

STATES OF JERSEY



STATES OWNED OR CONTROLLED COMPANIES: RIGHTS AND RESPONSIBILITIES (P.100/2014) – AMENDMENT

Lodged au Greffe on 24th June 2014
by Deputy R.G. Le Hérisier of St. Saviour

STATES GREFFE

STATES OWNED OR CONTROLLED COMPANIES: RIGHTS AND
RESPONSIBILITIES (P.100/2014) – AMENDMENT

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After paragraph (b) insert a new paragraph as follows –

- “(c) to request the Minister for Treasury and Resources, on behalf of the panel referred to in paragraph (a), to present the draft Strategic Plan of each company to the States for debate at an interval of not less than every three years and to present the Business Plan of each Company to the States annually with any subsequent amendments being approved by the ministerial panel.”

DEPUTY R.G. LE HÉRISSIER OF ST. SAVIOUR

REPORT

I fully support Deputy G.C.L. Baudains of St. Clement in his efforts to tighten oversight over States owned companies and utilities. The shift to such entities was made for laudable reasons, like the need to give them more flexibility, particularly in operational matters. In the case of Andium, the new Housing Authority, an important reason was the fact that such a structure enabled it to raise funds on the capital markets.

However, I doubt if it was the intention of the States to allow such bodies to operate with total independence, with the States' shareholder, the Minister for Treasury and Resources, only intervening in the most exceptional circumstances. His understandable wish not to get dragged into micro-management has sometimes led to the perception of a total hands-off approach. However, there have been paradoxical interventions, such as the active role played by the Minister and the Treasury in obtaining finance for the Gigabit project.

Latterly, and in the light of the problems with the new JT billing system, the Minister has announced in the States that he will become an "activist" shareholder.

As with Planning I, like Deputy Baudains, am very concerned at the concentration of power in one person and the heavy, almost impossible, responsibility placed upon such Ministers to be the interpreters and protectors of the public interest.

Background

There appear to be 2 reports which have, in recent years, informed debate on how utilities should interact with the shareholder – the States.

First is the Report of the Comptroller and Auditor General, "States owned companies: accountability – Final Report of the Comptroller and Auditor General" ([R.123/2008](#)), presented to the States on 26th November 2008.

This essentially asked that the accounts of the utilities be placed before the States, albeit with some possible restrictions for part-owned bodies like Jersey Electricity and Jersey Water. The Report talks of the differences between accountability required of the then Waterfront Enterprise Board and the other utilities, but does not delve further into the different approaches required. This is tantalizing, as it quite clear that WEB's successor, the Jersey Development Company, is experiencing similar issues of accountability.

Second is the Report compiled by the Consultants, Deloitte, "States of Jersey Owned Utilities Governance Review" ([R.76/2010](#)), presented to the States on 17th June 2010 by the Minister for Treasury and Resources.

This is an in-depth piece of work which deserves more prominence, and which concluded that the preferred model of shareholder oversight was that of "Enhanced Engagement".

Essentially, this seems to require the Treasury to be involved in an ongoing dialogue around matters like the Business and Strategic Plans of the Utilities/Companies. The relevant portions of the Report are attached as an **Appendix**.

Conclusion

While it appears that the “Enhanced Engagement” model was chosen, the actual shareholder – the States – has often been left out of the loop, and a policy of “positive non-intervention” has been pursued at a political level.

I am concerned at the States becoming too involved with micro-management but, to avoid this, it is important that the Board has fully-developed antennae, so that matters like the issues with billing are picked up at an early stage and dealt with.

To strengthen political accountability, I am asking that the Strategic Plan of the Utility/Company be laid before the States at 3 yearly intervals and be subject to a debate so that the Panel, chaired by the Minister for Treasury and Resources, is fully cognisant of the views of the States on the Plan. Similarly, the Business Plan should be laid before the States annually. Obviously, there will be situations in which commercial confidentiality will prevent full publication but, for this to happen, the States will have to approve the presentation of a redacted Plan.

Financial and manpower implications

There are no additional financial or manpower implications other than the additional time required to discuss the draft Strategic Plans in the States.



Corporate Finance – Government and Infrastructure

States of Jersey Owned Utilities Governance Review Key Findings Report

10 June 2010

This Key Findings Report has been prepared on the basis of the limitations set out in the Governance Review Scope and Approach on pages 15 and 16 and the matters noted in the Important Notice over the page.

Auditor, Tax, Consulting, Corporate Finance.

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Executive summary

Overview

- The States of Jersey (the 'States') is the sole shareholder of Jersey Post International Limited ('Jersey Post') and JT Group Limited ('Jersey Telecom') and it is the majority shareholder of Jersey New Waterworks Company Limited ('Jersey Water') and The Jersey Electricity Company Limited ('Jersey Electricity') (collectively, the 'Utilities'). Jersey Electricity is listed on the London Stock Exchange.
- States of Jersey Investments Limited ('SJIL') holds the majority of the shares in Jersey Telecom and Jersey Post as a nominee for the Treasury and Resources Minister (the 'Minister'), whilst the remaining shares are held by individual States' employees with nominee agreements in place, holding them on behalf of the States and the Minister. Shares in Jersey Electricity and Jersey Water are held directly by the Minister.
- The Minister, supported by staff within the Treasury and Resources Department (the 'Treasury'), fulfils the shareholder role for the four Utilities. For the purposes of this report, the Treasury is referred to throughout as performing the shareholder function in respect of the Utilities, on behalf of the States.

Approach and methodology

- The Minister is seeking to implement a 'best practice' shareholder model which will enable the Treasury to exercise proper oversight over the States' investments in the four Utilities. Deloitte has been appointed to provide advice in respect of an appropriate shareholder model in the context of Jersey.
- A fundamental principle of good governance is that there should be a clear demarcation of roles and responsibilities whereby:
 - The Boards of the Utilities are responsible and accountable for managing the operations and delivering the strategy, consistent with the shareholders' objectives; and
 - The Treasury is responsible for shareholder governance and oversight over the Boards.
- The effectiveness of the shareholder governance arrangements, irrespective of the specific shareholder model adopted, relies on the Treasury being empowered with 'shareholder levers'. These would enable the Treasury to engage effectively with the Boards of the Utilities as an active and intelligent shareholder, holding the Boards and management teams to account for delivery of the shareholder's objectives.
- This report identifies the shareholder levers which are appropriate in the context of Jersey based on:
 - A review of the existing governance arrangements through:
 - Discussions with the Minister and the principal Treasury staff responsible for the shareholder governance arrangements;
 - A review of the existing governance documentation – Articles of Association and Memoranda of Understanding ('MOUs'); and
 - Meetings with members of the Boards of each Utility: Chairman, Chief Executive, Finance Director and a Non-Executive Director ('NED'); and
 - Drawing on global best practice in respect of corporate governance, notably the Organisation for Economic Co-operation and Development ('OECD') Guidelines and the experience of exemplar shareholder arrangements in other jurisdictions, including the UK.
- Having identified which shareholder levers are required by the Treasury, it is important to establish a functional model which provides the shareholder with a formal structure through which it can exercise the levers in the context of Jersey. In recommending a preferred model, consideration has been given to the likely resource requirement and the steps to implementation.

Executive summary

Shareholder levers

To successfully fulfil its shareholder function, it is important that the Treasury has the appropriate governance levers, whilst avoiding the risk of usurping the role of the Boards or becoming involved in the management of the Utilities. Recognising the specific context of Jersey and in line with best practice, the following shareholder governance levers are relevant:

1) Ensure adherence to the UK Corporate Governance Code: all four Utilities

- The Boards should adopt the governance standard for UK listed companies, the UK Corporate Governance Code (formerly the Combined Code on Corporate Governance). The Treasury should consider and challenge any non-compliance with the Code through active dialogue with the Utilities.

2) Participation in the appointment of the Chairman and oversight of the composition of the Board

- The Chairman's role is fundamental in setting each Utility's direction and strategy. The Treasury, should have a role in the appointment of the Chairman and in overseeing the composition of the Board, in particular, its size and the skills and experience of the Directors.

Jersey Telecom and Jersey Post: 100% owned by the Treasury

- The Treasury should be consulted by the Utilities on the proposed shortlist and the preferred candidate for Chairman, to ensure that the Minister and the Board are in agreement, in advance of the Chairman's appointment.

- The Treasury and the Chairman should agree the composition of the Board of Directors. The Utilities should consult with the Treasury prior to appointing the Chief Executive and any other new Directors to the Board and it would be appropriate for the incoming Chairman, Chief Executive, Finance Director and Non-Executive Directors to meet the Treasury before taking up their appointments, to discuss the shareholder's objectives for the Utilities.

Jersey Water and Jersey Electricity: the Treasury is the majority but not 100% shareholder

- The Utilities should consult with the Treasury during the Chairman's appointment process to ensure that the Minister is in agreement with the Board on the preferred candidate, in advance of the appointment being formalised.
- The Chairman should consult with the Treasury to ensure the shareholder's views on the composition of the Board are considered. It would be appropriate for the incoming Chairman, Chief Executive and Senior Independent Non-Executive Director to meet the Treasury on being appointed.

3) Participation in setting objectives and agreement of strategy

- One of the key shareholder levers is the participation by the Treasury in setting the objectives and agreeing the strategy of each of the Utilities. The degree of involvement by the Treasury is dependent upon the States' shareholding in each Utility.

Jersey Telecom and Jersey Post: 100% owned by the Treasury

- The Treasury, with the Boards, should set and agree the overall objectives for the Utilities on an annual basis. The shareholder's objectives should be prioritised and potential conflicts (such as social provision requirements and profit maximisation) should be identified and clarified. Examples of social policy objectives which the Utilities have identified as potentially being in conflict with their ability to maximise shareholder value and where they would benefit from clarification, are provided as an appendix to this report.

Executive summary

Shareholder levers (*continued*)

- In advance of the Annual Business Plan and longer term Strategic Plan being drafted, the Treasury should meet with each Utility to discuss and agree the Board's proposed strategy. Thereafter, the Utilities should be responsible for developing and delivering the Plans, subject to review and formal approval by the Treasury.
 - The Strategic Plan should set out clearly defined key performance indicators ("KPIs") against which performance can be measured.
- Jersey Water and Jersey Electricity: the Treasury is the majority but not 100% shareholder*
- The Treasury should engage with Jersey Water and Jersey Electricity to communicate its objectives as shareholder and to understand and challenge the strategies of those Utilities, to the extent they are inconsistent with the Treasury's objectives.
 - In accordance with best practice, the Boards would be expected to ensure equal access to corporate information for all shareholders. In addition, Jersey Electricity must avoid any breach of the UK Listing Rules.
 - Jersey Water and Jersey Electricity set the tariffs charged to customers. Unlike Jersey Telecom and Jersey Post, these Utilities do not operate under license agreements awarded by the Jersey Competition Regulatory Authority ("JCRA") and the JCRA does not regulate their prices. The Treasury currently performs a dual role of owner and quasi-regulator of those Utilities in the event the prices are challenged. These functions should be clearly delineated within the Treasury. The Treasury's ability to determine the Utilities' pricing and tariff arrangements are not shareholder levers.
 - Arguably, this dual role of shareholder and quasi-regulator could create conflict within the Treasury and consideration should be given to how this could be resolved.

4) Performance monitoring and intervention

- Good shareholder governance requires the Treasury to monitor the performance of each of the Utilities and intervene to challenge any underperformance. In extremis, where the Treasury is dissatisfied with performance and has lost confidence in the Board's response, this could lead to the shareholder seeking to replace the Chairman or Chief Executive.
- Jersey Telecom and Jersey Post: 100% owned by the Treasury*
- The Treasury should meet quarterly with the Utilities to review financial performance against their Strategic and Annual Business Plans, holding the Board to account for delivery and meeting the shareholder's objectives.
 - In so doing, the Utilities and the Treasury should agree the information to be provided to the shareholder. The shareholder should focus on reviewing the Utilities' performance at a strategic level, based on agreed KPIs and should not usurp the role of the Boards or the Executive teams.
- Jersey Water and Jersey Electricity: the Treasury is the majority but not 100% shareholder*
- Performance monitoring of these Utilities should be based around quarterly meetings to discuss emerging strategic issues and reported financial performance against earnings guidance. In assessing the performance of Jersey Electricity and Jersey Water, the Treasury should develop and agree appropriate KPIs and benchmark performance measures with the Utilities.

Executive summary

Shareholder levers (continued)

5) Consultation on remuneration of the Executive Directors: all four Utilities

- To deliver shareholder value, it is essential that the objectives of the management team are aligned with those of the shareholder. In the context of the States' shareholdings in the Utilities, this is best done by aligning the delivery of the shareholder's objectives with the Directors' remuneration and incentivisation arrangements.
- Whilst the shareholder does not have the power to reject the proposed remuneration packages, on a shareholder vote (the vote being non-binding on the Utilities), the Treasury could make clear its displeasure in the event that a remuneration package was put in place that was outside industry norms or did not properly align the shareholder's and the management team's objectives. Accordingly:
 - The Remuneration Committee of each Utility should consult with the Treasury on their remuneration strategies.
 - The remuneration packages should be clearly linked to delivery of the Strategic Plan and the shareholder's objectives, based on clearly defined KPIs.
 - The Treasury should be consulted on the remuneration packages prior to formal Board approval, to ensure the shareholder's views are considered.

6) Consultation in determining an appropriate capital structure and dividend policy: all four Utilities

- Ensuring an appropriate capital structure is a means by which a company delivers shareholder value. Surplus capital which is not required for reinvestment in the business, should be returned to shareholders by way of a share buy-back or dividend.
- The shareholder has a role to play in ensuring that the Utilities adopt an appropriate capital structure, notably in comparison to their peer groups.
- The Treasury should participate in discussions with the Utilities, challenging the Boards to demonstrate that their capital structure (level of financial leverage) is optimal, based on appropriate industry comparators.
- The Treasury should also engage with the Utilities on their annual dividend policies, challenging them to increase the payout where capital is not required for reinvestment in the business, making use of industry benchmarks, as appropriate, to support the debate with the Utilities.

7) Approval of major transactions: all four Utilities

- As owners of a business, shareholders have a role to play in approving major transactions, as it is their capital which is being invested. Accordingly, an important shareholder lever is the requirement for companies to seek shareholder approval for major transactions and those outside the normal course of business.
- The Treasury should approve any significant transactions or transactions outside the ordinary course of business, either as part of its approval of the annual Strategic Plan or by a separate business case for any additional investment opportunities identified during the year.
- In relation to Jersey Electricity, the shareholder approval threshold is set out in the UK Listing Rules, whilst in relation to the other Utilities the approval threshold should be set out in the MOU between the shareholder and the Utilities.
- Proposed investments should demonstrate delivery of shareholder value, identifying the level of investment risk and that the return on capital is appropriate.

Executive summary

Potential shareholder models

- Having identified the appropriate rights, powers and shareholder levers, consideration should be given to which model or organisational structure best enables the Treasury to exercise its levers.
- Cognisant of the Treasury's shareholder governance objectives and drawing on international exemplar shareholder arrangements for state owned entities, three shareholder governance models have been identified which have the potential to enable the Treasury to exercise its shareholder levers:
 - **Nominated Non-Executive Director:** an individual would be nominated by the Minister to serve on the Boards of each of the four Utilities as an independent Non-Executive Director.
 - **Board of Boards:** the Minister would appoint individuals to sit on a Supervisory Board which would undertake some of the key shareholder functions on behalf of the Treasury; and
 - **Enhanced engagement with a dedicated resource within the Treasury:** the resource within the Treasury which currently performs the shareholder role would be developed and enhanced to enable it to engage better with the Utilities as an effective, intelligent shareholder.
- The characteristics of the three models are outlined further within the *Recommended shareholder model* section of this report, together with detailed analysis of the relative merits and drawbacks of each model, focused on their ability to enable the Treasury to exercise its shareholder levers. The key conclusions of the analysis are set out below.
- **Nominated Non-Executive Director**
 - The appointment by the Treasury of a Nominated NED could provide benefits in ensuring that the Boards of the Utilities function properly, but this would be to the extent that they do not already do so. The model would not provide a basis for the Treasury to improve its existing shareholder governance arrangements, merely the Board governance.
 - A Nominated NED would arguably not provide any additional benefit to the Treasury than the current arrangements. A Nominated NED could not report or be accountable to the Minister. The appointee's fiduciary duties as a Director would prevent a nominated NED from promoting the Treasury's views if not believed to be in the best interests of the Utility.
 - A Nominated NED has the potential to undermine and duplicate the role and responsibilities of the Chairmen of the Utilities who meet regularly with the Minister to discuss the Utilities' strategic issues and obtain the Treasury's views.
 - As a member of the Boards of the Utilities, the Nominated NED is unlikely to provide the same degree of independent challenge to the Utilities as could typically be provided by an "outsider" such as the shareholder or equity analysis.
 - The Treasury could not delegate its shareholder governance responsibility to a Nominated NED. Under this model, the Treasury would continue to be reliant on the Boards of the Utilities and the governance they exercise, to manage the businesses in the shareholder's interests to keep it abreast of issues as they arise. To fulfil its shareholder role, the Treasury would still need to enhance its existing resource and expertise to enable the Minister to have informed discussions with the Chairman and the Nominated NED, particularly in respect of strategy and financial performance.

Executive summary

- **Board of Boards**

A Board of Boards would act as a Ministerial Advisory Board, accountable to the Minister. Such a model would be capable of delivering some but not all of the Treasury's requirements as shareholder:

- The Minister would be reliant on the Board of Boards in the same way it is currently reliant on the Boards of the Utilities. The Treasury could not delegate its responsibility to perform the shareholder role to the Board of Boards.
- To be effective and add value, the calibre of the appointees to the Board of Boards would have to be greater than the individual Boards of the Utilities. This is likely to have a high associated cost.
- There is a risk that the Board of Boards is perceived to blur the accountability of the Boards of the Utilities, undermining the role and responsibilities of the individual Boards and in particular the role of the Chairmen of the Utilities. This could lead to the existing Directors resigning or becoming demotivated and abdicating responsibility to a 'higher authority.'
- To enable the Board of Boards model to work effectively, the Treasury would need to engage in regular dialogue with the Board of Boards. It would need to exercise governance over the Board of Boards to ensure it was operating effectively and remained accountable to the Minister. This would require the Treasury to enhance its existing resource with the appropriate skills and expertise and could result in the duplication of the shareholder's role and additional cost.

- **Enhanced engagement with a dedicated resource within the Treasury**

Establishing a dedicated, professional capability within the Treasury with experience of managing investments would enhance the current level of engagement between the shareholder and the Boards of the Utilities and would meet the Treasury's requirements of:

- Implementing a formal and transparent framework for the Treasury's engagement with the Utilities, with a clear demarcation of respective roles and responsibilities;
- Retaining the accountability and independence of the Boards of the Utilities, ensuring the role of the Chairman is not undermined;
- Enabling the Treasury to be an active and intelligent shareholder, able to effectively exercise its governance levers to hold the Boards of the Utilities to account for the delivery of the Strategic Plan and the shareholder's objectives; and
- Establishing a shareholder function which creates a "buffer" between the Boards of the Utilities and the Minister, distancing the Minister from direct decision-making and reducing the risk of political interference in the day-to-day management of the Utilities.

This model does not have the drawbacks of the other two models.

It is also noteworthy that this is the model preferred by most of the Utilities, albeit they expressed concern that in enhancing the capability of its shareholder function, the Treasury should ensure that it did not seek to involve itself in the management of the Utilities' operations.

Executive summary

Conclusion – the preferred shareholder model

- Establishing a dedicated, professional capability within the Treasury is the model which would deliver the optimal shareholder governance arrangements in the context of Jersey.
- The Nominated NED and the Board of Boards models have inherent limitations in the context of Jersey. Both models would still require the Treasury to enhance its existing shareholder resource to be capable of engaging with the Nominated NED or exercising governance over the Board of Boards respectively. Otherwise there would be risk of the challenge that the Treasury had delegated its shareholder governance arrangements to the Boards.
- In establishing an enhanced shareholder function within Treasury, it should be recognised that the effectiveness of these governance arrangements would be dependent on the Treasury assembling a dedicated resource with the appropriate skills, experience and commercial expertise to be capable of performing the shareholder function and commanding the respect of both the Minister and the Boards of the Utilities.
- Although the cost of the shareholder function would be borne by the Treasury, it would be appropriate for the Treasury to consider the options available for the funding of the shareholder function, including the ability to recover the cost by levying a charge on the Utilities. In the cases of Jersey Water and Jersey Electricity, where the States is not the sole shareholder, the minority shareholders may oppose such a levy if they viewed it as being an additional dividend payable to the States. This is less likely to occur where the minority shareholders are inactive and recognise the benefit to them of the Treasury's enhanced shareholder function.

Implementation of the preferred shareholder model: Enhanced engagement with dedicated resource within the Treasury

A detailed assessment of the resource requirement and the steps to be taken to establish the enhanced shareholder function are provided in the *Implementation of the preferred model* section of this report. The key recommendations are summarised below.

Resource requirement

Enhanced engagement by the Treasury to fulfil the shareholder role would have a resource requirement comprising:

- **Senior individual – initially, near full time**
 - The individual must be capable of commanding the respect of the Minister, the Boards and the Regulator.
 - To be effective, the individual should be empowered to make decisions in relation to the States' holdings in the Utilities, referring to the Minister where appropriate.
 - This individual would require a financial and commercial background, with experience of working in the private sector and managing investments.
 - The time commitment is estimated to be four or five days per week, although once the function is established, the role may reduce to part time of one to two days per week.
- **Supporting resource – full time**
 - The senior individual would require access to a dedicated resource to support him/her, comprising either in-house staff within the Treasury, external advisers or a secondee to the Treasury.
 - The expected time requirement is likely to be full time.

Executive summary

Implementation of the preferred shareholder model: Enhanced engagement with dedicated resource within the Treasury (continued)

Cost of resource requirement

- Based on the cost of comparable resource within the Shareholder Executive in the UK, the combined direct salary costs of the enhanced resource is estimated to be in the region of £200,000 to £250,000 per annum. Depending on the level of activity of the Utilities, such as diversification into new products or markets, the shareholder function would expect to be supported by external advisers on an ad hoc basis. The budget requirement for advisers' fees is likely to be similarly in the region of £80,000 to £120,000 per annum (equivalent to £15,000 to £30,000 for each Utility).
- The cost of external advisers may be higher in the early stages of implementing the enhanced shareholder arrangements as the shareholder develops a deeper understanding of each Utility and establishes a core base of data and supporting analysis. The cost is likely to vary by Utility, depending on the Treasury's existing relationship with the Utility, the complexity of each Utility and their current performance.

Steps to implementation

- The key steps required to establish an enhanced shareholder function within the Treasury comprise:
 - Agreement of the mission, remit, accountability and budget of the shareholder function;
 - Appointment of the shareholder function: development of role descriptions, candidate interviews;
 - Consultation with the Chairmen and Boards of the Utilities: ensuring the Boards' support for the enhanced shareholder arrangements;
 - Drafting of the formal framework for engagement: MOU/Principles of Ownership;
 - Agreement of the timing of meetings and annual information requirements;
 - Implementation of an appraisal process for the shareholder function.
- The effectiveness of the enhanced shareholder function relies on the Boards of the Utilities being appropriately constituted and effective. In the first six months of the new arrangements, the Minister, with the shareholder function, should review and discuss with each of the Chairmen of the Utilities, the strength of the current Board, its composition and its operating effectiveness. Any required enhancements or revisions should be agreed and implemented.

Enhanced engagement with a dedicated resource within the Treasury

Recommended shareholder model

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Recommended shareholder model

Enhanced engagement with a dedicated resource within the Treasury

Treasury's requirement	Benefits	Drawbacks
<p>Provides a formal framework for the Treasury's engagement with a clear demarcation of roles and responsibilities between the shareholder and the Boards of the Utilities</p>	<ul style="list-style-type: none"> The model would provide a formal framework for engagement between the Treasury (via a dedicated shareholder function within the Treasury) and the Boards of the Utilities, supported by: <ul style="list-style-type: none"> Clear documentation of the respective roles and responsibilities of the shareholder and the Boards; and Regular dialogue between the Minister and the shareholder function within the Treasury. The framework would protect the independence and autonomy of the Boards, with a clear delineation of responsibilities between the shareholder role and the management of the Utilities. The model would not undermine the role of the Chairman, who would continue to meet with the Minister on a regular basis. However, the enhanced capability within the Treasury would ensure that the Minister was appropriately briefed to enable him to engage in informed discussions with the Utilities' Chairmen. Establishing individuals in post within the Treasury and formalising the framework for engagement between the Treasury and the Utilities would ensure that the shareholder function could continue to operate effectively over time, irrespective of other changes within the Treasury, such as a new Minister. A dedicated shareholder function within the Treasury would create a "buffer" between the Boards of the Utilities and the Minister. This would distance the Minister from direct decision-making and reduce the risk of political interference or exposure in the day-to-day running of the Utilities. The enhanced shareholder function provides a scalable solution, such that resource could be increased or decreased in response to any adjustments to the current portfolio of the States' owned enterprises over which the Minister takes a more active shareholder role (such as the Jersey Development Company Limited). The shareholder function would provide the Utilities with a "champion" within the Treasury to articulate the Utilities' perspectives. For example, the shareholder function could brief the Minister on any adverse impacts on the Utilities of policy initiatives or could present the case for retention of capital. 	<ul style="list-style-type: none"> The level of engagement between the Treasury and the Boards of Jersey Water and Jersey Electricity would need to be such that it enables the Boards of those Utilities to ensure equitable treatment of all shareholders. Jersey Electricity also needs to be cognisant of the UK Listing Rules. There is a risk that enhancing the shareholder function within the Treasury is perceived to increase the politicisation of the Utilities. The Treasury needs to clearly delineate its shareholder function from any policy or regulatory functions to preserve the independence of the Utilities to operate as commercial entities. Enhancing the shareholder function to ensure it has the appropriate level of resource and expertise has an associated cost, so the Treasury would need to satisfy itself that the additional expense was outweighed by the value which the enhanced shareholder function would generate. Appropriate resource to perform the shareholder function may not be available within Jersey. Any individuals recruited 'Off-Island' would need to have a good understanding of the nuances of business operating in the context of Jersey, including the Islands' political environment and culture. Recruiting individuals from outside Jersey would also provide independence and objectivity.

Recommended shareholder model

Enhanced engagement with a dedicated resource within the Treasury

Treasury's requirement	Benefits	Drawbacks
<p>Participation in the appointment of Chairman and oversight of the composition of the Board</p>	<ul style="list-style-type: none"> The Treasury's shareholder function would participate in the appointment of the Chairman and agree the composition of the Board. As appropriate, the shareholder function would also have involvement in the appointment of the Executive Directors and senior management and participate in succession planning. 	<ul style="list-style-type: none"> The Boards of the Utilities expressed concern that the Treasury's enhanced shareholder function would lead to increased bureaucracy, resulting in slower decision-making. However, having a dedicated resource within the Treasury is likely to increase the Minister's understanding of the Utilities and emerging issues, reducing the time required for decisions to be taken. The effectiveness of the model is dependent on the appropriate resource, in terms of skills and commercial expertise being recruited by the Treasury to be capable of performing the shareholder function and commanding the respect of the Minister and the Boards of the Utilities. The shareholder function would need to have sufficient industry and business expertise to perform the shareholder role. albeit it could use external advisers where necessary. The Boards of the Utilities have a role in being able to "educate" the Treasury's shareholder function in respect of its understanding of the Utilities and being able to explain their strategies.
<p>Participation in setting objectives and agreement of strategy</p>	<ul style="list-style-type: none"> A dedicated shareholder function within the Treasury would enable it to better understand the Utilities' businesses and to be an informed and active shareholder. The Treasury's shareholder function would meet with each Utility to: <ul style="list-style-type: none"> Communicate the Treasury's objectives and requirements; Discuss and agree the Utility's strategy; Review and challenge the Strategic Plan; and Agree appropriate performance measures (KPIs). The Treasury's discussions with Jersey Water and Jersey Electricity, in contrast to discussions with its 100% owned operations, Jersey Telecom and Jersey Post, would recognise their respective limitations on disclosure. The Treasury's shareholder function would provide an independent, objective challenge to the Boards and ensure the Boards were responsive to the Treasury's views. The shareholder function would ensure the Minister was aware of issues arising, briefed in advance of discussions with the Utilities' Chairmen and able to make informed decisions, on a timely basis. 	

Recommended shareholder model

Enhanced engagement with a dedicated resource within the Treasury

Treasury's requirement	Benefits	Drawbacks
Performance monitoring	<ul style="list-style-type: none"> The Treasury's shareholder function would provide an independent review of the Utility's ability to deliver the Strategic Plan and the Treasury's objectives. Arguably, the Treasury is currently reliant on the Boards to perform this function. Having a dedicated capability within the Treasury would enhance the Treasury's ability to hold the Board to account and increase the shareholder oversight over the Boards and management teams of the Utilities. The shareholder should focus on the Utilities strategy, performance and risk management (i.e. equivalent to the role of an equity analyst in the private sector). The shareholder function would keep the Minister abreast of emerging issues. 	
Consultation on remuneration of the Executive Directors	<ul style="list-style-type: none"> The Treasury's shareholder function would engage with the Remuneration Committees of the Utilities to ensure appropriate levels of remuneration and incentive arrangements were set for the Executive Directors. 	
Consultation in determining an appropriate capital structure and dividend policy	<ul style="list-style-type: none"> The shareholder function would challenge the Executive Directors and management team to demonstrate that the Utility's capital structure and dividend policy were appropriate. The shareholder function would represent the Treasury's requirements, such as dividend expectations. It would mediate in resolving any conflict between the objectives of the Treasury and the long term interests of the Utilities. 	
Approval of major transactions	<ul style="list-style-type: none"> The shareholder function would be capable of understanding and assessing the benefits of any proposed transactions by the Utilities. It would be able to represent the Treasury's views and ensure the expected risk level was appropriate. 	

Recommended shareholder model

Enhanced engagement with a dedicated resource within the Treasury

Conclusion

Establishing a dedicated capability within the Treasury and enhancing the current level of engagement between the shareholder and the Boards of the Utilities would meet the Treasury's requirements of:

- Implementing a formal and transparent framework for the Treasury's engagement with the Utilities, with a clear demarcation of roles and responsibilities;
- Retaining the accountability and independence of the Boards of the Utilities, ensuring the role of the Chairman is not undermined;
- Enabling the Treasury to be an active and intelligent shareholder, able to effectively exercise the shareholder governance levers it requires to hold the Boards of the Utilities to account for the delivery of Strategic Plan and the shareholder's objectives; and
- Establishing a shareholder model which creates a "buffer" between the Boards of the Utilities and the Minister, distancing the Minister from direct decision-making and reducing the risk of political interference in the day-to-day management of the Utilities.

This model does not have the drawbacks of the Nominated NED or the Board of Boards models.

The effectiveness of this model is dependent on the appropriate, dedicated, professional resource, in terms of skills, experience and commercial expertise being assembled within the Treasury, capable of performing the shareholder function and commanding the respect of both the Minister and the Boards of the Utilities.

The Treasury would bear this cost and would need to satisfy itself that the additional expense was outweighed by the value which an enhanced shareholder function would deliver. It would be appropriate for the Treasury to consider the options available for the funding of the shareholder function, including the ability to recover the cost by levying a charge on the Utilities. In the case of Jersey Water and Jersey Electricity where the States is not the sole shareholder, the minority shareholders may oppose such a levy if they viewed it as being an additional dividend payable to the States. This is less likely to occur where the minority shareholders are inactive and recognise the benefit to them of the Treasury's enhanced shareholder function.

The model is scalable, enabling the Treasury to increase or reduce the resource and time commitment of the shareholder function in response to any changes in its engagement with other States' owned enterprises.

The implementation of the preferred shareholder model is considered in more detail in the following section of this report.

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Implementation of the preferred model

Enhanced engagement

To fulfil its role as an effective shareholder, exercising shareholder governance in line with best practice, the Treasury should enhance the level of engagement with each of the Utilities, holding regular meetings with relevant members of the Board and management teams of each Utility.

Whilst the listed status of Jersey Electricity and the fact that Jersey Water has other shareholders will place certain restrictions on the timing of the discussions between the Treasury and those Utilities and to a degree, the level of disclosure permissible, the principle of increased dialogue between the shareholder and the Utilities is similar to those where the States is the sole shareholder.

The shareholder function should focus on communicating the Treasury's shareholder objectives to each of the Utilities and on holding the Utilities to account for the delivery of their strategy, avoiding any tendency to replicate the role of the Executive and the Board in managing the business or reviewing the financial performance in detail.

Under the 'enhanced engagement' model, a series of set piece meetings is envisaged, supported by ad hoc ongoing dialogue between the Treasury and the Executive Directors of the Utilities and the Chairmen of the Remuneration and Nomination Committees, such as:

- **Objective setting meetings to discuss strategy**
 - Communication of the Treasury's objectives for the Utilities and its specific requirements;
 - Discussion of the Utility's strategy, prior to development of the Annual and longer term Strategic Plans by the Utilities; and
 - Review and discussion of the Strategic Plan¹, following approval by the Boards.
- **Quarterly meetings with the Utilities**
 - Discussion of most recent quarterly performance against Plan, with explanation of significant variances; and
 - Review of the outlook and discussion of any material changes to the strategy.
- **Ongoing dialogue, outside of the set-piece meetings**
 - Engagement with the Utilities during the year to discuss ad hoc matters such as: Board appointments, remuneration, proposed major transactions, capital structure and dividend policy.
- **Pre-meeting preparator/ Ministerial briefings**
 - The Treasury's attendee(s) at the meetings with the Utilities would need to allocate additional time for:
 - i. Meeting preparation, including a review of the information provided by the Utilities;
 - ii. Keeping themselves informed of industry and market developments relevant to each of the Utilities; and
 - iii. Regular Ministerial briefings to keep the Minister abreast of the Utilities' performance and any issues arising.

Notes:

¹ To ensure best practice regarding the equitable treatment of minority shareholders and to avoid Jersey Electricity being in breach of the UK Listing Rules, Jersey Water and Jersey Electricity would not be expected to provide a copy of their Strategic and Annual Business Plans to the Treasury, but would provide sufficient forward looking information to enable the Treasury to be able to understand the strategy of the two businesses and hold the Boards to account for delivery of the strategies.

Implementation of the preferred model

Resource requirement

To enhance the shareholder engagement with the Utilities, the Treasury requires a dedicated shareholder function. To be effective, it would need to be empowered and capable of discussing issues on behalf of the shareholder, commanding the respect of the Chairman, Chief Executive, other Board Directors and the Regulator and able to discuss and challenge the Utilities' strategies and performance. Equally, it would need to be capable of advising and briefing the Minister ahead of the shareholder meetings and providing advice to the Minister on matters such as Board appointments, Directors' remuneration, appropriate capital structures and dividend policy. Where necessary, in the event of underperformance by one of the Utilities, the shareholder function would be responsible for providing advice to the Minister on how the shareholder should intervene.

The Treasury would need sufficient resource to enable it to fulfil this role. On the assumption that the remit of the shareholder function, at least initially, would be limited to exercising governance over the four Utilities, the resource requirement is likely to comprise:

- **Senior individual – initially, near full time**
 - A senior individual, capable of commanding the respect of the Minister and the Boards of the Utilities and the Regulator. The individual would need to be viewed by the Utilities as capable of discussing strategy, performance, Board appointments and other issues on behalf of the Minister.
 - This individual would require a financial background with experience of working in the private sector at Board level.
 - The Minister would need to delegate the appropriate level of authority to this individual to empower him/her to be effective in the role and be capable of making day-to-day decisions on behalf of the Minister, referring to him where appropriate.
 - The expected time commitment for this individual is likely to be four to five days per week, although once the shareholder function is established, the role may reduce to part time, of one to two days per week. During the 'set up' phase, as the Treasury introduces its enhanced shareholder governance model, the time commitment to secure the Utilities' buy-in to the revised governance arrangements should not be underestimated. The success of the model will be dependent on the Utility Board's acceptance of the arrangements and their willingness to engage with the shareholder function: this is best achieved through the development of mutual respect.
- **Supporting resource – full time**
 - The senior individual would require access to a dedicated resource to support his/her role. This could comprise or be a combination of:
 - i. In-house resource within the Treasury; or
 - ii. External advisers, such as one of the accounting firms, banks or fund managers; or
 - iii. A seconded within the Treasury, such as could be provided by an accounting firm, bank or fund manager.
 - The expected time requirement of this individual is likely to be full time.

This model is scalable in the event that the Treasury wishes to increase the engagement remit of its shareholder function to include other States' owned entities.

Based on the cost of comparable resource within the Shareholder Executive in the UK, the combined direct salary costs of the enhanced resource is estimated to be in the region of £200,000 to £250,000 per annum. Depending on the level of activity of the Utilities, such as diversification into new products and markets, the shareholder function would expect to be supported by external advisers on an ad hoc basis. The budget requirement for advisers' fees is likely to be in the region of £50,000 to £120,000 per annum, equivalent to £15,000 to £30,000 for each Utility.

The cost of external advisers may be higher in the early stages of implementing the enhanced shareholder arrangements as the shareholder develops its understanding of each Utility and establishes a core base of data and supporting analysis. The cost is likely to vary by Utility, depending on the Treasury's existing relationship with the Utility, the complexity of each Utility and their current performance.

Implementation of the preferred model

Steps to implementation

A high level summary of the key steps which the Treasury would need to take to implement the preferred shareholder model is provided below.

- **Agreement of the remit of the enhanced shareholder function**
 - At the outset, it will be important for the Minister and the Treasury to agree the mission, remit, reporting lines and accountability of the shareholder function. In addition, agreement would need to be reached on how the function is funded and the budget for the enhanced shareholder capability. Whilst the Minister would remain the shareholder, the senior individual responsible for leading the shareholder function would be a senior member of the Treasury team with a wide remit to develop the shareholder role and able to speak on behalf of the Minister.
- **Appointment of the enhanced shareholder function**
 - Appointment of the appropriate individual(s) to fulfil the shareholder function within the Treasury which is likely to comprise a senior and a junior individual. This would require the development and documentation of role descriptions, use of recruitment consultants, candidate interviews, etc.
- **Consultation with the Utilities**
 - A consultation process would need to be undertaken between the Treasury and the Boards of the Utilities to explain how shareholder governance will be undertaken in future and to secure the Boards' buy in' and support for the new arrangements.
 - Fundamental to the success of the model will be to explain the implications and benefits of the enhanced shareholder function to the Utilities, including an outline of the respective roles of the Treasury and the Boards of the Utilities and the framework for engagement. It is essential that the enhanced dialogue between the shareholder and the Utilities is not seen as an additional layer of bureaucracy.
- **Implementation**
 - The shareholder function would be responsible for putting in place a formalised framework for the Treasury's engagement with the Utilities. This could take the form of an MOU or Principles of Ownership which sets out what the Treasury expects of the Utilities as shareholder and what the Utilities should expect from the Treasury.
 - MOUs already exist to govern the Treasury's relationship with Jersey Telecom and Jersey Post. These documents would need to be updated to reflect the enhanced governance arrangements. MOUs do not currently exist between the Treasury and Jersey Water or Jersey Electricity and would need to be drafted, reflecting the fact that the States is not the sole shareholder of those Utilities.
 - The MOU/Principles of Ownership would set out the governance arrangements and a clear and comprehensive description of the rights and levers the Treasury would hold and the basis by which they will be exercised. The Treasury should ensure the Utilities' compliance with the MOU/Principles of Ownership which should be capable of being amended to reflect evolving best practice in corporate governance. A summary of the key components which would be expected to be included in the MOU/Principles of Ownership is provided as an appendix to this report.

Implementation of the preferred model

- **Implementation (continued)**
 - The Treasury shareholder function should agree with the Boards:
 - i. The timing of the annual strategic and quarterly review meetings between the Treasury and the Utilities. The quarterly performance meetings would be expected to occur immediately following the Board approval of quarterly results in the case of Jersey Telecom and Jersey Post and immediately following publication of the quarterly results in the case of Jersey Water and Jersey Electricity. The annual objective-setting and strategy meetings should be held in advance of the Utilities developing the Strategic and Annual Business Plans; and
 - ii. The Treasury's annual information requirements from each Utility – expected to include items such as the annual and longer term Strategic Plans or forward-looking statements and quarterly financial results. Examples of the information requirements which the Treasury is expected to require (to be specified in the MOU/Principles of Ownership) is provided as an appendix to this report. Typically, the shareholder's information requests should be information and analysis which the Utilities management teams prepare as a matter of course, including benchmarking of its financial performance, KPIs and capital structure.
 - One of the key premises that supports the effective operation of the enhanced shareholder function as a means of exercising good governance over the Utilities, is the assumption that the Board of each of the Utilities is appropriately constituted and effective. Accordingly, in the first six months of the new arrangements, it will be important for the Minister, in conjunction with the Treasury's enhanced shareholder function, to review and discuss with the Chairman of each of the Utilities, the strength of the current Board composition and their operating effectiveness as a means of:
 - i. Establishing the vision, mission and values of the Utilities;
 - ii. Setting their strategy and organisational structure;
 - iii. Delegating authority to the management teams to deliver the strategy; and
 - iv. Exercising accountability to shareholders and responsibility to relevant stakeholders.
 - To the extent that there is a need for enhanced or revised arrangements, these should be agreed and an outline timetable for their implementation should be established
 - It would also be appropriate for the Treasury to put in place an appraisal process for assessing the effectiveness of the shareholder function. This need not be elaborate but is likely to provide important feedback to assist in the development of the shareholder function.