Indian Journal of Accounting (IJA)
ISSN : 0972-1479 (Print) 2395-6127 (Online) Vol. XLIX (2), December, 2017, pp. 121-126

THE ROLE OF CORPORATE GOVERNANCE IN MIDDLE EAST
(CORPORATE GOVERNANCE AND ETHICAL ISSUES)

Dr. Prahlad Sharma*

ABSTRACT

Now a day, around the world in corporate entities, governance has become the important focus of attention. The exercise of power over corporate entities, the legitimacy of companies and their directors, the effectiveness of governing bodies, and their accountability in the society have become crucial and critical issues. The corporate governance is expanding overwhelming and changing dramatically at very fast pace. The global economic and financial crisis is also affecting the MENA region, and threatening its capacity to attain the necessary level of economic growth in order to meet the demands of citizens in search of improved welfare, without destroying natural resources. It is clear that there is no one ideal structure for corporate governance. Many alternative structures can work well in the appropriate context. In fact, despite all the commentary on governance structure-unitary and two-tier board, the proportion of INEDs, the separation of chairman and CEO, board committees and the rest, the issue of effective governance is not really about structure but about process.

KEYWORDS: *State-Owned Enterprises, Global Economic & Financial Crisis, Shariah Rules, MENA Region.*

Introduction

Corporate Governance has been practiced for as long as there have been corporate entities. Yet the study of the important crucial subject is less than half a century old. Indeed, the phrase 'corporate governance' was randomly used until the 1980s.The 19th century saw the foundation laid for modern corporation: this was the century of the entrepreneur. The 20th century was the century of management: the phenomenal growth of management theories, management practices, management consultants, management institutions, management teaching, and management gurus, which all simultaneously reflected a pre-occupation with different styles of management. Now the 21st century promises to be the century of thinking on the subject of governance: As the focus swings to the legitimacy and the effectiveness of the wielding of power over corporate entities worldwide.

New Concepts of Corporate Governances

Overall, corporate governance continues to evolve. The metamorphosis that will determine the bounds and the structure of the subject has yet to occur. The recent financial crisis prompted by the securitization of sub-prime mortgage loans in the United State, which led to the collapse, takeover and, in some cases, nationalization of banks and other financial institutions around the world raised some fundamental corporate governance issues. There are few questions rise up in my mind:

- Where were the directors of these failed institutions, particularly the independent directors who were supposed to provide checks on overenthusiastic executives?
- Did the boards understand their firm's exposure to strategic risk?
- Will those who designed and encouraged the derivative products and securitization systems be held to account?
- Did the auditors ensure that their clients' exposure to risk was reported?
- Were any of the companies, financial institutions or financial intermediately activities illegal?

G *Assistant Professor, Parishkar College of Global Excellence, Jaipur, Rajasthan, India.*

The global economic and financial crisis is also affecting the MENA region, and threatening its capacity to attain the necessary level of economic growth in order to meet the demands of citizens in search of improved welfare, without destroying natural resources. One of the fundamental lessons to be learned from the global financial crisis is that future strategies cannot be adopted without coordinating public policies at all levels of governance, and without the participation of government, local authorities, legal advisor, civil society and the media at different levels. Around the world, in large and small corporate, in the public and the private sectors, governance has become the focus of attention. The exercise of power over corporate entities, the legitimacy of companies and their directors, the effectiveness of governing bodies, and their accountability in society have become crucial topics. Now a days the field of corporate governance is expanding and changing dramatically at very fast pace. Twenty-five years ago the phrase ‘corporate governance’ was not used in corporate sector but now, it is frequently and prominently being used in corporate world.

Corporate Governance in Middle East Region

In Middle East region, businesses are classified as having:

- Concentrated ownership, with strong family ownership of both private and listed, companies with state ownership.
- Dominant family oversight and control, with leadership from the head of the family, entrepreneurial decision making, opaque communications, and relationship based trading.
- Debt financing in which bank financing is often more than shareholders’ equity.
- Banking sector equity investment, with banks holding significant shares in companies.

The states are typically grouped together as the Middle East and North Africa (MENA). The MENA region includes:

Table 1: The MENA States

Algeria	Jordan	Iraq	Morocco	Syria
Bahrain	Kuwait	Iran	Sultanate of Oman	U.A.E.
Egypt	Lebanon	Israel	Qatar	Tunisia
Djibouti	Libya	Malta	Saudi Arabia	West Bank & Gaza

Sources: http://go.worldbank.org/

Broadly, some of these countries have relatively low GDPs and slow industrial growth. In recent years the oil producing countries, benefiting from rising oil prices, have generated large surpluses, which have been invested abroad. Banking reforms have attempted to channel some of these saving into local growth, but domestic financial markets were not so emergent. States also appreciate the need to attract foreign direct investment (FDI) and, therefore, recognize the importance of sound corporate governance. Since the capital markets are not so emergent characterized as small size therefore facing liquidity. Consequently the market does not offer opportunities to investors. Of course there are *exceptions* to such aforesaid general observations, like *Dubai & Abu Dhabi* (UAE) are making massive investment in tourism and property, whilst attempting to become an international financial centre. Recent evidence shows in UAE, ‘ Burj Khalifa’ is not a just a building, it is a global icon. As the tallest free-standing man-made structure in the world, the gleaming tower reaching to 828 meters in the sky is an example of courage and man’s ability to realize the dreams.

Dubai Declaration on Corporate Governance

The Dubai Declaration by Hawkamah’s first MENA conference in Dubai formulates a road map and key corporate governance initiatives for the region, writes Bhaskar Raj “Good corporate governance is a vital key factor in sustaining economic growth and development in the Gulf region. Policy makers are taking the lead and committing to secure significantly higher standards of corporate governance in the member countries of the GCC”. Policy makers, regulators, representatives from regional and international organisations, and business leaders from across the Middle East and North Africa, representing countries of Bahrain, Egypt, Iraq, Jordan, Kuwait, Lebanon, Morocco, Oman, Qatar, Saudi Arabia and the UAE, gathered in Dubai to jointly issue the Dubai Declaration on Corporate Governance. This was a landmark event for the region, and they agreed upon following initiatives for reforms in governance:

- The criteria of two taskforces: one focusing on the corporate governance of banks; and a second focusing on the corporate governance of State-Owned Enterprises.
- The issuance of two policy briefs: one for banks; and a second for SOEs; both to be approved by the relevant taskforces.
- The consideration of issues relating to the corporate governance of Shariah compliant banks and financial institutions and the importance of ensuring that regional corporate governance frameworks and standards are in line with international codes and the key standards, whilst at the same time remaining consistent with Shariah rules.
- The preparation of a corporate governance survey of SOEs, to be developed on a consultative basis with the cooperation of key organizations and governments.
- The recognition of a need to tackle issues surrounding insolvency and corporate restructuring.

The Hawkamah

Hawkamah, the Institute for Corporate Governance, is a regional entity whose mission is to assist countries and companies of the wider MENA region in developing sound and globally well-integrated corporate governance frameworks, policy and practices. Executive Director of Hawkamah Nasser Saidi outlined "Whilst there is still a need for raising awareness and capacity building in this field, we have made significant headway in terms of taskforces, policy briefs, addressing corporate governance in Islamic banking and finance, corporate restructuring and insolvency, family-owned enterprises and small & medium enterprises. We now move towards concrete actions and direction resulting from these principles, facilitating the design of a comprehensive roadmap for corporate governance in our region. This will enable us to achieve our ultimate goals of encouraging investment, project finance, job creation and the development of sound financial markets."

Need for Successful Corporate Governance

The values of corporate governance: transparency, accountability, and responsibility offer the key for the modernization of the countries of the Middle East and North Africa. The private sector business community can play a leading role in economic, political, and social reforms in the region. In fact, reforms led by the private sector provide the greatest promise for meeting the challenges caused by the region’s tepid economic growth and surging youth demographic. Sound corporate governance practices will attract new, much needed investment to the Middle East and North Africa because they improve their management of firms and reduce risk. National institutions, laws, regulations, and practices based on international norms and standards would enable the countries of the region to modernize their corporate sectors, enabling them to attract technology and foreign investment and become internationally competitive. It is clear that there is no one ideal structure for corporate governance. Many alternative structures can work well in the appropriate context. In fact, despite all the commentary on governance structure-unitary and two-tier board, the proportion of INEDs, the separation of chairman and CEO, board committees and the rest, the issue of effective governance is not really about structure but about process. As we have seen some of the different ways countries and cultures apply in the corporate governance, we can now identify the few thrust areas that are needed to support successful governance. These include:

- Accounting and legal professions that are internationally respected, able to discipline their members, and ensure compliance with accounting standards, and legal requirement.
- A company’s registry that facilities comprehensive disclosure, with high levels of transparency.
- Always vigilance regulatory authorities including securities and future market regulators.
- A stock market with sufficient degree of liquidity, standing on international norms and foreign and institutional investors.
- Auditing firms that are professionally managed, reliable, and independent of their clients.
- A reliable legal system including an independent judiciary, courts that are bias and corruption free, and judgments that are enforceable, free of state or other political pressures.
- Accountability fix for financial institutions, including brokers, sponsor for new issues, and financial advisors.
- Professional organizations such as director and company secretary qualifying and disciplining bodies.

- Accountability also given to educational institutions to develop education standard and train for relevant qualifications require for corporate governance.
- Consulting agencies able to advice companies and its directors.
- With the support of private and public organization, seminars, workshop to be conducted or organized on different platforms, and conclusion report to be sent to competent authority for taking decisions.
- Research institution making research on different aspects of corporate governance according to the need of region. Research publications, international conferences and professional journals play a significant contribution to the convergence of corporate governance thinking and practice.
- Formulate corporate governance codes of good practices.
- Just implementing Western rules and standards will not improve corporate governance and accounting quality in MENA region. Standards alone do not help. There need to be more disclosure on key government variables and related party transactions. They are more important than accounting. Other important changes include building the right market infrastructures and systems for companies to operate, as well as leveling the playing filed between government-owned and privately-owned firms.

Findings and Conclusion

Transparency

Corporate practices in the MENA region are often shrouded in secrecy. Many companies try to keep business and financial practices away from public knowledge and scrutiny. Whatever the perceived benefits of this strategy, opacity has its drawbacks, including reduced investment from outside sources. Traditionally, companies were also reticent to bring in outside investment for fear of losing control; however, attracting outside investment is slowly becoming more commonplace. That path is only open if potential external investors know enough about the company and can monitor its results. Investors have more confidence in companies that provide clear and accessible information, allowing them to evaluate the potential risks and rewards of their investments. With a new generation of managers in the MENA region who understand the benefits of external financing and the growth it can bring, greater transparency will become more demanded and accepted in the market. As evidenced in many of the case studies, when there has been a need for capital, companies in the region have provided the requisite information. That trend is likely to quickly become more widespread.

All publicly-listed companies are required to disclose financial results. However, a more detailed annual report is not a requirement for most companies in the MENA region. In some instances, companies disclose more than what is required in order to generate and maintain confidence in their operations or to establish trust with stakeholders. Such disclosure is an essential tool to attract and inform investors and potential partners. In smaller companies, shareholders may consist mainly of the controlling family so the annual report can also serve as a unifying communication tool. A survey conducted by Price Waterhouse Coopers of 685 institutional investors and 445 stock market analysts across 14 countries indicated that they considered an annual report more as a communications tool on the dynamics of business development than evidence of performance. The market is no longer only interested in past financial performance, but also its future direction in terms of strategy, investments, and projected growth. In this regard, anticipated future performance of a company (correctly characterized) is of key interest to investors, as their profits are largely tied to the company's strategy and execution.

The layout and information contained in an annual report can have a major impact on potential readers. Stakeholders are interested in the structure and content, including cover pages, important events that occurred during the calendar year, the layout, images, financial results, and any predictions for the future. Annual reports also allow for informal practices to be codified and communicated as a part of the ongoing development of corporate culture. Countries have different customs and norms concerning the actual make-up of an annual report. In addition, international annual report disclosure standards have surfaced as a result of the globalization of capital markets. The Organization for Economic Co-operation and Development recommends that annual reports include a discussion and analysis of company operations by management. Combining that discussion with a company's financial statements creates a powerful and transparent message. As a regional resource, the Institut Arabe des Chefs d'Entreprises in Tunisia developed a Guide for Annual Reports to provide a model for companies regarding the content and structure of annual reports. Filing management reports in conjunction with financial statements is also recommended by the International Accounting Standards Board, 36 including:

- An explanation of key financial and performance indicators,
- Statements on the company's financial position,
- Potential risk factors,
- Market and industry trends,
- Sources of capital, and
- Basic information on how risk is managed.

A company can disclose information beyond what is necessary, such as its environmental policy or corporate social responsibility initiatives. Some companies include such information in their annual reports, and others in special corporate responsibility reports.

Family-Owned Enterprise Governance

Family-run businesses have traditionally consisted of a strong family patriarch who established the business, often taking the initial form of a "one-man-show." Family members are often actively involved in establishing the board of directors, whether by actually sitting on the board themselves, or by suggesting other family members, relatives, or friends to serve as directors. If the CEO comes from the family, then boards tend to wield less power, with most of the control remaining in the family's hands. Family and other shareholders also have the ability to extend their influence in less direct ways, as a result of shares held in holding companies and/or subsidiaries. The old model of highly centralized family control functioned well when business depended heavily on relationships, which served as the glue in murky regulatory markets. It is questionable whether this system will be as valuable in the future. Increasing competition requires companies to become more strategic in how resources are allocated and brings family-owned companies into competition with global corporations. This interaction provides family businesses new opportunities to access to capital and talent. Presently family businesses typically go through **three stages of development**, which are characterized by certain features:

	Stage 1 Founder (1st generation)	**Stage 2 Next Generation (2nd generation)**	**Stage 3 Extended Family (3rd generation)**
Common Characteristics	• Business owned & managed by the founder (chairman & CEO) • Decisions made primarily by the founder with little external input • Simple and informal governance structure • Few shareholders • Board made up of family members, oftentimes also shareholders	• Management and ownership transferred to children of the founder • Governance issues become more complex as the company grows	• More family are directly or indirectly involved including children of siblings, cousins, and in-laws • Any conflicts are carried over
Typical Shareholder Issues	• Leadership transition • Succession • • Estate planning	• Maintaining teamwork and harmony • Sustaining family ownership • Leadership transition • Succession • Formalizing business processes and procedures • Establishing effective communication	• Allocation of corporate capital: dividends, debt, and profit levels • Shareholder rights • Family member employment • Shareholder liquidity • Family conflict resolution • Family participation and role • Family vision and mission • Family linkage with the business:

References

⇒ Accounting Standards Steering Committee (1975) the Corporate Report: A Discussion Paper. London: Accounting Standards Steering Committee.

⇒ Kaen, Fred R. (2003) A blueprint for corporate governance: Strategy Accountability and Preservation of shareholder value. New York: American Management Association.

⇒ Chew. Donald H. and Stuart L. Gillan (2005), corporate governance at the crossroads: A book of readings. Boston: McGraw Hill.

⇒ Batra, Sumant, Kesar Dass and Association (2008) India: National Experiences with Managing Related party transactions. Round table on corporate governance. Hong Kong: OECD

⇒ Lipton M. (2007), Some thoughts for board of directors, New York: Watchell

⇒ Lee, Thomas A. (2004). Financial Reporting and Corporate Governance. London: John Wiley.

⇒ Mallin, Chris (2006) International Handbook on Corporate Governance, London: Edward Elgar publishing.

⇒ Monks, Robert A. G. and Nell minnow (2007) Corporate Governance, 4th edn. Chichester, UK: Wiley.

⇒ Marc Goergen (2015), International Corporate Governance,

⇒ Robert lan Tricker (2009), Corporate Governance: Principles, Policies, and Practices.

⇒ Smith, Adam (1776) (1976), The Wealth of Nation (revised sdn.,) George J. Stigler (sd.), University of Chicago Press, Chicago.

⇒ Soloman, Jill (2007) Corporate Governance and Accountability. Chichester: Wiley.

⇒ Wright, Roert E. (2004) History of corporate governance: London: pickering and Chatto.

⇒ www.hawkamah.org

⇒ www.icaew.co.uk

⇒ www.acga-asia.org

⇒ www.blackwellpublishing.com/corg

⇒ www.corpgov.net/links/links.html

⇒ www.thecorporatelibrary.com

⇒ www.baacgsig.qub.ac.uk

Abbreviation Used in Paper

⇒	CEO	Chief Executive officer
⇒	CG	Corporate Governance
⇒	GCC	Gulf Cooperation Council
⇒	GDP	Gross Domestic Product
⇒	FDI	Foreign Direct Investment
⇒	INSOL	International Federation of National Associations for Accountants and lawyers
⇒	INED	An independent non-executive director
⇒	MENA	Middle East and North Africa
⇒	OECD	Organization for Economic Development and Co-operation
⇒	SOE	State Owned Enterprises
⇒	UAE	United Arab Emirates

❍☯❍