



CORPORATE GOVERNANCE -BOARDS OF PARTNERSHIPS AND STATE OWNED ENTITIES IN MINERALS, OIL AND GAS INDUSTRIES. "A PERSONAL PERSPECTIVE BY SHEILA KHAMA"

Preface



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PREFACE

In recent years, governance of minerals, oil and gas industries has been brought into sharp focus. Books have mainly been written about resources governance from a policy and corporate perspective. Given challenges facing governments as investors in developing the resources, these publications are limited in one important respect. The publications tend to focus on the State's custodial responsibility and regulatory functions. Less attention is paid to the role of governments in their capacity as investors with shareholder responsibility for strategically leading companies in which the State has a stake. Yet, unless public officers give equal and adequate attention to their responsibility as representatives of shareholders, the capacity of the State to reduce risk is and will continue to be compromised. After all, in many of the countries (thanks to minerals, oil, and gas wealth), State-Owned Entities (SOEs) and other companies in which governments have an equity stake are often the largest investors and sources of public revenue. In 2018, the IFC reported 'SOEs account for 20% of investment, 5% of employment and up to 40% of domestic output in countries around the world. They deliver critical services in key economic sectors, including utilities, finance, and natural resources.'¹ A 2017 report by the IMF suggested that the government take (equity) in petroleum-producing countries ranges from about 60% to 85%.² SOEs are less dominant in the mining sector, but still play an important role in the economies of many countries.

When it comes to managing state investments in the minerals, oil and gas industries, governments in the Gulf region and South East Asia fare better. In these parts of the world, the State assumes tighter control and assumes leadership in determining long-term business strategy for resource exploitation and the direction that SOEs take. Governments in these parts of the world look past rent collection to much broader economic benefits of resource endowment. While recognizing injustices of past colonial masters and current global trade distortions, the governments go beyond rhetoric and put strategies in place to reverse their countries' fortunes. Efficient management of state-owned companies is one of the major vehicles for achieving this and is underpinned by state's capacity to successfully leverage natural resources wealth. Unfortunately, the same cannot be said for many countries, especially in Africa, former Soviet states and parts of Latin America, where the political economy prevails.

Though a lot has been written about corporate governance, the publications are limited in two ways. In the first instance, the publications are generic and do not address corporate governance as peculiar to the environment of minerals, oil and gas companies. The publications also focus largely on foreign private sector entities doing business in the developing world. On one hand this is understandable given the significantly larger footprint of foreign owned entities. However, the limited attention given to the subject as relates to SOEs and partnerships between governments and multinationals is inexplicable given the importance of minerals, oil and gas companies in many developing countries. Because of the risk that poor corporate governance of such entities poses in resources rich countries, the unique corporate governance challenges facing such companies do, however, deserve greater scrutiny. Below are some of the reasons I believe the matter warrants attention.

¹ State-Owned Enterprises (ifc.org), 2018

² www.degruyter.com, Review of Middle East Economics and Finance Volume 12 Issue 3 (2016)

As a director of boards of partnerships with a state, I was struck by the inherently different mindset of representatives of public and private shareholders. I am also acutely aware of the impact that the divergent goals of public and private sector shareholders and their representatives can have on companies. This includes the tension it creates and the influence that this has on decisions taken by the board and therefore the board's effectiveness as the custodian of corporate strategy and protector of shareholder interests.

I have also been struck by the disproportionate level of expertise between public officials whose skills base is rooted in the public sector and those of their private sector peers whose skills base is typically rooted in the core business of the companies. Most commentators suggest that this situation suits private sector representatives. My experience suggests to the contrary because any lack of alignment between representatives of shareholders and lack of synergy on the board can cripple a company and does not serve either party in the long run. It is also a source of frustration for all and can lead to decisions that are based on compromise and not the core interests of the company. The result is sub-optimal board outcomes. This alone should be a major source of concern for the shareholders including the state because in the end it undermines corporate performance.

But public officials are not the only ones who need to be competent in the boardroom. I also witnessed a skills gap on the part of first-time senior management appointees of private companies nominated to serve on the boards of subsidiaries in a non-executive capacity. At this stage in their careers, the appointees would typically have distinguished themselves in their professional areas of expertise. But, being a competent metallurgist, lawyer, engineer, geologist or marketing executive alone is insufficient to transform an individual into an effective member of a board of directors. The difference between private companies and government nominees, however, is that companies make a conscious effort to ensure their candidates receive sufficient support to discharge their duties. Secondly, they have mentors and others to learn from in the course of their day-to-day work. By contrast, public officials leave the boardroom and go back to a completely different work environment. In my experience, this is one of the greatest sources of disadvantage for state appointees. It stems from the fact that their day jobs often fundamentally differ from the core business of the companies on whose boards they serve. As such thought needs to be given to how to bridge this gap.

These and other considerations are my motivation for the approach to this book. I use these experiences to make the point that board effectiveness in state-owned companies and partnership is often taken for granted and that state shareholders do not proactively and adequately prepare their nominees to discharge their duties competently. Given this and the fact that minerals, oil and gas resources are finite public assets, the implications of an ill-prepared board nominee charged with the responsibility to protect public interest has potentially dire inter-generational consequences. This is more than sufficient justification to give the matter additional attention.

Purpose, Approach and Target Audiences

Therefore, this book is my contribution towards some solution and is written in the full knowledge that it can only be a small part of a much bigger and complex jigsaw puzzle of minerals, oil and gas corporate governance. So, it is not intended to be a toolkit or a complete guide for directors who find themselves in this unenviable position. Instead, the book is intended to do a few things. The first is to raise an alarm by drawing attention to the problem. The next is to highlight specific

areas that, if addressed, could help minimize the risk of lack of board effectiveness. It is intended to provide broad parameters for increasing the effectiveness of directors representing sovereign states and *de facto* public interests. Finally, the book is intended to assist those responsible for selecting and nominating representatives with some guiding principles for performing the function in a way that sets the appointees up for success. I suggest the specific actions and approaches to the appointment of directors.

Regarding the audiences, I am writing this book for policymakers in the first instance. It is intended to serve as a framework of reference for policymakers responsible for decisions on a few issues. Firstly, the all-important question of the criteria for selecting nominees to the boards. Another matter is the need to ensure the competency of nominees to discharge their duties. Finally, the question of the effectiveness of state representatives. Hence, the publication is not only intended to raise awareness, but I hope it leads to some rethinking of ways and means by which relevant decisions and policies on board memberships are made and performance assessed.

The publication will also be useful for organizations that have been set up to build institutional and skills capacity of governments to steward extractives resources development. In my experience, many such institutions invest a disproportionate amount of time on theory. I am sure this is necessary on some level, but in the space of corporate governance some practical knowledge is essential. The book therefore is intended to balance theory with practice by providing some insights into the boardroom environment.

By the same token, civil society organizations that advocate good governance in these industries will benefit from the content by having an additional lens through which to assess state effectiveness in protecting public interests. I hope that think-tanks and researchers will also find the book interesting and the content worthy of further analysis. Though the book draws primarily from minerals, oil and gas business environments, many of the issues covered have relevance across other industries in which SOEs are prevalent.

For individual directors, the book sounds a word of caution for those who take the responsibility of being a director and custodian of public interests lightly. Some wear the appointments as a badge of honour and maybe it is. However, there is nothing light about a director's responsibilities, especially as relates to non-renewable public assets and publicly listed companies. For my part, I always thought of my appointments as a burden of responsibility instead.

Finally, I remind the reader that the book is not based on research but draws directly from my own 20 years experiences as director and advisor of some of the mining industry's largest companies. It speaks to the practical and experiential aspects rather the legal or policy aspects of corporate governance. I use case studies to transport the minds of appointees into the boardroom and other decision-making fora. In the interest of confidentiality, I do not always reveal personal and corporate identities that are the subjects of the case studies. But, if I do, it is either because the matter is already in the public domain or with the explicit consent of the entities and their representatives. I occasionally share common scenarios that confront directors and provide a perspective on ways and means to respond in ways that can increase individual director and board effectiveness.
