

Model Shareholder Expectation Letter

Strictly Private and Confidential

SAMPLE LETTER TO COMMERCIAL SEMISTATE BODY FOR CORPORATE GOVERNANCE COMPLIANCE AND SHAREHOLDER EXPECTATIONS

[On Letterhead of Relevant Line Minister]

Note: This is an illustrative example of a shareholder expectation letter setting out what typically should be included. Please note that the shareholder expectation letter should be tailored to meet the particular circumstance of the commercial State body.

[Date]

Intended Recipient:

Dear []

Introduction

The Minister for Public Expenditure and Reform and I have given consideration to the way in which Government objectives for [insert name of entity] are formulated and shared with the Board of Directors (the “Board”). Arising from that consideration, we are now proposing a more structured approach to confirming Government's objectives for [insert name of entity] over the short and medium term with a view to assisting the Board in its operations and in complying with its obligations under the prevailing governance framework.

This letter is intended to provide guidance to the Board with respect to Government's current objectives for [insert name of entity] and the primary considerations which will be taken into account in respect of matters for which consent may be required under legislation, [the entities Constitution] and/or the Code of Practice for the Governance of State bodies (the “Code”). We believe that this letter will be helpful to the Board, particularly in its corporate and strategic planning processes, and it is our intention that we would in future issue a similar letter on an annual basis.

The specific objectives outlined in this letter should be considered in the context of the Government's overall policy objectives for [insert name of entity], namely that:

- [Insert name of entity] should continue to deliver on its corporate strategy, [including]

- [\[Insert name of entity\]](#) should maintain financial policies and a capital structure, taking account of future obligations (including pensions), that facilitate the payment of dividends to the Shareholder(s).

1. Dividends

It is our view that a new Dividend Policy, tailored to the specific circumstances of each commercial semi state body, should apply in the commercial state sector, with a view to facilitating management in prioritising objectives and providing greater clarity on dividend payments over the medium term. We therefore request that the Board of [\[insert name of entity\]](#) would now develop a new formal dividend policy for [\[insert name of entity\]](#), which would take into consideration the following principles:

- a) an appropriate balance should be struck between payment of dividends and reinvestment in the business; in this context it is the strong objective that a robust medium term framework for the calculation of dividends be put in place which will reflect the imperative that [\[insert name of entity\]](#) remain strong financially and in a position to invest commercially whilst also delivering an appropriate return to the Shareholder(s);
- b) the policy and its implementation should ultimately be comparable with peer companies within a period of 5 years, taking into account structural, ownership, regional and other relevant differences; and
- c) the policy should also be related to an agreed proportion of cash flow as well as net profit after tax (NPAT).

In this regard, it is proposed that a list of appropriate peer companies be agreed between our respective Departments and the Board. A suggested list of peer companies is set out in Appendix II.

As indicated above, the objective of formulating a new dividend policy is to assist the Board by bringing clarity to the Government's objectives as regards future dividend payments over the medium term, thereby avoiding the uncertainty created by special dividends potentially being requested from time to time. It may still be necessary or appropriate for special dividends to be paid from time to time (e.g. in event of sales of assets, windfall gains, etc). However, to the extent that any special dividend is paid, it is our expectation that the likely impact of such payment on the policy would be reviewed at the time. We also believe that greater certainty on dividend policy will assist in enabling informed decisions to be made on financial management and investment, while providing an appropriate, regular and predictable return to the Shareholder.

We ask that you engage with the Departments with a view to developing an appropriate new dividend policy, with a target of having this finalised no later than [deadline].

2. Return on Capital

A key focus for the Shareholder(s) in the commercial state companies is the return generated on capital invested. We propose to augment our monitoring and measurement of [insert name of entity] investment returns and in this regard Appendix 1 includes financial performance measures in respect of profitability and investment return which we propose to use to assess company performance. While acknowledging that returns will vary from year to year, sometimes due to temporary or non-controllable factors, it is, however, a key Government objective that [insert name of entity] delivers investment returns over the relevant period that are in line with peer companies, while also having regard to the cost of capital.

This proposed approach to developing a perspective on shareholder return will be reviewed on an on-going basis and may be adapted as necessary.

3. Sectoral Policy Objectives

In addition to the overall policy objectives of [insert name of entity] listed above, we wish to ensure that [insert name of entity] continues to work actively to support general Government policy in the XXX sector [including] This will require an appropriate level of on-going investment by [insert name of entity], with care being taken to ensure that core areas of activity are prioritised within the resources available to the company for reinvestment.

4. Governance Arrangements

Corporate Plan

The Code of Practice for the Governance of State bodies (the "Code") sets out the governance framework for the internal management, and the internal and external reporting relationships of commercial and non-commercial State bodies. As you know, the Code requires State bodies to prepare a rolling 5-year corporate plan, which should be submitted to the relevant parent Department within six months of the year end. We would propose to engage with you early on in the process of preparing/updating this corporate plan, in order that we can provide feedback to you on the plan in a timely fashion.

Remuneration and Superannuation

The Remuneration and Superannuation Annex, appended to the Code, outlines the requirements which must be met By State bodies under this heading. In particular, this document now includes revised approval requirements in relation to severance schemes and pension scheme proposals¹. These should be read in conjunction with circular 16 of 2021.

¹ Paragraphs 1.7 and 2.23 refer.

You should ensure that all necessary governance steps are taken to comply fully with these new requirement as well as with all of the other provisions contained in the Remuneration and Superannuation Annex.

Reporting

The Business and Financial Reporting Requirements document, appended to the Code, sets out the reporting requirements to which State bodies should adhere, including the provision of interim and final financial statements. We would propose to enhance the existing reporting arrangements by introducing regular three-monthly review meetings between [insert name of entity] and the Departments, to review progress in relation to the financial performance measures referred to above (as set out in Appendix I) and other key performance indicators.

Board Evaluation

Consistent with the requirement in the Code, we expect that the Board constantly reviews its own operation and performance and that of its committees and individual members and that the Board undertakes an evaluation of its performance on an annual basis.

Engagement

Our expectation is that you will engage with the Department in the near term to discuss the matters set out in this letter in more detail. Please make arrangements with your usual contacts in the Department.

Yours sincerely

Minister for

Financial Performance Measures

Shareholder Return	
Measure	Calculation
Dividend Payout	(i) Dividends paid / Adjusted net profit after tax (prior year) (ii) Dividends paid / net cash flow from operating activities (iii) Dividends paid / (net cash from operating activities less capex)
Return on Equity	Adjusted net profit after tax / Average Equity
Earnings Growth	Compound Annual Growth Rate in Adjusted net profit after tax

Profitability/Efficiency	
Measure	Calculation
Return on Capital Employed (ROCE)	(i) Adjusted EBIT / Average Capital Employed (ii) Adjusted EBIT/Adjusted Average Capital Employed

Wages and Salaries	
Measure	Calculation
Average Pay	Wages & Salaries Cost / Average no. of employees
Average Pay incl. Employer Contributions	Wages & Salaries plus Employer Pension Contributions / Average no. of employees

Leverage/Solvency/Credit Metrics	
Measure	Calculation
Gearing Ratio (net)	(i) Net debt / Net debt plus equity plus minorities (ii) Net debt / Net debt plus pension liabilities plus employee related liabilities plus equity plus minorities
EBITDA Interest Cover	Adjusted EBITDA / Net Interest Payable
Interest Cover	PBIT/Net Interest Payable
FFO / Debt	Funds from Operations / Gross Debt
Financial covenant metrics	e.g Net Debt/EBITDA, others

Definitions of Key Terms used in Calculations

Term	Definition
Adjusted EBIT	Earnings before interest and tax adjusted for exceptional items and IFRS fair value movements
Adjusted EBITDA	Earnings before interest, tax, depreciation and amortisation adjusted for exceptional items and IFRS fair value movements
Adjusted Net Profit after Tax	Net profit after tax adjusted for exceptional items and IFRS fair value movements
Adjusted Capital Employed	Net debt plus equity plus pension liabilities plus employee related liabilities
Capital Employed	Net debt plus equity
Dividends Paid	Dividends paid during the financial year per the cash flow statement (excl. special dividends)
Equity	Total shareholder(s) equity taken from the balance sheet
Funds from Operations	Net cash flow from operating activities (post interest and tax paid and pre-working capital changes)
Gross Debt	Interest bearing debt such as loans, bonds and commercial paper <i>plus</i> interest bearing finance leases
Fair value adjustments	Includes unrealised fair value gains / losses on derivatives or all fair value gains / losses on derivatives where the entity does not separately identify unrealised items.
Net cash flow from operating activities	Taken directly from the cash flow statement - ensure interest paid is included
Net Debt	Interest bearing debt such as loans, bonds and commercial paper plus interest bearing finance leases less cash

List of Peer Companies

To be agreed