

The 2009 code of practice for governance of state bodies

Imelda Reynolds assesses the impact of the new code

On June 15 2009, the Department of Finance published an updated *Code of Practice for the Governance of State Bodies*. The updated code more clearly defines the role and responsibilities of board members of statutory authorities and imposes additional compliance and reporting obligations on them.

As far back as 2002, the *Mullarkey Report of the Working Group on the Accountability of Secretaries General and Accounting Officers* highlighted the need for clarity in relation to responsibility and accountability in both existing and new State entities.

More recently, the OECD's 2008 *Public Management Review – Towards an Integrated Public Service*, addressed the relationship between Irish agencies, semi-state bodies and parent departments and stated, "the lines of accountability need to exist in which all key actors know to whom they are responsible, and for what".

Taking up this issue, the November 2008 *Report of the Taskforce on the Public Service* recommended the development of a new governance framework to improve efficiencies and effectiveness in state agencies, while clarifying the respective role and function of departments and agencies in policy making and strategic direction. The Government's response to the taskforce report committed to a review of existing agencies and to the introduction of new governance and performance frameworks that would, amongst other things, clarify the role of boards of agencies.

It is against this background that, on June 15 2009, the Department of Finance issued a welcome update to the *2001 Code of Practice for the Governance of State Bodies* ('the 2001 Code'). The updated code represents a new blueprint against which the performance of state bodies will be measured. In developing the new code, the Government clearly noted the OECD recommendations and also took into account other guidance, such as that available from the UK's Financial Reporting Council, and the UK's Independent Commission on Good Governance in Public Service's '*Good Governance Standards for Public Services*'. The result is a Code of Practice which brings some welcome clarity to the functions and responsibilities of board members of state bodies.

Legal structure of state bodies

In general, state bodies have been created in two ways. Some are companies registered under the Companies Acts 1963 to 2006. For



Imelda Reynolds

such bodies, board members are 'directors' within the meaning of the Companies Acts. As such, they are subject to the legal and fiduciary obligations imposed on company directors by statute and at common law.

A far greater number are bodies corporate incorporated by statute. This means they do not have to observe the provisions of the Companies Acts. It is the board members of these entities who, up to now, lacked definition as to their role and responsibilities. These individuals are not directors within the meaning of the Companies Acts, so the legal obligations imposed on registered company directors do not apply to them. The 2009 *Code of Practice for the Governance of State Bodies* ("the Code") goes some way towards answering the questions as to what responsibilities do apply.

Of course, the code's provisions do not apply only to such boards and board members. The code is equally applicable to registered company directors of state bodies. The code specifically provides that it does not override existing statutory requirements and other obligations imposed by the Companies Acts, by ethics legislation, by Standards in Public Office legislation, by the specific statutory provisions relating to the state body itself, or any other relevant legislation such as equality legislation and employment legislation.

Statutory framework

In seeking to understand the legal responsibilities of the board members of state bodies, the logical starting point is the relevant enabling legislation. The code requires each state body to be clear about its mandate, and from that, to identify the various functions, roles and responsibilities

entailed in the delivery of that mandate.

Legal structures of statutory bodies differ - some may have a board, and look to all intents and purposes like limited liability companies. Others may have no board at all.

The code recognises that state bodies may be constituted in different forms, and that the provisions of the code may need to be adapted. In particular, referring to bodies constituted with an individual office holder as a tribunal, or as a commission, the code says the relevant body should reach agreement with the parent department on the extent to which the code might be adapted. It goes on to say that this agreement must be noted in the state body's annual report, which should explain whether the requirements are to be phased in over a longer period of time or otherwise varied. It is clearly envisaged that such agreements will be the exception rather than the rule and that where compliance is not the norm, there will be transparency as to why this is so. The Department of Finance is to be advised about any such proposed statement in advance of publication of the report.

The board

For those state bodies with a board, the code, as an overriding principle, specifies that the board is, "...collectively responsible for promoting the success of the state body by leading and directing the board's activities. It should provide strategic guidance.... and monitor the activities and effectiveness of management. Board members should act on a fully informed basis, in good faith, with due diligence and care, and in the best interest of the State body, subject to the objectives set by Government".

These general principles are supported by more detailed requirements, many carried over from the 2001 Code. There are, however, some additional responsibilities included in this code. One is an obligation for the board to consider succession planning for the chief executive. Another is where the state body operates on a commercial basis, the Code requires the Board to report to the Minister that the business is a going concern with supporting assumptions or qualifications, as necessary. Reflecting developments in relation to 'good faith reporting' the board must put in place procedures whereby employees may, in confidence, raise concern about possible irregularities in financial reporting or other matters and for ensuring meaningful follow-up of matters raised in this way. This particular provision represents quite a material change. There are more detailed directions to the Board in relation to

the formulation of strategy. The Code also directs that the role of chairman and chief executive should not normally be combined, save with the consent of the Minister.

The Code also includes instructions regarding board composition, a subject to which much more attention is now being given, at least in relation to public companies. The board is mandated to constantly review its own operation and to identify ways of improving its effectiveness, including identifying gaps in competencies and ways these could be addressed.

Directors

The code repeats the provision included in 2001 Code requiring non-executive directors to bring independent judgment to bear on issues of strategy, performance, resources, key appointments and standards of conduct.

As a principle, it also states that “All directors should..... regularly update and refresh their skills and knowledge”. This is a principle contained in the UK Financial Reporting Council’s Combined Code on Corporate Governance of June 2008 and its inclusion in this code is a signal to directors of the importance of maintaining high standards.

The board is also required to keep the performance of individual directors under review – this particular requirement may well bring new challenges to the chairs of many state bodies. The attendance record of each board member at board meetings is also to be reported in the annual report.

In addition, in an acknowledgement of the distinction applicable to directors of registered companies, the Code specifically refers to directors’ duties under the Acts and the responsibility of such directors to act in conformity with the applicable provisions of the Acts.

The requirement for a state body to have a written ‘Code of Business Conduct’ exists under the 2001 Code. These codes of conduct are to be amended to include a recommendation that where potential for conflict of interest arises acceptance of further employment by directors and staff should be avoided for a reasonable period after employment ceases where potential for conflict of interest arises. The code also elaborates in some detail on the obligations of board members and persons holding a “Designated Position of employment” in a state body in relation to obligations pursuant to the Ethics in Public Office 1995 and the Standards in Public Office Act 2001.

In terms of disclosure of interests, the provisions of the 2001 Code still apply and the guideline financial thresholds have not changed – disclosure is required in respect of shareholdings valued above €15,000 or more than 5 per cent of the issued share capital of a company.

An interesting new requirement is that directors should not retain documentation obtained during their term as directors – they

should return it to the secretary or else indicate that all such documents have been disposed of in an appropriate manner. If board papers are later required, the Code states that this can be facilitated by the board secretary.

The Code makes no material changes concerning fees payable to board members, but the Chairman is, as part of his annual report to the relevant Minister, required to affirm that the July 1992 Guidelines covering payment of fees to Chairpersons and Directors/Members of State Bodies are being complied with, in relation to both the main board and any subsidiary boards. The annual report is also to include a schedule of fees and details of aggregate expenses paid to each of the directors, broken down by category.

Risk management

The Code introduces new obligations on board members concerning risk management. Each State body is required to develop a risk management policy. The board must approve the framework and monitor its effectiveness. It also has to review material risk incidents and note or approve management’s actions, as appropriate. The Code goes into some detail as to the key elements included in the Board’s oversight of risk management.

Audit committee

In relation to the audit committee, the Code clarifies that only those state bodies with more than 20 employees must have an audit committee made up of at least three independent non-executive directors. Reflecting the requirements of the Combined Code, at least one member of the committee has to have ‘recent and relevant financial experience’. The audit committee is also mandated to review the effectiveness of the State body’s internal audit activities and the Code specifies that any internal audit/audit items that relate to the Board’s areas of responsibilities should be communicated to the board as soon as they are identified.

Relations with the Oireachtas and the Minister

There are significant new responsibilities under this heading. Taking on board the OECD’s recommendations, the Code envisages the development of ‘*Performance Frameworks*’ through dialogue between the state body and the department. These will define both parties’ expectations, clarify the State body’s role in the public sector and define parameters surrounding resources and income. The development of the performance frameworks will include agreement on annual and multi-annual targets and the development and use of service level agreements.

Matters to be covered in the Chairman’s annual report and accounts have been extended to include (in circumstances where there has been a breach of internal financial

controls) an outline of the steps that will be taken to guard against such a breach occurring in future. In addition, reflecting one of the recommendations in the Report of the Committee of Public Accounts concerning the FAS 2007 Accounts, the Chairman is required to certify that Government travel policy requirements are being complied with in all respects. The Code incorporates a Framework Travel Policy and requires compliance both with it and with Department of Finance circulars issued from time to time. The Framework requires a value for money approach to be taken to travel policy, including consideration being given to alternative possibilities, such as the use of video conferencing facilities.

Disposal of assets

In relation to disposal of assets, the threshold for activating the procedures regarding disposal of assets is increased from €70,000 to €150,000. Where consideration is being given to a disposal to a director or a person connected with a director, that director must absent himself from the board deliberations on the issue.

Legal disputes and procurement

The Code introduces new responsibilities regarding legal disputes involving other State bodies. Where there are such disputes, every effort should be made to resolve them before expensive legal costs are incurred. State bodies are also asked to provide a list of such legal issues to the Department of Finance together with an estimate of the legal costs incurred. Regarding procurement, there is considerable detail given on procedures to be followed.

Conclusion

Publication of the Code has thrown more light on the legal responsibilities of boards and board members of state bodies. But what sanctions apply to a board member who fails to fulfil these more onerous responsibilities? Legislation establishing a state body will typically provide that the relevant Minister may remove a member where he becomes incapable due to ill-health, or for ‘stated misbehaviour’. Will failure to comply with, or live up to the standards imposed by the Code now amount to stated misbehaviour? It remains to be seen.

This enhanced focus on the responsibilities of board members of state bodies is welcome. The Code goes some way towards giving such directors greater clarity in terms of their roles and responsibilities and, indeed, their accountability. The attention focused on this area, and the guidance in the Code should enable state bodies and their directors enhance performance in these challenging times.

Imelda Reynolds is a partner at Beauchamps Solicitors.

When do changes to an existing public contract trigger an obligation to re-advertise?

Sarah Johnson discusses a recent case which offers guidelines on the effect of changes to an existing public contract

The question of exactly when changes to the terms of a contract trigger an obligation to re-tender is a thorny one from a public procurement perspective, and one in relation to which there was little guidance up until recently. However, the decision of the European Court of Justice (ECJ) last year in the landmark *Pressetext* case (Case C-454/06), gave valuable guidance on the principles applying in such situations. The judgment is also interesting in that it demonstrates how these principles should be applied in practice.

Background

In 1994, the Austrian Government entered an agreement with the Austrian Press Agency (APA) for the provision of certain press agency services. The agreement was for an indefinite period and contained a clause by which the parties waived the right to terminate the agreement before December 1999.

In September 2000, APA transferred the operation of one element of the service to a wholly-owned subsidiary. APA gave assurances to the Austrian authorities that, following the transfer, APA was jointly and severally liable with the subsidiary, and that there would be no change in the overall service performed.

The pricing and indexation clauses of the agreement were amended in 2001 to take account of the introduction of the Euro. Simultaneously, minor price adjustments were made so that the prices could be expressed in round figures. In 2005, there were two further amendments: the waiver of the right to terminate was extended to December 2008, and the discount given on a price for certain on-line inquiries was increased from 15 per cent to 25 per cent.

In 2006, *Pressetext*, an unsuccessful tenderer, took action in the Austrian courts claiming that the restructuring of APA and the subsequent amendments made in 2001 and 2005 constituted new 'awards' and should have been re-tendered. The Austrian court suspended the case and referred the matter to the ECJ.



Sarah Johnson

When does an amendment give rise to a new award?

The ECJ firstly emphasised that the principal objective of the Community rules on procurement is to ensure the free movement of services and the opening up of competition throughout the EU. The principles of non-discrimination on grounds of nationality, equal treatment and transparency are applied in order to achieve this objective.

It ruled that amendments to the provisions of a public contract constitute a new award of a contract when they are "materially different in character" from the original contract and,

'The Pressetext judgment provides us with clear guidance as to when an amendment to an existing public contract may be found to give rise to a new award.'

therefore, are such as to show the intention of the parties to re-negotiate the essential terms of that contract.

The court then took the opportunity to identify three situations where an amendment would be regarded as "material" namely:-

- when the contracting authority introduces conditions which, had they been there originally, would have allowed for the admission of tenderers other than those originally admitted or would have allowed for the acceptance of a tender other than the one accepted;
- when the amendment considerably extends the scope of the contract to include services not originally covered; and
- when the amendment changes the economic balance of the contract in favour of the contractor in a manner which was not provided for in the original agreement.

It is instructive to consider in detail how the court treated the particular changes subject to challenge in this case, in order to understand how these principles are applied in practice.

• The change to the identity of the service provider

On the facts, the ECJ found that the arrangement whereby APA's subsidiary would now perform the services was simply an internal re-organisation of the contractor and did not fundamentally modify the terms of the original contract. It was noted that, in this case, the company to which the contract was transferred was a wholly owned subsidiary of APA, was integrated financially, organisationally and economically within APA, and was required to manage its business on the basis of instructions from APA.

The ECJ clarified that a new contract is not awarded in a situation where: (1) the sole shareholder in the new service provider is the original service provider, (2) the original service provider controls the new provider and gives it instructions, and (3) the original service provider continues to assume responsibility for compliance with the contractual obligations.

• Euro conversion

As regards the price amendments, the