CFA Society Brazil

POLICY BRIEF

CORPORATE GOVERNANCE OF STATE-OWNED ENTERPRISES IN BRAZIL

Becoming aligned with international best practices

Fight against corruption in Brazil is in the spotlight: market participants and civil society are claiming for improvement in the governance of state-owned enterprises (SOEs). Robust corporate governance is regarded as an antidote to corporate-level corruption by promoting transparency and better grounds for accountability.

BACKGROUND AND POLICY DEVELOPMENTS

- Brazil is currently coping with important challenges in face of corruption scandals, which in some cases involve the misuse of SOEs resources. Data published by the Federation of Industries in the State of Sao Paulo estimate that corruption amounts to as much as 2.3% of Brazil's GDP.
- In April 2015, BM&FBovespa launched the SOE Governance Program, which focuses on transparency, internal controls, board composition, and the obligations of the Public Controlling Shareholder.
- In June 2015, IBGC (a not-for-profit organization that promotes best Corporate Governance practices in Brazil) published a set of recommendations for SOEs. The guidelines encompass the State's roles as regulator and controlling shareholder, the Administration and Fiscal Boards, transactions with related parties, internal controls and compliance, transparency, and information disclosure.
- There are currently in Brazil proposals under discussion in Congress that may alter Corporate Law, specifically concerning issues pertaining to SOEs. Such changes should bring Corporate Governance of SOEs closer to international best practices.

CFA SOCIETY BRAZIL ACTIONS AND FURTHER READINGS

- The Advocacy Committee of CFA Society Brazil contributed in the BM&FBovespa hearing (held in April 2015), based on an ample survey among its members and the participation in the round of discussions held with selected market entities. The suggestions of CFA Society Brazil covered key issues such as transparency, the conciliation of public and private interests inherent to SOEs mission statements and by-laws, product pricing policies and especially reporting practices concerning capital expenditures. Such suggestions were partially incorporated into the set of requirements established in BM&FBovespa's SOE Governance Program.
- BM&FBovespa's SOE Governance Program. Available at www.bmfbovespa.com.br.
- IBGC's Guidelines for SOEs. Available at www.ibgc.org.br.
- Article on the governance of SOEs written by Ana Novaes, CFA, member of the Advocacy Committee of CFA Society Brazil. Available at http://www.ibgc.org.br/inter.php?id=19628.

CFA SOCIETY BRAZIL VIEWPOINT

- The poor governance of Brazilian SOEs brings significant economic and political costs for the Brazilian society. Best international corporate governance practices for SOEs focus on the separation between two conflicting attributions of the State: controlling ownership and regulatory role.
- Emphasis on short-term political actions/policies, as opposed to long-term economic sustainability, is an important factor negatively affecting SOEs valuations compared to their peers.
- The Brazilian legal framework is complex and contributes to the existence of conflicting objectives SOEs carry in their by-laws. All companies must abide by Corporate Law and their own by-laws. International recommended best practices emphasize that there should be no distinction between the way SOEs and purely privately owned companies pursue shareholder's interests.
- The Board and executives of a SOE must balance diverse interests in the company's growth and sustainability while managing the company, considering all the different perspectives of shareholders.
- The existence of a structured and transparent way for the appointment of Board members is critical to prevent political pressures on the SOEs. In such companies, the State should delegate the nomination of CEOs to the Board, which is ultimately where responsibility lies for guiding and monitoring executives concerning the companies' objectives.
- Obligations of SOEs related to the public interest and their cost must be clearly disclosed. The Board must monitor the achievement of objectives and communicate effectively with shareholders and the public.
- When disclosing the return on investments, obligations towards public interest and those aiming at maximizing financial and economic returns should be clearly separated, guaranteeing full disclosure of the targeted investment returns at SOEs and their justification.