State-Owned Enterprises" (2009) 6 *Brigham Young University Law Review* 1713 p. 1729.
[983] Ibid.

benefit of citizens they may not maximise stakeholder's value, as chapter one outlined that SOEs are established for a number of reasons. This may lead to stakeholders being more passive about stakeholder activism in SOEs.

Transparency is necessary to ensure credibility is not undermined. Transparency measures should be in place, one way of achieving this is information should be communicated to shareholders and conflicts of interest are disclosed. If SOEs are ultimately owned by citizens in the State, there must be confidence in SOEs that government funding is put to the intended use. On this basis, it is time for SOEs to disclose how they are spending its budget in annual returns. There should also be clear methods for electing new board members and remuneration should be set in accordance with government policy to fairly reflect their contribution to the SOE.

Increasing transparency will be useful as a means of measuring the success of SOEs, year on year. This is also true for comparatively measuring salaries of all board members across other SOEs and so this information should be published in SOEs annual report. To ensure transparency, individual board members should be individually named. By releasing this information, salaries can be compared across all SOEs which will highlight disparities between salaries across all SOEs. Salaries may not be the only compensation directors will receive and so where directors receive additional emoluments, benefits and gifts details of such should be disclosed on a mandatory basis. It is envisaged that both Ministers and directors want to maintain a sense of integrity so that the best interests of SOEs are protected, so a board should be clear on what they are entitled to accept and what has to be reported.

(iv) Conflicts of interest

Due to a lack of stakeholder engagement, this pushes the responsibility back on the government as shareholders with the duty of properly managing and monitoring SOEs on behalf of citizens. Pargendler recognises the adverse effects of the governmental influence as a controlling shareholder in SOEs as being both the player and referee due to the

proximity of policy making and the influence policy to its advantage.[984] The government may not always pursue the interests of citizens and an SOE can dominate a niche sector preventing private sector companies entering the market, and offering an alternative for citizens.[985]

Conflict of interest that may arise in the Minister's role of ensuring SOEs comply with standards should be safeguarded against without limiting the Minister's functions. Having contractual agreements between government and SOEs that balance independence but do not undermine the monitoring aspect, are required. This is linking the Statement of Corporate Intent that a board follows through on the intended governance arrangements. Also, indicators should be in place for Ministers when governance is not being followed and this will assist in execution of monitoring aspects but limit excessive government interference.

On this basis a governance model that will ensure the rights and interests of stakeholders as ultimate owners of SOEs are protected is necessary. Ultimately these decisions should be made with the focus on the principal recipients as ultimate users of SOEs.

(v) Accountability and the Ministers role

The Minister has an active role in an accountability framework for SOEs. However, increasing Ministers' role in SOEs gives rise to the third agent dilemma and there is a conflict of interest. The third agency is based on citizens acting as principal, and the government acting as principal to the board. The role that the State has in this through the government adds to the complexity of achieving and sustaining accountability and transparency. This is recognised by the OECD, who provided a recommendation to aid SOEs entitled *Accountability and Transparency: A Guide for State Ownership*.[986] The OECD recognises the importance of a high level of accountability and transparency which will promote growth, investment and competitiveness. The government is responsible for

[984] Pargendler, M. "State Ownership and Corporate Governance" (2012) 80(6) *Fordham Law Review* 2917 p. 2921.
[985] Ibid.
[986] Supra note 976.

monitoring SOEs but it is a balancing act of allowing SOEs to exercise their duties without political interference and simultaneously being accountable to the government. There will be conflicting goals for this, with the State being the source of financing but also monitoring SOEs.

New Zealand operates its governance on the basis that two Ministers are responsible for each SOE. Including two government departments can offer a useful perspective from the respective government departments. A dual ministry should dilute the problem of the government having a role in owning and managing SOEs as power is diluted but competency is increased as SOEs will benefit from the expertise from two government departments. It is vital that the regulatory aspect is separated from the governments' management duties. While there are benefits to a dual ministry function, this may lead to duplication of resources and may not be cost efficient. Therefore, the dual ministry model may be a more realistic model for larger SOEs and particularly commercial SOEs. Functions of the role of each ministerial department should be clearly defined but it is expected that the Department of Public Expenditure and Reform should be one department involved and responsible for financial issues. The dual Ministry model exists to an extent in Ireland as two Ministers are responsible for each SOE; the relevant department and the Department for Public Expenditure and Reform. Previously, the Department of Finance was part of this dual model but this changed to Department for Public Expenditure and Reform in the *Code of Practice* 2016.

An alternative to a dual Ministry model is for the supervisory function to be carried out by a specialised body appointed by the Department to dilute government involvement in SOEs. For example, NewERA may be better qualified to appraise SOEs performance.[987] NewERA provides financial and commercial advisory services to the relevant Government Ministers for the following State Bodies; Bord na Móna, Coillte Teoranta, EirGrid, Ervia, ESB and Irish Water but can also be requested to advise the Minister on other State Bodies.

[987] Established under the *National Treasury Management Agency (Amendment) Act* 2014.

Recommendations

It is recommended to strengthen implementation of governance standards a board must be answerable for the decisions it makes on both on an individual and collective basis. A board must understand and justify its decision in an annual review with the government department and show how they were made in the best interest of the SOE. Instead of using the principle of comply or explain a board should operate on a comply and co-operate basis with the code, this should reinforce a board's commitment to letting the Minister know when governance provisions are not implemented. It is suggested that the board should inform the Minister in advance of not implementing governance standards. A departure from a governance provision should only be acceptable where the following three conditions are met:

1. An extensive explanation when not complying with governance provision is provided.
2. The Minster is made aware in advance of governance provisions that have not been implemented.
3. The provisions not complied with are disclosed in annual reports, along with the explanation for not complying.

(3) REVIEW PROCESS – Monitoring and Enforcement

A fundamental part of this research is determining what mechanisms can be relied upon to ensure an accountability regime in governance standards. Accountability will be improved where the board is appraised on its performance and called to defend its actions. This should be the fundamental basis for a regulatory model and in order for this to be achieved, the board should be subjected to annual review of its performance.

(i) Performance Appraisals

Performance appraisal should take two forms. Firstly, the Minister should review the performance of SOEs and if they have operated effectively and achieved value for money. Secondly, there should be a review of governance standards to determine how well the board how engaged with governance standards.

(ii) Repercussions for not implementing standards

Associated with this is the question of whether there should be repercussions or penalties for a board for non-compliance with standards. Pressure from the relevant Minster, Department of Public Expenditure and Reform and other relevant Departments should ensure a board is performing and there should be ramifications where a board is not meeting its objectives. It is essential that the governmental departments ensures governance provisions are met and the Minster should be made aware if this is not happening. This would allow for a review process to afford the board an adequate opportunity to adjust their actions where they have failed in their duties.

If board members are individually named for the performance and if the board members have been given specific roles for example in finance, overseeing shareholders' interests, this should assist with their appraisal. This raises the issue of whether directors should be held personally liable for their failings in governance as this would act as a persuasive incentive to ensure good application of governance standards. Ahern recognises the requirement for the application of duties, enforcement and remedy for breaches to be all considered together to strengthen directors' duties.[988] Ahern notes there is an assumption of a legal remedy for breaches of duties which assists with enforcement of directors' duties but a remedy is not always available.[989] This is a problem that is relevant for SOEs as penalising breaches in duties is difficult as governance standards are not implemented on a legislative basis. However, a solution for this problem can be found in the *Companies Act* 2014 as it gives statutory recognition for directors' duties and this should be contained with a code of practice for it to have equal application for SOEs.[990] This approach was adopted in the Code in 2016 as the statutory recognition of duties is now part of the Code.[991] This now gives statutory in recognition of the fiduciary duties owed by the board of SOEs requiring directors to act in good faith, not profit, act with due care and skill. This duty should be exercised with key stakeholders in mind, as ultimate owners of SOEs.

[988] Ahern, D. "Directors' Duties: Broadening the Focus beyond Content to Examine the Accountability Spectrum" (2011) 33 *Dublin University Law Journal* 116 p. 118.
[989] Ibid p. 119.
[990] *The Companies Act* 2014 section 228.
[991] Supra note 964 principle 3 p. 20.

(iii) Complete a self-evaluation questionnaire

A board evaluating its own performance should also be a fundamental part of a governance framework as it should identify competencies of the board and provides an opportunity to reaffirm their responsibilities. What happens with the outcome of the evaluation is important as this can be used as an opportunity for continued improvement and development.

The Code of Practice 2016 requires a board to complete a self–evaluation questionnaire to review their performance. The questionnaire is extensive in its application, however, there is no specific requirement to inform the Minister of the results of the questionnaire which is a recommendation of this thesis. As outlined in chapter five, the internal audit of FÁS revealed spending was not in line with government policy and the decision was taken by the Director General to conduct his own review rather than report this to the government. There is a danger of this happening with a self-evaluation questionnaire, as unless there is a specific requirement for the board to do something with the information, finding it out becomes a missed opportunity. Sokol points out that mandatory reporting should reduce monitoring requirements,[992] and so this would lead to better management of government resources as the information is more freely given to them. The 2016 Code places a requirement to inform the Minister of matters arising within an SOE,[993] but this not far reaching as this does not require the details of the questionnaire to be disclosed. The obligation to inform the Minister of matters arising with an SOE draws similarities to the 'no surprise policy' in New Zealand discussed in chapter two.[994] This indicates that it is only material changes that are required to be disclosed to the government department.

[992] Supra note 982 p. 1743.
[993] Supra note 964 p. 58.
[994] Crown Company Monitoring Advisory Unit *Owners Expectations Manual for State-Owned Enterprises* (New Zealand 2012) p. 67.

Recommendations

- There should be better streamlining of board accountability. As a board is responsible for the application of governance standards it will be appraised on its performance and accountable for decision it makes. This will make the decision making process more transparent. This review should be carried out by an overseeing body on behalf the Minister on an annual basis.
- As the interests of stakeholders have to be protected and both the Minister and board have an obligation to ensure this objective is fulfilled, enhanced information should be provided by SOEs in their annual reports on the implementation of governance provisions.
- Performance appraisal should be carried out which should involve a report being sent to the department on how governance has been implemented in an SOE. This will add to the monitoring activities as it demands a board to keep adequate records. During this process it should be agreed what actions are required when areas of weaknesses are uncovered.

This research has discovered a fundamental issue with governance for SOEs is that soft law does not require all governance provisions to be implemented by a board. Therefore, to ensure a board's commitment to good governance, it is recommended that as part of the review process a report be provided to the Minister. This offers the opportunity for the board to review its performance and also for this information to be available for the Minster. This provides a channel for a board to disclose to the Minister, so there is an awareness of governance procedures that are implemented along with principles that are not executed.

Strong provisions on accountability and transparency will not eliminate all controversies within a corporate governance framework but where governance standards are implemented on a soft law basis, they will play a key role in a successful model of governance. These principles will contain the ground rules and will be useful as a gauge for evaluating the performance of the board. Governance is also about setting controls and has been described as being a facilitator of the allocation of resources.[995] An important

[995] Vermeulen, E. "The Role of the Law in Developing Efficient Corporate Governance Frameworks" in OECD *Corporate Governance of Non-Listed Companies* (2006) 91 p. 96.

aspect of governance is that SOEs should operate as efficiently as possible, achieving value for money and SOEs who operate efficiently should be rewarded for this. Commercial SOEs in New Zealand are required to be successful companies and to pay a dividend back to the State.[996] On this basis, there is link between successful engagement with governance standards and financial performance. There should be a conscious effort for SOEs to operate efficiently, this is in terms of budget spending of SOEs and what they can contribute to the State. This should be included as part of the review process as it is not acceptable that SOEs should have free reign of funds without being called into account for their expenditure.

As highlighted in earlier chapters, in recognition of the difficulties boards face with executing a governance code there should be a three step plan for dealing with accountability within SOEs. Firstly, the board should set out responsibilities and objectives for the coming year, in a similar way to the Statement of Corporate Intent in New Zealand and Australia. A clear framework should be in place for the board setting out their duties and responsibilities. The board should take individual ownership of its duties and provide a statement on how they have implemented its duties. This should help address the agency issue of individual board member, where they do not act in the best interests of the SOE.

A statement should be backed up by the board firstly reviewing its own performance, followed by reporting mechanisms to the relevant Minister with this which will allow Ministers to scrutinise the decisions of the board and challenge difficult issues. The final step of the process is for the board to receive feedback from the Minister and establish how they intend to move forward in the future. Implementing what is essentially a business plan will give clear focus to SOEs and this will establish the main objectives and priorities to determine standard operating procedures as to how standards can be executed. This will become their mission statement so that a board should be clear on its functions and what is expected from the board. The standards should be based on SOEs operating as efficiently as possible.

[996] Supra note 977 part 4, principle 15.

To achieve these targets, performance measures should be set for the board. This should contain both financial and non-financial targets to give a clear focus and direction for the board. This should be specific and give a timeframe for the board. Financial targets will be linked back to their budget and SOEs should aim not to overspend and achieve value for money. Non-financial targets will include SOEs overall performance. This will be linked to increasing transparency, as the expectation is more information will become available within the public domain. If citizens are effectively owners of SOEs, they should be able to access information regarding SOEs. This can be achieved in a number of different ways - through annual reports, ensuring their websites contain adequate detail and allow interaction from citizens. Transparency will also require financial transparency and so this will be predominately achieved through annual audits. The reporting aspect of a board back to the Minster is clearly a very important aspect of a governance framework, this will allow the government be an informed owner. Under the *Code of Practice* 2009, the board had only to confirm annually that governance practices were being followed by the board. However, firmer application of governance process should be introduced, directors concealing information may become an issue and something that governance principles should address by containing a duty to disclose provision.

D. SUGGESTED QUESTIONNAIRE FOR SOES

As discussed in chapter five, the corporate governance model did not work to prevent the FÁS scandal. It was clear that the Department of Finance had no idea of what level of governance was implemented by the board in FÁS. To assist the board with the implementation of governance provisions and to provide the relevant government Departments with a better insight to this, a questionnaire is drafted below. The questionnaire is based on the provisions with the *Code of Practice* 2016 and to strengthen accountability, additional standards have been included.

A recommendation of this thesis is for the board to self-evaluate their corporate governance and this should be provided to the Department. Providing an assessment tool should highlight how governance is being implemented. It is recommended this should be annexed to *the Code of Practice* so while it will also be on quasi-legal basis, it will

strengthen existing governance standards by requiring a board to review how it has applied governance standards. This would improve transparency as a board will be clear on how it implemented provisions, thereby improving monitoring and accountability.

Providing a questionnaire would give the Department a snapshot of how SOEs have fared in their governance regime for the preceding year. Therefore, it is used as a guide to aid the board, by acting as a self-assessment tool, it will allow the board to tailor and focus its governance. However, a brief statement will not suffice in the narrative but a more detailed explanation will satisfy the Department that the correct governance procedures are being followed. The questionnaire should be provided to the Department annually when supplying the annual accounts.

What will be contained in the questionnaire will be imperative. Identifying central areas of focus will be key to its success and dividing the areas into different phases will make it more manageable for the board. The principle of comply or explain should not be disregarded as the questionnaire cannot undermine the standing of *the Code of Practice*. However, the basis of the principle can be revised, the principle of comply or explain operated on the default that governance provisions were implemented and it was only principles that were not followed needed to be explained. However, an inverse of the principle may also prove useful; for the board to explain when they have implemented governance standards. Following governance standards is largely not a black and white procedure, there are areas that may require further clarification from the board on certain provisions. For example, if the board follow governance provisions and explain how they have engaged with such principles this may give a clear outline for Ministers on how governance issues are being applied in practice. This should remove disconnect between theory and application. It will also act as a means of bridging the gap of governance set at a low threshold on a soft law basis as this will highlight to the Minister areas of concern that may otherwise go undetected as the board would not have to bring to their attention. A discursive narrative should be provided as to why provisions are not considered relevant and not implemented. Also, the board should disclose if it consider if particular provisions will become relevant at a point in the future. This shifts responsibility back to the Minister

to decide if the board are correct in their assumptions where they have not followed governance principles.

Many provisions of *the Code of Practice* provide clear guidelines such as the structure of the board and specific procedures to be followed. However, as outlined in earlier chapters, a board must follow the spirit of the Code. This should provide the Minister with a better understanding and a sense of how governance has been executed by SOEs. The questionnaire should be signed off by the board. But in order for this to be successful, there will be an accountable person who ultimately will have responsibility for governance issues, this ideally will be the chief executive of the SOE.

By implementing a questionnaire there will be a better analysis by a board of the governance procedures and this information will be available for the government to review. This model will amplify the positive effects of existing governance framework. So while much of the focus has been on how the governance principles can be approved, the boards approach to governance will also be instrumental in improving corporate governance for SOEs.

The potential benefit for a questionnaire is evident. It provides the Minister with a scoring mechanism so they are aware of SOEs who are more vulnerable to weaker implementation of governance procedures. This will allow the government to work with these entities to build up compliance with governance procedures. Mitigating factors for lower levels of compliance will also be considered but it will move the assumption of assuming governance has been complied with. Codes could be weighted in reference to their importance and this would provide a weighted average of how governance is implemented. An example of the questionnaire is provided in below which addresses mechanisms of improving accountability in SOEs.

PART A **LEADERSHIP**		**FULLY COMPLIANT (FC)** **PARTIALLY COMPLIANT (PC)** **NON COMPLIANT (NC)** **(Please identify the level of compliance for each governance provision and provide further comment where full compliance not achieved in each section below.)**
1	**Principle: The board is collectively and individually responsible for promoting the success of the SOE, this is requirement of the Code.**	
(i)	Is there a clearly defined framework in place to allow a board to provide leadership and direction to SOEs?	
(ii)	Has the relevant Minister been notified if there are any restrictions or barriers to achieving this?	
(iii)	Is the board are aware of all its duties and responsibilities and have capacity to exercise them?	
(iv)	Have new board members received induction training and been provided with all required information to complete their duties?	

2.	**Principle: The Code provides for output statements based on the performance framework to be provided.**	
(i)	Has the performance and effectiveness of the SOE been reviewed?	
(ii)	Have there been areas where this has been prevented or areas that required the board to intervene?	
(iii)	Has the board provided signed confirmation that the code of conduct has been followed?	

PART B **COMPOSITION OF THE BOARD**	**FULLY COMPLIANT (FC)** **PARTIALLY COMPLIANT (PC)** **NON COMPLIANT (NC)** **(Please identify the level of compliance for each governance provision and provide further comment where full compliance not achieved in each section below.)**
3.	**Principle: Board appointment procedures are to be followed in line with the Code and conflicts of interest disclosed.**
(i)	Have board appointment procedures been followed?

(ii)	Do new board members have sufficient competency to fulfil their role?	
(iii)	Have new directors been fully briefed and provided training regarding their responsibilities and been provided with a copy of conduct and a code of ethics?	
(iv)	Has an explanation been provided as to why board members have been selected, which outlines their qualifications and experience?	
(v)	If the board considers that a particular skillset is missing, which could add value to the board, has this been brought to the Minister's attention?	
(vi)	Have new board members disclosed any potential conflicts of interests, including connected parties it has to the SOE?	
(vii)	Has the role of CEO and chairperson been separated and carried out by two different individuals?	
(viii)	If the above roles have not been separated has prior Ministerial approval been sought?	
4.	**Principle: The independence of non-executive Directors is paramount as they advise on issues relating to strategy, key appointments and standards of conduct.**	
(i)	Has the independence of newly appointed NEDs been confirmed and verified?	
(ii)	Is there a minimum of two NEDs on the board of directors and the audit committee is comprised only of NEDs?	

PART C **DUTIES OF THE BOARD**		**FULLY COMPLIANT (FC)** **PARTIALLY COMPLIANT (PC)** **NON COMPLIANT (NC)** **(Please identify the level of compliance for each governance provision and provide further comment where full compliance not achieved in each section below.)**
5.	**Principle: The board is required to confirm compliance with the Code as it provides duties and responsibilities of the board.**	
(i)	How many board meetings took place in the past year?	
(ii)	Please advise which members did not have 100% at board meetings and was a reason for not attending the meeting provided in advance?	
(iii)	Did the Audit Committee meet a minimum of four times as required the Code?	
(iv)	Has the board complied with its duties and responsibilities in the Code? If provisions have not been complied with, has a reason been provided? Has the board indicated when they anticipate provisions that were not implemented in the prior year?	

(v)	Have protocols on budget spending, travel and procurement principles been implemented in line with the Code and relevant government policy?	
(vi)	Has government policy been followed regarding setting remuneration? Has this been authorised by the relevant Minister? Have fees paid to board members been made available? Is the remuneration linked to performance?	
(vii)	Is the board satisfied with the performance of the CEO?	
(viii)	Is the board satisfied with the independence and competency of the auditors?	
(ix)	Has the board established strategic plan for the next 3-5 years ahead, which has approved by the relevant Minister? Has the board reviewed the plan annually to ensure the objectives are met?	

PART D **DISCLOSURE & TRANSPARENCY**		**FULLY COMPLIANT (FC)** **PARTIALLY COMPLIANT (PC)** **NON COMPLIANT (NC)** **(Please identify the level of compliance for each governance provision and provide further comment where full compliance not achieved in each section below.)**
6.	**Principle: This section is an opportunity to ensure that the disclosure and transparency principles are being implemented by the board and that effective communication channels are in place.**	
(i)	Have disclosure mechanisms been identified and notified to relevant persons? Has there been any material change in the SOE? Has the board made disclosures relevant to the Code of Conduct?	
(ii)	Has the board kept the Minister informed of issues relevant to the SOE as required by the Code? Where relevant, has the board made the Minister aware when major governance provisions were not be followed and approval sought?	
(iii)	Has the board provided necessary information to internal and external auditors so the quality of the audits is not compromised per the Code?	

	What mechanisms are in place to inform stakeholders of the performance of SOEs?	
(iv)	To track performance progress, has the board highlighted governance provisions that have not been followed in the current year but have been followed in previous years? If this is the first year that a provision is applied has this been highlighted?	
(v)	Is there a suitable risk management framework to be in place? Have potential areas of weakness been identified?	

PART E **ACCOUNTABILITY**	**FULLY COMPLIANT (FC)** **PARTIALLY COMPLIANT (PC)** **NON COMPLIANT (NC)** **(Please identify the level of compliance for each governance provision and provide further comment where full compliance not achieved in**

		each section below.)
7.	**Principle: This section provides an opportunity to establish if internal controls in place and functioning correctly and that the board is competent and effective in carrying out its duties.**	
(i)	Have conflicts of interest been disclosed and how have they been managed? Are there any further procedures that need to be put in place?	
(ii)	Has the board provided an accountability statement and confirmed that disclosure requirements have been met in the annual report?	
(iii)	Have protocols regarding expenditure, procurement and travel with the correct restrictions been met?	
(iv)	What is the reporting structure for reviewing the performance of the board?	
(v)	Are there any areas of the board's duties that are not being carried out correctly and are stakeholder's interests protected?	
(vi)	Has the board co-operated fully with the internal and external auditors with annual accounts being provided to government? Have recommendations by the board been implemented promptly?	

	Has the board confirmed that all information provided in the questionnaire is true and accurate and reflect how corporate governance standards have been implemented by the board?	Signed by each member of the board _____ _____

E. CONCLUSION

This chapter has provided recommendations to strengthen board accountability provisions within governance standards for SOEs in Ireland. The ultimate goal of a governance framework is to align the objectives of SOEs to allow it to operate as successfully as possible for citizens in the country. This should stem from a solid governance framework but there should also be an inherent ethos within SOEs with a willingness and expectation to operate and be as successful as they can.

While adopting a framework is critical, maintaining a level of efficiency is important and this requires a shift to a more formal review of the performance of SOEs. This thesis has highlighted the emphasis on accountability and enforcement. Without a board being clear on its responsibilities and being accountable to the Minister, this will not be achieved. A board should be given direction and support to assist them in its duties. A consultation process and review is therefore necessary.
This will allow a board to adopt any procedures as required. A consultation process will allow the board a negotiation period to ensure that realistic targets and objectives are set and if governance provisions are in place that are outside the scope of the SOEs remit, they can be disbanded. This should create a balanced approach as a situation should not arise where individuals are put off becoming directors of SOEs. Therefore, a governance regime should not create barriers to entry. This will also require appointing directors who are both qualified and experienced to take on the role of a board member of an SOE.

To assist directors in their duties, it would be useful for directors in SOEs to link in with each other where they encounter difficult situations in their duties. While a soft law framework doesn't carry the same weight as legislation, conclusions from this analysis above show that corporate governance regimes can be strengthened if there are rigid accountability standards. This requires commitment from the board to uphold governance principles. It is clear that a system of disclosure and transparency needs to be in place and so governance on a soft law basis can provide an adequate solution in mitigating adverse effects of the principal-agent dilemma.

It is suggested that governance standards can be effective on a soft law basis, but only where suitable accountability provisions are in place. If governance principles are not introduced on a legislative basis to ensure their success, the government should have an acceptable level of procedures in place if governance standards are not met. This will require an overhaul of the government's view of their approach where standards are not met. Their approach should align more closely to the rule of law, making a board accountable for its failures as for not implementing standards. It is recommended that this would require a board to defend its actions in an annual review from the government department. The accuracy of how well a governance model on a soft law basis will be used by the board can never be guaranteed but the focus should rest on tailoring a governance framework to particular SOEs so that while all governance provisions are applicable, this should clear to the board.

There is a tendency to draw on corporate governance codes for listed companies to set the benchmark for a governance framework for SOEs. However, due to the ownership structure, financing structure and accountability requirements, the governance requirement differ and so frameworks for SOEs cannot mirror frameworks for listed companies. However, governance principles for listed companies will indirectly affect governance for SOEs as they will influence their framework. Drawing on good aspects is necessary to assist with good governance for SOEs. A key feature of UK governance was the premise of standards containing key governance principles with sub-provisions providing further guidance on principles. This is a beneficial model to adopt; having provisions that principles will be based upon and providing further guidance on achieving the principles. This thesis aimed to establish the best structures that should be in place to assist SOEs achieve a higher level of governance. Governance provisions should be based on principles, most notably, on accountability and transparency, responsibility, fairness, stakeholder and give a clear aim and focus for SOEs. Ancillary principles supporting this should be based on flexibility, participation, responsibility and be solution orientated. Indicators based on risk management should also be part of a governance framework. While the basis of corporate governance is transparency and accountability, this is underpinned by disclosure. There must be a continuing onus for directors to disclose information on the performance of SOEs, both through annual reporting and their

accounting mechanisms. This is ultimately a significant difference between corporate governance standards for SOEs and listed companies. The board has a duty and responsibility to ensure SOEs are run in the best manner for the protection of its stakeholders – ultimately citizens of the State. This thesis has argued that it's a combination of both internal and externals mechanisms that's required for a governance framework to improve board accountability in SOEs.

By adding to the existing framework in place a requirement of the board to attach a questionnaire explaining their specific governance arrangements should be provided annually to the Minister. This will also allow time for self-evaluation, on how the entity has been performing and review their governance agenda. A scoring system could be implemented with consequences of falling below certain levels should also be secured, for example being answerable to the Public Accounts Committee (PAC) in the Oireachtas. However, the Public Accountants Committee limitations were evident during the FÁS saga when reports presented had large sections of spending blacked out as FÁS, arguing they were not obligated to disclose certain information.[997]

Chapter five examined the governance failure in FÁS and it was clear the *Code of Practice* 2001 was insufficient in preventing and curtailing the reckless activities of the board and adverse effects of inadequate transparency and disclosure mechanisms became apparent. One of the major issues that ran throughout this thesis is a board not implementing governance provisions. If this was more transparent, this would improve governance as external pressure would play a role and if the Department are aware if the board are not implementing applicable provisions, they can remedy this in time. An examination of annual reports found boards rarely disclosed which governance provisions they were not implementing. This thesis has directed attention to a governance framework and to areas that require reinforced governance principles. Critical to the process are guidelines to strengthen accountability and transparency within SOEs. The future of corporate governance for SOEs in Ireland will be determined by the success and effectiveness of the governance Code 2016 and it remains to be seen if contains adequate safeguards as

[997] Lavery & Neville "Fury grows over 'outrageous' FÁS spending on US junkets" *The Evening Herald* 25 November 2008.

ultimately what a governance framework for SOEs needs to do is enhance the SOEs performance and protect the interests of stakeholders.

The updated *Code of Practice* 2016 coincides with an update from the OECD on governance guidelines for SOEs.[998] The updated Code of Practice reflects the increased interaction that is required from government departments. In a similar way to other countries relying on a statement of corporate intent, SOEs must set Performance Delivery Agreements. These are agreements between the department and SOE on how SOEs should operate. Including this plan as part of governance arrangements would improve the efficiency of SOEs but only where targets are correctly monitored.
Best practice indicates the provisions should be drafted so that each member should show leadership and act in the best interests of the SOE. A questionnaire should be annexed to the report that is presented to the Minister annually. The aim of the questionnaire is to allow a board to self-evaluate its own performance and it gives a clear insight for the Minister on the implementation of governance standards. On this basis, the questionnaire will become an effective means of increasing accountability within SOEs.

The following chapter is the concluding chapter for the thesis which will draw together research from previous chapters to offer recommendations on how accountability should be managed by both a board and the government.

[998] OECD *Guidelines on Corporate Governance of State-Owned Enterprises* (France 2015) available at http://www.oecd.org/daf/ca/OECD-Guidelines-Corporate-Governance-SOEs-2015.pdf.

CHAPTER 7
CONCLUSION

A. INTRODUCTION

Bentham contends 'the more strictly we are watched, the better we behave.'[999] The central research question in this thesis is to determine how board accountability in corporate governance standards for SOEs can be strengthened to narrow the accountability deficit. This thesis sought to address this issue firstly, by addressing the key issues in a governance framework. The aim of identifying these issues was to build a supporting framework to assist in a successful implementation of these principles in practice. Regulatory intervention can be an effective means of increasing accountability in SOEs.

Traditionally corporate governance standards lacked force, the *Code of Practice* 2009 required updating to allow for a more rigorous and standardised approach to implementing and enacting governance standards. The updated *Code of Practice* in 2016 was required and it focuses on responsibility for both the board and the government. Increasing focus on accountability will serve to review the institutional process of monitoring board performance and provide a means to measure their performance. This provides more accurate channels of ascertaining how a board is implementing governance provisions. The *Code of Practice* 2009 was outdated as it required a board to state in their annual reports if it was applying governance principles relevant to the SOE. However, this provides incomplete information as it gives very little detail on how well a board is interacting with governance standards. Therefore, one of the limitations with the 2009 Code was that the government was unaware if the board was implementing governance standards. Finding a solution to this will require a number of different criteria that are both results driven and performance driven. Combining both approaches moves away from an annual 'tick the box' approach taken by SOEs that governance standards are implemented by the board. A higher level of scrutiny is required by the government. By setting obligations and goals, the output performance of the board can be assessed. This was implemented in the *Code of*

[999] Bentham, J. Panopticon (Thomas Byrne Dublin 1791).

Practice 2016 by requiring Minister approval in writing if not implementing governance standards.[1000]

To avoid cross purposes, a board must be clear to whom they are accountable and on what they are accountable for. The board should be aiming to achieve a high level of accountability. This requires the board to have a clear definition of accountability. The hierarchal structure within SOEs creates challenges within an accountability framework as accountability is based on control. A board is required to report to the government and so this provides a vertical control arrangement between the two. However, this structure is weakened by the government being required to act in a supervisory capacity but also to respect SOEs independence and refrain from undue political interference. The boundaries issues that exist between the two create difficulty but primarily, the board must be clear on who they are answerable to, and what the sanctions are for non-compliance or non-performance. For this reason, an overseeing body such as NewERA may be better qualified to appraise the performance of SOEs.

To deal with the agency issue of individual board members accountability, provisions should concentrate on individual board performance as part of a governance framework of accountability for SOEs. Individual performance will focus individual board members responsibility but this will also require expectations to be managed. Drawing from Agency and Stakeholder theory, prioritising self-interest purposes may not just be at an individual basis but the issue may also arise in a group context, where management as a group may act in a manner that is not keeping with the best interests of relevant stakeholders. To counteract this, this thesis has provided a means for improving the quality of disclosure and harmonising the information made available to the Minister. Meeting the public service obligation is paramount to the performance of SOEs and this should be done with the consideration of stakeholder's interests. To facilitate this, the maintenance of good relationships can be achieved from attaining a good level of accountability for SOEs.

[1000] The Department of Public Expenditure and Reform *Code of Practice for the Governance of State Bodies* (Dublin 2016) principle 7.

B. SUMMARY OF FINDINGS

The purpose of accountability is "to give an account of themselves."[1001] This thesis has examined how a board of SOEs has failed to be accountable for its actions and this thesis addresses how a framework can prevent this going forward. Chapter one set the context of SOEs in Ireland, highlighting the vital role they play in Ireland. The chapter also sets out key corporate governance issues relevant to SOEs, as this set the basis for determining limitations to existing governance standards. The government's involvement in SOEs indicates how this is a fundamental issue with accountability as the government dual role of financier and supervisor gives rise to the third agency problem; two principles - being citizens and the government. Key issues of corporate governance standards were also outlined to provide a context of current corporate governance principles. This was linked to how corporate governance standards add to SOEs and how they strive to bring accountability, disclosure, transparency and fairness with SOEs. The remaining chapters sought to uncover how it is possible to achieve these principles. Chapter two examined how board accountability is dealt with internationally.

Chapter three focused on the regulatory model of governance for SOEs, which is largely driven by governance being implemented on a legislative and quasi legal basis. This investigated whether a sufficient level of board accountability can be attained from quasi legal framework. Arguments for and against implementing governance standards on a legislative basis formed part of the research, along with taking examples of the two approaches in different jurisdictions. Notably, New Zealand opted for a legislative basis and Australia has used a mix of both legislation and quasi legal standards, making both countries adequate comparators. Governance standards on a quasi-legal basis have not always been successful at promoting an adequate level of governance practices by SOEs. Imposing a legislative framework for governance standards implements a top down approach to governance standards. For Irish SOEs, it is recommended that a quasi-legal basis for governance provisions should be retained. A quasi-legal basis lends itself move favourably to governance for SOEs but this only will work where strong enforcement and

[1001] Moore, M. "The (neglected) value of board accountability in corporate governance" (2015) 9(1) *Law & Financial Markets Review* 10 p. 10.

compliance standards are part of the governance regime. It allows for more flexibility to allow a board to use governance provisions relevant to its entity. But a quasi-legal framework will only be successful if is properly supervised and later chapters offered methods to achieve this.

Chapter four focused on external and internal mechanisms of accountability for strengthening governance standards. The power at the board disposal demands sufficient accountability structures. The board has influence over SOEs and power provided by the government. An accountability regime should be proportionate to the power of the board.[1002] Ensuring effective implementation of standards is an important aspect to ensure a board is engaging with standards, so suitable checks are in place such as a consultation with the government. A board can be considered as having double edged responsibilities, to both internal and external environments and questions if there is a gap between public expectation and what the board is capable of achieving.[1003] This should be considered in the context of Irish SOEs, the government should not impinge on the freedom of the board but expected intrusion from the government should hang over the board so they are aware they may have to defend their actions.

Chapter five focused on how board accountability operates in practice, how a board engage with governance standards and it was found that there was very little monitoring of the board in FÁS, highlighting the accountability deficit. The scandal reduced faith in the ability of corporate governance standards to offer supervisory functions that could be relied upon. The freedom enjoyed by the board to spend money without interference did not sustain a healthy picture of the activities by board members. This allowed a clear conclusion to be drawn that existing governance principles were insufficient at restraining the board and accountability provisions are far too weak.

Consequently, chapter six progressed to offer measures that would assist in increasing board accountability and provided a framework on how governance can be strengthened

[1002] Keay, A & Loughrey, J. "The framework for board accountability in corporate governance" (2015) 35(2) Legal Studies Journal 252 p. 260.
[1003] Soltani, B. & Maupetit, C. "Importance of Core Values of Ethics, Integrity and Accountability in the European Corporate Governance Codes" (2015) 19 (2) *Journal of Management and Governance* 259 p. 260.

within SOEs. In addressing the accountability deficit for governance of SOEs, critical questions have been asked and solutions proposed on how corporate governance mechanisms can secure accountability within SOEs. This thesis has argued that increasing board supervision will improve their application of governance standards. It asserted that there are three key stages for a successful implementation of a governance regime. Firstly, a consultation process is required so both the board and the government are clear on the outcomes they are striving to achieve. The second stage is implementation of governance provisions, how they will be applied and how the board should be clear on their respective role. The third stage is the review process and is a vital stage so the board know they must defend their actions but also so the supervisory capacity of the government is not forgotten. These three stages of equal importance are the cornerstones to what a successful model of accountability will be based upon as outlined below.

C. TOWARD INCREASED BOARD ACCOUNTABILITY FOR SOES

This thesis raises the important question of how corporate governance standards should progress from this and what can be taken from this thesis to enhance good governance and increase board accountability. Effective mechanisms to combat the accountability deficit are set out below.

(1) Set targets for the board

It was concluded that one of the best methods of ensuring better board performance is to set targets. Monitoring of performance against targets is crucial to their effectiveness. Targets should be part of an annual strategic plan for SOEs. This will also serve as a tool for measuring board's performance. Targets should not be solely based on financial goals but a board should be familiar with the organisations objectives. Providing the Minister or supervisory body with clear guidance on what they are expected to achieve and how to do this will improve their performance. Setting targets gives responsibility to the board and allows them to take ownership of their own role within the SOE. Part of the targets for a board will be based on budget performance to incentivise the board to achieve value for money.

Target setting will harmonise external and internal obligations for the board. External obligations require the board to meet expectations from the government and stakeholders and targets will prevent the board failing short of obligations. Internal targets will encourage the board to work together and provide an incentive linking accountability to performance. The success of these targets could be measured through Annual Output Statements.

(2) Review performance

Making the board individually responsible for their performance may focus the board in applying governance standards but standards should ensure board members do not manipulate information to provide desired results.[1004] This may arise from the board limiting information it supplies and not co-operating with auditors. Sanctions should be balanced for not implementing standards. For example, board members should be put before PAC committee and publishing breaches in their performance in annual audits and in the annual report. Serious sanctions should result in board members being removed from their position. These recommendations contribute to the goal of the thesis and existing literature in increasing accountability of board members.

Setting targets for the board loses merit if its performance is not reviewed so pressure should be put on the board to ensure it is performing. This becomes a role for the relevant Minister to act to ensure regulatory enforcement, or a supervisory body to act on behalf of the government. This opens the channels of communication between the board and the Minister and doing so should give the government a clearer insight in the internal running of SOEs. A contentious issue surrounding this will be consequences for a board not meeting its targets and objectives. Perhaps a useful deterrent is for board members who do not reach their targets is to have this information be published.

[1004] Chiu, I. "Reviving Shareholder Stewardship: Critically Examining the Impact of Corporate Transparency Reforms in the UK" (2014) 38(3) *Delaware Journal of Corporate Law* 983 p. 1020.

Board members should also be accountable for its actions, even if they are no longer serving board members, if breaches of their duties do not come to light for some time. This should deter board members from taking risks. However, if board members are no longer serving members, the likely consequences is their failings to be made available publicly or preventing them serve on future boards.

(3) The Influence of Stakeholders

The role that key stakeholders affected by SOEs can play in increasing accountability should not be overlooked. Irish Water is an example of the public putting enough pressure on the government to resist the full introduction of water charges in Ireland. But the motive for stakeholders in this context is directly linked to the cost that would directly affect them. To engage stakeholders with other SOEs firstly, information should be available to them. Open documents being available will allow for greater transparency in the workings of SOEs. This information may not be in high demand and these documents may primarily be of interest to news reporters but allowing access to bring this information to the attention of the greater public will assist in generating public interest.

Currently, gathering information on corporate governance practices of SOEs is very difficult. As outlined in earlier chapters, what is contained within annual reports provides a snapshot to the board practices. Freedom of information requests were made as part of this thesis but they provided very little insight into SOEs as many requests were refused on grounds of the information being commercially sensitive. The information obtained from the FOI request on FÁS was information that was already in the public domain. To improve the process, transparency policies should be introduced. The result of this should allow stakeholders to review how the government have reacted to board performance and if they have been proactive with areas of governance weakness. After the FÁS saga, there were no renewed efforts to bring information into the public domain indicating the continued lack of drive in transparency. Transparency is concerned with the disclosure of information.[1005] To encourage stakeholder engagement accountability provisions should

[1005] Mäntysalo, V. "The Importance of Transparency in Ethical Governance: Current Research and Finnish Citizens Perceptions" (2015) 16(1) *Administrative Culture* 48.

promote public access to information from the board so there is increased transparency within SOEs.

(4) Ethical Standards

As already outlined there is undoubtedly a dependency on trust and openness between the board reporting to the government. This requires 'social accountability' as part of a governance arrangement:

"Rather than insisting on definitive accounting in the mechanical sense of the term, social accountability in the context of network governance promotes consensual processes rooted in forms of reciprocity"[1006]

Ethics should form part of governance principles to foster values of trust and fairness. Othman and Rahman argue, due to the subjective nature of governance, introducing morality as a core element will create good governance.[1007] Ethical standards will assist a board when it faces challenges, for example, it will assist in instances of conflicts of interest and encourage disclosing information to the government.

(5) The role of the State

One of the most important tasks for the State is to ensure that the benefits provided from accountability standards are not weakened. A zero tolerance policy needs to be in place for any corruption uncovered within SOEs, so that board members are automatically disbarred from serving on boards in SOEs. The issue remains how the government can ensure that accurate information is being reported from the board. The ability of the board to cover up information from the government is a contentious issue. Structures of transparency and mutual trust are unable to provide a solution to this, transparency on its own will not secure accountability.

[1006] Millar, H. "Comparing Accountability Relationships between Governments and non-State actors in Canadian and European International Development Policy" (2013) 56 (2) *Canadian Public Administration* 252 p. 252.
[1007] Othman, Z. & Rahman, A. "Attributes of Ethical Leadership in Leading Good Governance" (2014) 15(2) *International Journal of Business & Society* 359 p. 359.

As part of any review of accountability, the government's role requires firming up with the development and implementation of new procedures that are called for. This links back to the responsibility that stems from individual Ministers responsibility for their SOEs and what they need to do fulfil their obligations. This two way channel between the board and the government will hinge on the success of accountability. The board must act and be responsible within defined expectations and the board must ensure the board have met their obligations.

D. AN ACCOUNTABILITY FRAMEWORK

This thesis proposes an accountability framework within corporate governance standards within SOEs.

(1) The Planning and Consultation Process

The *Code of Practice* 2009 only calls for a strategic plan for a 3-5 year period with a focus on budget planning, this will not provide adequate safeguards to ensure annual compliance with the plan.[1008] For example, Bord Bia provides a statement of strategy but this is limited to business strategies for the SOE and governance measures are omitted.[1009] This thesis recommends that a board should establish a statement of corporate intent annually, that includes details on planned budget spending but also extends to listing their governance objectives. Implementing this on an annual basis will allow revisions the following year if the initial plan had over or underestimated targets. The 2016 Code has implemented part of this recommendation. The Code supports the idea that business plans are required to be reviewed annually and the board have to undertake an evaluation of their actual performance by reference to their strategic plan.[1010]

[1008] Department of Finance *Codes of Practice for the Governance of State-owned Bodies* (Dublin 2009) at principle 2.14 p. 4.
[1009] Bord Bia *Statement of Strategy* 2016-2018. Available at http://www.bordbia.ie/industry/manufacturers/insight/publications/CorporatePublications/StatementOfStrategy2016/Making-a-World-of-Difference-StatementOfStrategy2016.pdf Last accessed August 2017.
[1010] Supra note 1000 principle 1.19 p. 16.

This plan should be worked on collaboratively by the board and is subject to approval of the Minister, giving the Minister the power of a veto, if necessary. This will be in line with the principle of comply and co-operate recommended by this thesis. The expectation is the board will comply with governance provisions and if they do not, they co-operate with the Minister as to why they have not followed governance provisions. The board must advise if it anticipates governance provisions will apply to the SOE in the future. This is stricter and more proactive approach than the *Code of Practice* 2009 which places an obligation on SOEs to take reasonable steps to confirm the Code has been implemented and let the Minister know they have complied with standards.[1011] This recommendation falls more in line with the 2016 Code, where a board must co-operate with the Minister by providing written explanations for before choosing not to implement governance provisions.[1012]

Functions of the board should be appropriately separated and so, where the board is responsible for implementing strategy, this should be distinguished from their monitoring functions within SOEs.

It is recommended that the Minister should review monetary spending of SOEs and satisfy itself that SOEs are operating efficiently and following government policy on spending.

(2) Implementation – Application of Governance Standards

It is recommended that a board should be accountable individually and collectively for its actions. Board members should be aware of its authority and act within these limits and act in the best interest of an SOE. This will require the board to deliberate over the decisions it will have to stand over. This combines both a top down approach to accountability with a horizontal method, as collective accountability makes the board members accountable to each other, fostering a sense of mutual benefit.

The board should provide full and accurate information on the SOE to internal and external auditors to enable fair and true information to be reported.

[1011] Supra note 1008 principle 1.2 p. 2.
[1012] Ibid p. 8.

It is recommended board members should attend all board meetings. New board members should be given an induction and where necessary training to familiarise themselves with their role as a board member.
SOEs are required to achieve value for money and commercial SOEs are expected to be profitable. In the interests of disclosure, the board's remuneration should be made publicly available.

The *Code of Practice* 2016 requires directors to monitor conflicts of interests,[1013] however, it recommends that directors should free themselves from decision-making where situations of conflict of interest arise and not use their position to attain personal benefit.

(3) Review Process

The board is accountable to the Minister and is required to disclose information. It is recommended that the board should provide a background for decisions it has made. An important aspect of the board's duties is to approve or reject requests by those managing SOEs. The board should provide reasons for its decisions to ensure they are in line with public policy objectives. A review can also include retrospective elements and the board can be accountable for decisions made in preceding years. As highlighted in earlier chapters, Ministers reviewing SOE's performance can be problematic. In this regard, it may be more beneficial for an overseeing body such as NewERA to provide a supervisory function and report to the Minister.

The board has a responsibility for the economic performance of the SOE. If SOEs are not operating efficiently or achieving value for money, the board has an obligation to review the performance and implement necessary changes.

The Minster is responsible for monitoring and managing the State's interest in SOEs. The Minister for Finance should review the audit of SOEs and ensure value for money is being

[1013] Supra note 1000 principle 5 p. 27.

achieved. The Minister is required to make recommendations to the board on areas that require improvement.

The Minister is responsible to the government for their supervisory role of SOEs. They are answerable to Public Accounts Committee relating to matters on their responsible SOE.

An audit committee comprising at least three NEDs is required. Annual audit reports should be submitted to the Minister outlining the performance and results from the internal audit.

Non-executive directors should form part of the monitoring process and assist the government in monitoring the board particularly in scrutinising the actions of the board. They should also assist in areas of audit and setting remuneration.

Regarding penalties for not complying with governance standards, a distinction could be made between primary and secondary failures on corporate governance and the penalties could be allocated accordingly. For example, penalties for board members being named for breaching standards or withholding funding for SOEs could be implemented. However, culpability should always be linked back to intention with the expectation board members will not act recklessly or negligently. Therefore, if governance provisions do not apply to SOEs and this has been disclosed, then board members will have fulfilled their functions.

E. CONCLUSION

This thesis has extrapolated and addressed some of the more substantive issues for a regulatory framework for governance of SOEs and has found there are many obstacles that earlier versions of *Code of Practice* for SOEs failed to overcome. Prior chapters focused on the framework of previous governance codes and how they did not work as intended as it essentially failed to provide adequate safeguards and could not serve as a means to ensure the application of a sufficient level of governance standards. The recommendations contained within this thesis sets out proposals for implementing a better regime which should increase board accountability. The main argument running throughout this thesis is that the quality of corporate governance for SOEs is greatly compromised without adequate functioning mechanisms on board accountability. If board accountability provisions are weak, this undermined the entire governance framework. This was recognised in the updated *Code of Practice* 2016, which, as outlined in chapter six, reformed accountability provisions strengthening board accountability.

This thesis has provided an alternative approach to how accountability standards should be included in a governance framework for SOEs, reflecting on best practices internationally. Rather than listing all the duties and responsibilities of the board and Minister, this thesis focus on three key areas of how accountability can be enhanced through establishing a strategic plan, implementing this plan and reviewing how successful this plan was and what changes are required.

This framework will assist in dealing with both Agency and Stakeholder theory issues that arise in SOEs. As the framework recognises both the benefits and the responsibilities of disclosure requirements, this prevents the board from acting in their own interests and more in line with relevant stakeholders. To assist with the agency issue, bodies such as NewERA have the potential to monitor boards without direct State involvement. If monitoring SOEs comes from an independent entity it dilutes the agency issue, as it reduces the conflict of the State being both investor and regulator. It is not possible to guarantee independence from such bodies appointed by the State and report to the State, but nevertheless they act as a means of reducing State interference in SOEs. A monitoring

body should acknowledge the importance of stakeholders and operate with keeping the greater public interest as a key objective, to protect the interests of stakeholders.

A revised framework provides a guide to the board and Minister. From the research it becomes clear that monitoring a board on its own will not achieve desired results. Increased monitoring of how SOEs implement governance is required, this should be from the government or an entity established by State to take on this role. There must be a dual responsibility and commitment on the board to implement governance and report to the Minister. If this is achieved, accountability will be the facilitator for reaching a high standard of corporate governance. As many of the recommendations in this thesis were implemented in the updated Code of Practice 2016, a review of SOEs annual reports for 2017, which reflects on the updated Code will be interesting to read. The updated 2016 Code has increased board accountability and this has the potential to change the direction of governance in SOEs so it is envisaged that it will bring a positive result.

APPENDIX 1:

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APPENDIX 2:

FREEDOM OF INFORMATION REQUESTS