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Disclaimer: The views expressed in this presentation are my own and do not necessarily represent the opinions of the OECD or its member countries.

Introduction

At the OECD, we have been working for many decades to help strengthen the corporate governance frameworks of emerging economies, providing a platform where they can share experience, identify best practices and together develop international standards and guidelines, like the OECD Principles of Corporate Governance.

But we also understand that implementation of standards requires adaptation to varying legal, economic and cultural circumstances. I invite you all to visit our website to learn about this, in particular about our work in the Russian Federation at www.oecd.org/daf/corporateaffairs/russia

Since 2010 the OECD Corporate Governance Committee is publishing a series of thematic country reviews examining specific areas of corporate governance both in developed and emerging economies. These reviews provide recommendations concerning good practices and assist market participants and policy makers to respond to emerging risks.

In the next minutes I would like to share with you a glimpse to what we have learned from these reports, which by the way you can find in our website available for download at www.oecd.org/daf/corporateaffairs.

Board practices

In 2010 we published a review of board practices regarding remuneration. It covers developments in 29 countries, including in-depth reviews of Brazil, Japan, Portugal, Sweden and the United Kingdom.

After the financial crisis the ability of the board to effectively oversee executive remuneration, as recommended by the OECD Principles of Corporate Governance, appeared to be a key challenge in practice in many countries around the world.

The report shows that across countries the nature of that challenge goes beyond setting the level of executive and director remuneration. Because it also encompasses how remuneration and incentive arrangements are aligned with the longer term interests of the company. A particularly important issue, which the board should manage, is the connection between remuneration structure and company risks.

The report shows that, in general, legislators and regulators capacity to influence remuneration outcomes via hard means is quite limited, and in fact very few jurisdictions had legislated specific measures. Policy makers have rightly focused more on measures that seek to improve the capacity of firm governance structures to produce appropriate remuneration and incentive outcomes. Many jurisdictions have favored soft law measures.

A common perception is that remuneration structures and levels in firms with a controlling shareholder, and in jurisdictions where controlling shareholders are more prevalent, are less aggressive than in companies and jurisdictions characterized by dispersed share ownership.

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However, even in jurisdictions characterized by block holders and concentrated ownership, there is still a question about how to ensure that executive incentives are tied to the longer term interest of the company as a whole, rather than to the interests of the dominant shareholder.

Performance-based pay instruments are often put forward as a solution but there are significant problems.

The key challenge for boards is to understand how risk flows through the structure of remuneration and, as importantly, the remuneration metrics. The report suggests that boards should establish explicit governance processes for setting remuneration, where the roles and responsibilities of those involved are clearly defined and separated, and could benefit from assigning a greater role to independent directors.

However, not all processes concern the board. Some policy options have also focused on improving shareholder engagement and remuneration disclosure. The report suggests that the effectiveness of "say on pay" provisions is fundamentally linked to having active and informed shareholders with a sufficient capacity to influence the board.

Institutional investors

This is in fact a good link to our second peer review report, on the role of institutional investors in promoting better corporate governance. This report investigates includes three peer reviews on the implementation of Principles (of Australia, Chile and Germany) and a general review of 26 jurisdictions.

The OECD Principles of Corporate Governance embrace the underlying assumption that shareholders can best look after their own interests, provided they have sufficient rights and access to information.

The increased presence of large institutional investors in the last decade fostered the expectation that a new breed of highly skilled and well resourced professional shareholders would make informed use of their rights, promoting good corporate governance in companies in which they invest. However, institutional investors are not like other shareholders but have a unique set of costs, benefits and objectives and, more importantly, in practice have not always behaved as desired.

By 2009, institutional investors managed an estimated USD 53 trillion of assets in the OECD area, including USD 22 trillion in equity. These numbers do not include large investments made by fund managers directly under their client's name, this is just AUM. From year 2000 to 2007, right before the financial crisis, the volume almost doubled.

With the goal of optimizing returns for targeted levels of risk, as well as for prudential regulation, institutional investors have diversified their investments into large portfolios, many of them having investments in thousands of companies. Some managers pursue active investment strategies, but increasingly, they passively manage against a benchmark, resorting to indexing. At the same time, the investment chain has lengthened by outsourcing of management, further distancing investee companies from the beneficial owners.

As a result, incentives do not always stimulate institutional investors to engage in monitoring the corporate governance practices of investee companies.

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Moreover, unlike in the case of private equity and hedge funds, most institutional investors are not remunerated on the basis of the performance of portfolio companies, but on the basis of the volume of assets under management. Mandates for fund managers are also getting shorter, not exceeding three years. Taken together, these factors favor a focus on increasing the size of assets under management and on investing them in indices, rather than on improving the performance of portfolio companies.

A key problem identified in the report is that domestic investors in many jurisdictions do not vote their foreign equity. This is important because foreign shareholders make up around 30% of ownership in many jurisdictions. This could in principle be solved by making use of proxy advisors, but this raises other concerns like the already large influence of proxy voting industry and some one-size-fit-all policies that do not sufficiently differentiate by country and by company. There is also the question of conflicts of interest prevalent in the industry.

And there is also the issue of whether institutional investors are becoming increasingly short-term investors, or at least promoting short-term thinking by investee companies.

In sum, the nature of institutional investors has evidently evolved over the years into a complex system of financial institutions and fund management companies with their own corporate governance issues and incentive structures.

However, the country reviews also show that a great deal can be done both by private agents and policy makers to improve the corporate governance outcomes of institutional investors' behavior.

In the private sector, enhancing collaboration among institutional investors, as by establishing industry associations to share the costs of monitoring and voting have shown positive results. That is the case of Australia, for example.

On the public policy side, prudential regulations sometimes excessively limit holdings by institutional investors in individual companies and restrictions on incentive schemes may also change their behavior in an unintended manner. In Chile, characterized by concentrated ownership and dominant company groups, policy has increased the powers of institutional investors and created incentives for cooperation on the election of independent board members, with encouraging results.

Board nomination and election

This gives me an opportunity to tell you something about our forthcoming report, on board nomination and election. Four jurisdictions were subject to the in-depth review: Indonesia, Korea, the Netherlands and the United States. Twenty one jurisdictions participating in the work of the OECD Corporate Governance Committee also provided general background information.

Apart from the appointment of the senior management team, including the CEO, the next most crucial event for a company is the nomination and election of its board members. The Principles define that it is a basic shareholder right to elect and remove board members and call for the "facilitation" of "effective" shareholder participation in the nomination and election of board members.

With respect to the jurisdictions under review, shareholders are often permitted, with or without an ownership threshold, to nominate board members. The United States is the exception, with the board generally having the prerogative of nomination unless it decides to

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accept shareholder proposals voluntarily. This may force shareholders to initiate expensive proxy contests if they want to replace incumbent directors.

However, around the world contested elections are rare even though in the United States this might be due, in part, to high costs of a challenge. It seems the shareholder right is a bargaining mechanism with boards and controlling shareholders either over corporate policy or to have a board member elected or changed. Indeed it seems that in a number of jurisdictions, such as the United States and the Netherlands, shareholders, and especially institutional ones, have significant communications with the company.

It is thus hard to say categorically whether shareholders have an "effective" participation, especially in jurisdictions with controlling shareholders which is the typical pattern outside the United Kingdom and the United States. Some jurisdictions such as Italy and Israel have special voting arrangements to facilitate effective participation by minority shareholders.

A number allow cumulative voting although, with the exception of Chile, it is seldom viewed as having a major positive effect, perhaps because it assumes shareholder cooperation that is rare. A number of others such as Korea have simply a requirement for the number of independent board members which are necessarily elected by controlling shareholders. This raises questions around the world about what independence means in such circumstances.

A practice that reduces effective participation by shareholders is voting by a show of hands such as in India.

The board's role in selecting candidates for nomination is changing in many jurisdictions with a greater role for board assessments facilitated by outside advisors who also play a role in locating suitable candidates. In the United States, it is necessary to disclose the selection search advisor and any conflicts of interest they may have.

With respect to transparency, there is a need for improvement in many jurisdictions especially with respect to disclosure of directors' qualifications and to other board appointments that they may hold.

In sum, like in the other reviews, the conclusion is that the Principles, in their role as international standards, are a good guide to the outcomes that should be expected from companies with respect to key corporate practices. However, it is also true that both in developed and emerging markets, country specific issues like the ownership structure and the presence of controlling shareholders or company groups, significantly affect the manner in which such outcomes and practices are achieved.

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