

IFC Corporate Governance Progression Matrix for State-Owned Enterprises

(Integrating Environmental, Social, and
Governance Issues)



© 2019 International Finance Corporation. All rights reserved.
2121 Pennsylvania Avenue, NW
Washington, DC 20433 USA
Internet: www.ifc.org

The material in this work is copyrighted. Copying and/or transmitting portions or all of this work without permission may be a violation of applicable law. IFC encourages dissemination of its work and will normally grant permission to reproduce portions of the work promptly, and when the reproduction is for educational and non-commercial purposes, without a fee, subject to such attributions and notices as we may reasonably require.

IFC does not guarantee the accuracy, reliability, or completeness of the content included in this work, or for the conclusions or judgments described herein, and accepts no responsibility or liability for any omissions or errors (including, without limitation, typographical errors and technical errors) in the content whatsoever or for reliance thereon. The boundaries, colors, denominations, and other information shown on any map in this work do not imply any judgment on the part of the World Bank concerning the legal status of any territory or the endorsement or acceptance of such boundaries. The findings, interpretations, and conclusions expressed in this volume do not necessarily reflect the views of the Executive Directors of the World Bank or the governments they represent.

The contents of this work are intended for general informational purposes only and are not intended to constitute legal, securities, or investment advice, an opinion regarding the appropriateness of any investment, or a solicitation of any type. IFC or its affiliates may have an investment in, provide other advice or services to, or otherwise have a financial interest in, certain of the companies and parties (including named herein).

All other queries on rights and licenses, including subsidiary rights, should be addressed to IFC's Corporate Relations Department, 2121 Pennsylvania Avenue, NW, Washington, DC 20433 USA.

International Finance Corporation is an international organization established by Articles of Agreement among its member countries, and a member of the World Bank Group. All names, logos, and trademarks are the property of IFC, and you may not use any of such materials for any purpose without the express written consent of IFC. Additionally, "International Finance Corporation" and "IFC" are registered trademarks of IFC and are protected under international law.

IFC Corporate Governance Progression Matrix for State-Owned Enterprises

(Integrating Environmental, Social, and Governance Issues)

A. Commitment to Environmental, Social, and Governance (Leadership and Culture)

	1. Basic Practices	+	2. Intermediate Practices	+	3. Good International Practices	+	4. Leadership
SOE Legal Framework	<ol style="list-style-type: none"> The SOE has a distinct legal personality from the state. The SOE is not entitled to invoke sovereign immunity and is not insulated from bankruptcy law. 		<ol style="list-style-type: none"> The SOE is corporatized under constituting statute or documents. The SOE operates on a level playing field with other industry competitors in that there are no laws, regulations or by-laws that would grant an unfair competitive advantage. 		<ol style="list-style-type: none"> The SOE is incorporated under the company law and all provisions and regulations of the company law applicable to private companies fully apply to the SOE. Laws and regulations applicable to private companies, including commercial, competition, bankruptcy and labor law apply equally to the SOE. 		
Operational Autonomy	<ol style="list-style-type: none"> The SOE has clearly identified and differentiated between its commercial and policy objectives. 		<ol style="list-style-type: none"> The SOE's commercial and policy objectives are explicit and disclosed to the public. Funding costs and sources, including any form of financial assistance¹ from the state are transparent and disclosed to the public. If any public procurement rules are applicable to the SOE, they do not unduly restrict the ability of the SOE to procure goods and services. 		<ol style="list-style-type: none"> The costs of meeting any policy objectives are funded separately by the state. The SOE conducts operations and engages in business just as private sector companies and freely submits to international arbitration and foreign law/jurisdiction in the context of international finance. Any restrictions related to the strategic nature of assets held by the SOE should be clearly defined and limited to specific asset class(es) only. 		<ol style="list-style-type: none"> The SOE's objectives are predominantly commercial. The SOE is, in practice and legally, fully autonomous from the state.
Formalities	<ol style="list-style-type: none"> The SOE addresses, through its constituting documents (e.g. articles of association) or corporate policies (e.g. board charter), CG principles and the role of the board. 		<ol style="list-style-type: none"> The SOE has a formal CG policy framework, through a CG manual or its set of constituting documents and corporate policies, addressing, at a minimum, CG principles, the role of the board, compliance with the law, rights and treatment of shareholders and other stakeholders and transparency and disclosure. A code of ethics and/or conduct is approved by the board and publicly disclosed. 		<ol style="list-style-type: none"> The policy framework also addresses E&S issues. A code of ethics is included in employee orientation program. 		<ol style="list-style-type: none"> Periodic disclosure to shareholders and the public on the SOE's CG framework and practices, their conformance to the country's national CG code of best practices is disseminated. The Codes of Ethics and/or conduct fully integrate ESG practices in business activities.
Designated Officer	<ol style="list-style-type: none"> A company officer serves as a corporate secretary. 				<ol style="list-style-type: none"> Designated full-time CG officer and/or company/corporate secretary. 		<ol style="list-style-type: none"> A compliance function ensures compliance with ESG policies and procedures, code of ethics and/or conduct.
Recognition			<ol style="list-style-type: none"> The SOE is publicly recognized, at least among SOEs, as a national leader in ESG practices. 		<ol style="list-style-type: none"> SOE is publicly recognized, at least among SOEs, as a regional leader in ESG practices. 		<ol style="list-style-type: none"> The company is publicly recognized, at least among SOEs, as a global leader in ESG practices.

¹ Includes: grants, subventions, subsidies or loans

B. Structure and Functioning of the Board of Directors

	1. Basic Practices	+	2. Intermediate Practices	+	3. Good International Practices	+	4. Leadership
Role	<ol style="list-style-type: none"> 1. The board is charged with objectively overseeing management. 2. The board formally reviews and approves the strategy. 		<ol style="list-style-type: none"> 1. The board sets and approves strategy independent from the state who only sets broad mandate and objectives. 2. The board ensures that key executive positions are filled and that the company has a strong CFO function. 		<ol style="list-style-type: none"> 1. The board is consulted on the selection, appointment and dismissal of the CEO and other members of senior management. 2. The board, or its specialized committee, formally evaluates the performance of the CEO and other C-Suite executives against Key Performance Indicators (KPIs) aligned with objectives. 3. The board has established a performance-linked executive compensation system aligned with the SOE's objectives. 		<ol style="list-style-type: none"> 1. The board is fully independent of the state and/or any government institutions. 2. The board is responsible for the selection, appointment, performance evaluation and dismissal of the CEO and other members of senior management.
Composition	<ol style="list-style-type: none"> 3. The SOE, the state or the ownership entity has adopted minimum education, experience and ethical requirements for the selection of board members. 4. The size of the board corresponds to the need for skills set diversity and is kept at a reasonable level (in any case between five and 15 members). 5. No ministers or elected officials serve on the board. 		<ol style="list-style-type: none"> 3. The board members are appointed for fixed renewable terms not exceeding three years. 4. Government officials with a regulatory role are prohibited from serving on the board. 5. The number of civil servants and employees from other SOEs serving on the board is restricted to less than 1/5 of the board. 6. The board composition is based on a skills matrix. 		<ol style="list-style-type: none"> 4. A formal, merit-based, and transparent process for the selection and nomination of board members, such as a board nomination policy is in place and publicly disclosed. 5. 1/3 or more of board members are independent from management, the state and controlling shareholders. 6. Roles of chair and CEO are separate. Board chair is independent from the state. 		<ol style="list-style-type: none"> 3. A board-established succession plan for board members and senior management is approved and implemented. 4. 1/2 or more of board members are defined as independent in accordance with international best practices.² 5. Board diversity, including gender and skill mix, is achieved.
Committees	<ol style="list-style-type: none"> 6. Directors have been assigned areas of focus, such as audit, nominations and risk. 		<ol style="list-style-type: none"> 7. The audit committee is fully non-executive. 		<ol style="list-style-type: none"> 7. Majority of audit committee membership is independent. 8. Specialized committees with independent members oversee conflicts of interest and technical topics (e.g., procurement technology/cybersecurity, E&S/sustainability, risk management, etc.), if applicable. 		<ol style="list-style-type: none"> 6. The audit committee membership is 100% independent. 7. Fully non-executive board nominations and compensation committee(s) are established. 8. Fully non-executive ESG or sustainability committee are established.

(continued on next page)

² For example, IFC's "Indicative Independent Director Definition."

B. Structure and Functioning of the Board of Directors *(continued from previous page)*

	1. Basic Practices	2. Intermediate Practices	3. Good International Practices	4. Leadership
Board Procedures	7. The board meets at least quarterly. 8. Board members are given sufficient time and information to exercise their duty.	8. The board members attend leadership and professional training on corporate governance and compliance. 9. The length and frequency of board and board committee meetings are adequate to enable the board to fulfill its role. 10. The board has defined in its charter its role and procedures. 11. The board undergoes periodic evaluation.	9. The board members receive induction and ongoing leadership and development training. 10. The board charter defines its role and procedures as well as those of its committees. 11. The board, committees and individual directors undergo an annual evaluation.	9. Independent directors meet separately at least once a year. 10. The board and committee evaluations are conducted/facilitated by a third party. 11. Outcomes of board evaluation are considered in making decisions to renew board mandates.
Oversight of E&S		10. The board is trained on general E&S risk issues.	11. Strategy and risk appetite integrate E&S issues/risks. 12. In sensitive industries, ³ at least one director is able to analyze E&S risks. 13. The board ensures that management systems are in place to identify and manage E&S risks and impacts.	12. The board is trained on industry E&S risk issues. 13. ESG issues are recurring board agenda items; board approves ESG strategy and E&S policies routinely; and ensures effectiveness of External Communications Mechanism (ECM). 14. Board reviews independent audits on effectiveness of Environment and Social Management System (ESMS), including stakeholder engagement processes and grievance mechanism.

Control Environment (Internal Control System, Internal Audit Function, Risk Governance And Compliance)

Internal Controls	1. The SOE has established documented internal control policies and procedures.	1. The audit committee ensures corrective actions on control deficiencies identified in Management Letters.	1. "Three lines of defense" model of risk management, internal control and internal audit has been adopted. ⁴	1. Control environment in accordance with highest international standards, including but not limited to IIA, ⁵ COSO, ISO 31000, 19600, 37001, and 27001.
Internal Audit	2. The SOE has an in-house or outsourced internal audit function. 3. The state audit institution, if any, interfaces with the internal auditors.	2. Internal audit function regularly interfaces with external auditors and is accountable to the board.	2. Head of internal audit reports to the audit committee and administratively to management. 3. The internal audit function is independent, objective, risk-based, and has unlimited scope of activity.	2. The internal audit function meets standards of the Institute of Internal Auditors (IIA). 3. The audit committee ensures that the internal audit function is subject to periodic quality assessment by third party.

³ Examples of "sensitive industries" include: oil, gas, mining, heavy industry (steel, cement), chemical manufacturers, and large agro-commodity production or processing.

⁴ Namely, management is the first line of defense, risk management and compliance function are the second line of defense, and internal and external audit as independent assurance providers are the third line of defense.

⁵ The Institute of Internal Auditors standards and related promulgations

(continued on next page)

Control Environment (Internal Control System, Internal Audit Function, Risk Governance And Compliance) *(continued from previous page)*

	1. Basic Practices	+	2. Intermediate Practices	+	3. Good International Practices	+	4. Leadership
Risk Governance			3. The Board receives and reviews information on key risks.		4. The Board approves risk appetite. 5. The SOE has established risk-management framework with a chief risk officer (CRO) or equivalent with unfettered access to the Board.		4. The board routinely monitors risk management and compliance with policies and procedures and discloses risk appetite information. 5. The CRO reports to board-level risk management committee or equivalent.
Compliance			4. A designated compliance officer is appointed.		6. Comprehensive compliance program annually reviewed, with mechanisms to report wrongdoing and misconduct.		6. The chief compliance officer reports to the audit committee and administratively to management.
External Audit	4. The SOE is audited by an independent external auditor (EA) irrespective of any state audit conducted. 5. Written Management Letters provided by an EA.		5. The audit committee is responsible for the selection of the External Audit and ensures their independence, including in relation to the provision of non-audit services.		7. Audit committee owns relationship with EA; agrees on scope and audit fees, has an early discussion on key audit matters and generally oversees the conduct of the external audit.		7. The audit committee undertakes a periodic EA quality assessment, using Audit Quality Indicators (AQI) and reviews EA long association.
Subsidiary Governance			6. The SOE has policies and procedures to control the creation and dissolution of subsidiaries.		8. A formal, merit-based, and transparent process for the selection and nomination of board members of subsidiaries, such as a board nomination policy is in place and disclosed.		8. The board of the holding SOE exercises oversight over the corporate governance framework of its subsidiaries.
Integrating of E&S			7. The SOE has established industry practices in its E&S risk management practices.		9. Comprehensive ESMS integrated in risk-management framework, and E&S risks are part of establishing the risk appetite. 10. E&S/sustainability head has unfettered access to senior management and CRO.		9. The board or sustainability committee ensures corrective actions on E&S issues. 10. The head of ESG reports to the board's E&S/sustainability committee. 11. ESMS is consistent with international standards (e.g., ISO 14001).

C. Disclosure and Transparency

	1. Basic Practices	+	2. Intermediate Practices	+	3. Good International Practices	+	4. Leadership
Financial Reporting	<ol style="list-style-type: none"> 1. The SOE publishes timely annual financial statements prepared in accordance with national standards of corporate accounting and audited by recognized independent external auditing firm. 		<ol style="list-style-type: none"> 1. The financial statements are prepared in accordance with International Financial Reporting Standards (IFRS) or equivalent unless more simplified reporting standards are warranted, such as IFRS for SMEs. 2. Financial statements are audited in accordance with International Standards on Auditing (ISA). 3. Audit committee approves accounting policies and estimates. 		<ol style="list-style-type: none"> 1. Financial statements separately report the impact of any state assistance or benefits. 2. The audit committee oversees financial and nonfinancial reporting and audit. 3. Disclosure policy is in place. 		
Corporate Disclosure	<ol style="list-style-type: none"> 2. The SOE prepares a publicly available annual report. 		<ol style="list-style-type: none"> 4. The SOE publicly discloses and reports on public service or policy obligations that go beyond commercial ones. 5. The SOE publicly discloses its stakeholder engagement policy and provides information on its implementation. 6. Each annual report includes management commentary, SOE policy and commercial objectives, and ESG information including specifically: ownership and control, risks, board composition and profile of board members. 		<ol style="list-style-type: none"> 4. The SOE publicly discloses separately the costs of meeting the company's policy objectives. 5. All public disclosures as well as communications with shareholders and stakeholders are made available online in a relevant and timely fashion. 6. The company discloses its internal procurement policies. 7. Summary information on all material contracts is disclosed to the public. 		<ol style="list-style-type: none"> 1. Executive compensation is disclosed. 2. Dividend policy is disclosed.
Risk Governance	<ol style="list-style-type: none"> 3. ESG/sustainability reporting, if any, follows minimum national requirement. 		<ol style="list-style-type: none"> 7. Information disclosed to Affected Communities is in understandable format and language. 		<ol style="list-style-type: none"> 8. ESG data subject to independent review. 9. Annual updates provided to locally affected communities. 		<ol style="list-style-type: none"> 3. Nonfinancial disclosure in accordance with highest international standards (e.g., GRI, IIRC, SASB). 4. Periodic nonfinancial reporting of ESG issues that are of concern to stakeholders.

D. Shareholders Rights

	1. Basic Practices	+	2. Intermediate Practices	+	3. Good International Practices	+	4. Leadership
Exercise of Ownership Rights by the State	<ol style="list-style-type: none"> 1. The state has identified an entity, agency or unit within the state administration to exercise its ownership rights on the SOE. 		<ol style="list-style-type: none"> 1. The ownership entity monitors SOE performance and voices any concerns through formal channels. 		<ol style="list-style-type: none"> 1. The ownership functions, with respect to all SOEs, are centralized in a single entity under one ministry. 2. A performance agreement or MOU is in place between the ownership entity and the SOE and is made publicly available. 3. The State has not been vested with golden shares or other types of special rights which would allow the state to block major corporate decisions. 		<ol style="list-style-type: none"> 1. The ownership functions, with respect to all SOEs, are centralized in a single independent entity. 2. Formal ownership policy is in place and publicly available. 3. The framework to monitor SOE performance includes adequate valuation methods and systematic benchmarking against both private and public-sector entities.
Minority Rights	<ol style="list-style-type: none"> 2. All shareholders of the same class have equal voting, subscription, and transfer rights. 3. Minority shareholders receive adequate notice and the agenda for all shareholders' meetings and are permitted to participate and vote at shareholders' meetings. 		<ol style="list-style-type: none"> 2. Effective representation of minority shareholders through cumulative voting or similar mechanisms and economic rights such as inspection rights, exit rights, and tag-along rights. 3. The SOE has a dividend policy and does not issue dividends to the state outside of the scope of this policy. 4. Policies are clearly communicated and enforced regarding the treatment of minority shareholders during of control transitions, including privatizations and re-nationalization. 		<ol style="list-style-type: none"> 4. Effective shareholder voting mechanisms are in place to protect minority shareholders from concentrated ownership or strong conflicts of interest with controlling shareholders (e.g., supermajority or "majority of minority" provisions). 5. Shareholders vote on executive compensation. 		<ol style="list-style-type: none"> 4. Treatment of shareholders consistent with best international market practices. 5. Executive compensation subject to shareholder approval.
Protective Rights	<ol style="list-style-type: none"> 4. Holders of all securities of the same type and class have access to equal information (fair disclosure). 5. Shareholders are provided with accurate and timely information regarding the number of shares of all classes held by the state and other major shareholders. 		<ol style="list-style-type: none"> 5. Well-understood policy and practice of full and timely disclosure to shareholders of all material related-party transactions and shareholder agreements. 6. Rules on related party transactions specifically address transactions with the government and other SOEs and require recusal by interested shareholders and board members. 7. Annual report discloses material risks to minority shareholders associated with the state ownership, other controlling shareholders, ownership concentration, cross-holdings, and voting-power imbalances. 		<ol style="list-style-type: none"> 6. Well-understood policy and practices of material transactions that could potentially affect the rights of minority shareholders. 		<ol style="list-style-type: none"> 6. Related-party transactions (over 2.5% of net assets or \$150,000) subject to shareholder approval or stricter requirements.⁶ 7. No special type of shares is held by the state.

⁶ Often, requisite thresholds are set by law/regulation in the listing jurisdiction; however, the OECD has recommended the referenced limits. See OECD, *Guide on Fighting Abusive Related Party Transactions in Asia* (2009) 31.

E. Governance of Stakeholder Engagement⁷

	1. Basic Practices	+	2. Intermediate Practices	+	3. Good International Practices	+	4. Leadership
Stakeholder Mapping	1. Ad hoc stakeholder-identification, including workers, customers, regulators, and the local affected community.		1. Key stakeholders identified also include local nongovernmental organizations (NGOs) and civil society organizations (CSOs).		1. Formal stakeholder-mapping process and expanded definition of stakeholders includes contracted workers, primary-supply-chain workers, neighboring projects, and international NGOs and CSOs.		1. Senior executive responsible for stakeholder relationships, including ensuring integration with strategy and target setting, appointed.
Stakeholder Engagement Policy	2. Stakeholders have access to redress through unbiased legal or arbitration processes when they consider that their rights have been violated.		2. Established Stakeholder Engagement (SE) policy and procedures. 3. The SOE publicly discloses its SE policy and provides information on its implementation.		2. SE policy and strategy include procedures with stakeholder analysis, differentiated approaches for priority groups, iterative disclosure and consultation requirements, and reporting. ⁸		2. Commitment to SE is visible to staff, contractors, suppliers, and collaborators through codes of conduct setting out expectations for stakeholder interactions and human rights.
Worker Grievance Mechanism	3. HR policy and procedures for worker engagement in place.		2. Established whistleblowing policy and basic grievance mechanism for workers. 5. Management responds to grievances from workers and contracted workers. 6. The board is informed about grievance outcomes and trends on a regular basis.		3. Workers are granted confidential direct access to a company ombudsman or an independent board member.		3. Issues raised through grievance mechanism for workers are analyzed and resolved with the participation of a worker representative.
Affected Communities Grievance Mechanism	4. Informal response to stakeholder requests and concerns.		7. External Communications Mechanism for stakeholder questions and complaints, and if there are Affected Communities, a grievance mechanism is established.		4. External and publicly accessible communication procedure. ⁹ 5. Grievance mechanism facilitates the resolution of concerns from Affected Communities. 6. Designated Affected Communities engagement personnel have clearly defined responsibilities, training, and reporting lines to senior management and the board. 7. SE policy incorporated into requirements for contractors. 8. Unresolved stakeholder issues require a management action plan.		4. Periodic analysis of grievances to identify trends and root causes is conducted by senior management. 5. Senior management participates actively in international industry discussions on related topics. 6. SE and reporting consistent with international standards (AA1000 Standards on Stakeholder Engagement and Accountability Principles and ISO 26000).

⁷ This section should not be completed without consulting with the assigned E&S Specialist. If assigned E&S Specialist is not a Social Specialist, consult with Social Specialist.

⁸ Consult with Social Specialist to determine quality of SE policy, strategy, and procedures, if applicable.

⁹ Consult with Social Specialist to determine whether communication procedure is adequate to (a) receive and register external communication from the public; (b) assess issues raised and determine response; (c) provide and document responses, if any; and (d) adjust the management program, as appropriate and if applicable.

2121 Pennsylvania Avenue, NW
Washington, DC 20433 USA

Tel: +1 (202) 458-8097

www.ifc.org/corporategovernance
www.ifc.org/sustainability

April 2019