ecoDa Corporate Governance Guidance and Principles for Unlisted Companies in Europe

New Edition - Short Version
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ecoDa
The European Voice of Directors

Executive Summary

Unlisted companies make a major contribution to economic growth and employment in all EU member states. According to the OECD, improved corporate governance amongst unlisted companies has the potential to significantly boost productivity growth and job creation in both developed and developing economies, as well as benefiting the company itself.

In the eleven years since the first edition of this guidance was published, the scope of corporate governance has widened. It is now often viewed as a component of a company's broader ESG (Environmental, Social, Governance) strategy. Partly as a result, the governance of unlisted companies is now attracting more attention from regulators and stakeholders.

However, it remains the case that there is limited recognition of the need for a distinct corporate governance framework that is appropriate for unlisted companies. In particular, most officially-endorsed corporate governance codes relate to listed rather than unlisted companies, who face different challenges and have different needs.

Most unlisted enterprises are owned and controlled by single individuals or by coalitions of company insiders such as families. In many cases, owners continue to play a significant direct role in management. Good governance in this context is primarily concerned with establishing a framework of company processes and attitudes that add value to the business and help ensure its long-term continuity and success.

Shareholders in unlisted companies are typically restricted in terms of their ability to sell their ownership stakes. This lack of liquidity presents shareholders with a significant investment risk. Investors are forced to commit themselves to the company for the medium to longer term. An effective corporate governance framework provides a way of mitigating this risk.

Furthermore, the voluntary adoption of sound governance practices by unlisted companies themselves may reduce the risk that a 'business-unfriendly' regulatory regime is imposed on them by policy makers in the future.

There is much to be gained from highlighting the specific governance issues of unlisted enterprises and outlining best practice solutions in the form of a set of voluntary corporate governance principles. That is the purpose of this guidance.

This guidance takes unlisted companies through the issues involved in designing their own corporate governance framework. It also presents a set of governance principles that can be followed or not. Determination of the most suitable governance framework for the company should largely be a matter for the shareholders and directors.

The principles are designed to take into account the size, complexity and level of maturity of individual companies, and their objectives concerning their own development. The guidance recognises that a 'one-size-fit-all' approach to governance frameworks at unlisted companies would be unhelpful. Given the diversity amongst unlisted firms, corporate governance principles should be applied in a pragmatic and flexible manner, reflecting the individual circumstances of each company.

A dynamic approach towards governance is essential since governance frameworks must evolve over the life cycle of a business firm. A corporation will generally develop a new governance structure and approach in anticipation of its next major strategic move or phase in development or financing structure.

By distinguishing between principles that are relevant to all companies and those relevant only to larger and more complex companies, or those seeking to grow, the guidance provides a governance roadmap for family owners or founder-entrepreneurs as they plan the development of their companies over the corporate life cycle.

In order to provide further assistance to companies, ecoDa has developed a self-evaluation questionnaire that boards can use to assess the extent to which they are already applying the principles and identify whether there are areas in which they might want to consider taking action to strengthen their governance framework.
This questionnaire can be found here.

Phase 1 principles:
Corporate governance principles applicable to all unlisted companies

Principle 1: Shareholders should establish an appropriate constitutional and governance framework for the company.

Principle 2: Every company should strive to establish an effective board, which is collectively responsible for the long-term success of the company, including the definition of corporate purpose and strategy. However, an interim step on the road to an effective (and independent) board may be the creation of an advisory board.

Principle 3: The size and composition of the board should reflect the scale and complexity of the company's activities, and take into account an appropriate level of diversity in its composition.

Principle 4: The board should meet sufficiently regularly to discharge its duties and be supplied in a timely manner with appropriate information.

Principle 5: Levels of remuneration should be sufficient to attract, retain, and motivate executives and non-executives board members of the quality required to run the company successfully.

Principle 6: The board is responsible for risk oversight and should maintain a sound system of internal control to safeguard the company's assets and the long-term interests of stakeholders.

Principle 7: There should be a dialogue between the board, shareholders and other key stakeholders based on a mutual understanding of objectives. The board as a whole has responsibility for ensuring that a satisfactory dialogue with shareholders and stakeholders takes place. The board should not forget that all shareholders have to be treated equally, and that each category of relevant stakeholder should be treated appropriately.

Principle 8: All board members should receive induction on joining the board and should regularly update and refresh their skills and knowledge.

Principle 9: Family-controlled companies should establish family governance mechanisms that promote coordination and mutual understanding amongst family members, as well as organise the relationships between family governance and corporate governance.

Phase 2 principles: Corporate governance principles applicable to large and/or more complex unlisted companies[1]

Principle 10: There should be a clear division of responsibilities at the head of the company between the running of the board and the running of the company's business. No one individual should have unrestricted powers of decision.

Principle 11: Board structures vary according to national regulatory requirements and business norms. However, all boards should contain members with a sufficient mix of competencies and experiences. No single person (or small group of individuals) should dominate the board's decision-making.

Principle 12: The board should establish appropriate board committees in order to allow a more effective discharge of its duties.

Principle 13: The board should undertake a periodic appraisal of its own performance and that of each individual board member.

Principle 14: The board should present a balanced and understandable assessment of the company's position and prospects for external stakeholders and establish a suitable programme of stakeholder engagement.

For more information, the main document can be found here.

1. Unlisted companies with significant external financing; and/or those aspiring to a public listing.

ecoDa Member Institutes

About the European Confederation of Directors Associations:

The European Confederation of Directors Associations (ecoDa) is a not-for- profit association founded in December 2004 under the laws of Belgium. Through its 21 national institutes of directors (the main national institutes existing in Europe), ecoDa represents approximately 55,000 board directors from across the EU. ecoDa's member organizations represent board directors from the largest public companies to the smallest private firms, both listed and unlisted.

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