New Year's resolutions

The next 10 years will see a corporate cultural revolution in the region. **Jan Bladen** outlines his top 10 New Year's resolutions for improving corporate governance in the Middle East

Until recently, the acceptance of the concept, and the subsequent implementation of the principles of corporate governance in the Middle East has not received strong support from institutional investors and private shareholders.

And whilst there may be a variety of reasons for this, I believe that some of the principle root causes are: (a) the fact that the majority of larger organisations are either family or state-owned; (b) capital markets remain relatively underdeveloped; (c) liquidity and financing requirements were easily available from banks and; (d) a disclosure averse culture where shareholders have been reluctant to publicise operational and financial aspects of their enterprises, which has contributed to a general acceptance of the lack of transparency. Consequently, and due to the lack of transparency, the region has not been on the radar of major international investors.

With this lack of investor enthusiasm, the weight of responsibility to initiate and impel the uptake of corporate governance has, to date, rested on the shoulders of regulators in the region, with many corporate governance codes having been developed.

The challenge is no longer the development of codes but their effective implementation, which will not occur until (a) regulators are given teeth (like the Dubai Financial Services Authority) and (b) corporations recognise and understand the real benefits that corporate governance brings to an enterprise and its shareholders.

Call me a sceptic, but this will only happen when shareholders realise that this generally means a better run organisation and higher returns. Until then, regulators' capacity to monitor and enforce breaches of their corporate governance codes will continue to be tested.

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New Year's Eve has always been a time for reflection and looking forward to the next year. If I had the ability to let the 'corporate governance genie' out of his brass lamp with a single rub, what would I wish to see as my Top 10 New Year's resolutions for improving corporate governance in the Middle East?

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1. Establish a clear and documented segregation between the roles and responsibilities of shareholders, the Board of Directors and management...

The large majority of corporations in the region are family businesses that represent a substantial part of the private sector. Within this segment, the roles and relationships between family members, the Board and its members, shareholders and the executive are undefined, undocumented, overlapping, conflicting and complex. Operating in an oral and consensus-based

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culture, many do not realise the need to create and document policies and procedures to improve operational efficiencies and reduce the incidence of blunders. I am still exasperated when I see how some of the family businesses within my spouse's 'tribe' are run and what never ceases to amaze me is the amount of time family members (in their capacity as shareholders, executives, management or simply elders and advisers) spend seeking consensus on basic items that should be sacrificed to simple policies and procedures.

3. Implement an authority matrix

There are a large number of traditional small to medium-sized firms in the region where the Chairman still signs the payroll, and if he happens to be travelling, his staff's salaries wait until his return for his signature on the cheques!

Whilst this example of the lack of delegation may seem archaic in terms of a 'Western' governance model, Middle Eastern culture has always been slightly resistant to the delegation of authority, which has contributed towards operational bottlenecks and restrictive corporate practices. Simply put, 'I hold the cheque book and don't trust anybody else to.' A clear authority matrix must allow for the delegation of authorities within specified limits and controls, whilst ensuring clear accountability (and freeing-up your chairman to be the chairman and not an accounting clerk!).

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2. ...and clarify the role of the Chairman

The interpretation of the title 'Chairman' in any reasonable corporate governance code means the Independent Non-Executive Director who chairs the Board of Directors. In Middle Eastern culture, and due to the prevalence of large family businesses, 'Chairman' generally means the principle shareholder and founder, who still owns the bulk of the enterprise and still possesses the majority, if not all, of the powers typically associated with the position of Chief Executive. The title 'Chairman' is also easily interchangeable with other titles such as General Manager, President and even Managing Director.

4. Provide further education for your board members

There are now several institutions and organisations offering board leadership and non-executive director courses in the region. Some offer professional certification for board members whilst assisting in developing skills and keeping individuals appraised of the most up-to-date corporate governance practices and regulatory frameworks within the corporation's home jurisdiction.

As a visiting Member of the Faculty of Mudara – the Institute of Directors headquartered in the DIFC, I've always been humbled by the desire to learn, that I have witnessed, from Middle Eastern board members. The course discussions inevitably come down to the difficult and demanding aspect of implementation, as board members start to openly discuss the cultural changes and challenges they are about to face.

5. Address those transparency issues

In 2009, Hawkamah reviewed some 600 regional companies and discovered that (a) only 10 per cent of Gulf Co-operation Council (GCC) listed companies provided information about their board members and executive management, beyond their names on the websites and annual reports; (b) only 22 per cent of GCC listed companies identified their executive and non-executives directors; (c) only four per cent of listed companies hold investor analysis meetings or conference calls; (d) only 30 per cent of companies provided a summary of their financial performance; and (e) 14 per cent of GCC listed companies did not have a website!

6. Respect the cultural challenges that lie ahead

Try convincing the joint Chairman/Chief Executive of the 'typical' corporation that, when the accounts are audited for the first time, the organisation may need to declare his remuneration! Whilst I am not suggesting that they have anything to hide I am highlighting the uphill struggle and cultural hurdles that these corporations and businesses are about to embark upon.

7. Attract experienced and independent non-executive directors onto the board

For the typical Middle Eastern Board that has chosen to appoint an independent

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non-executive Director, the challenge of selecting a candidate is not an easy one. The candidate must have industry experience but must also be independent. They ought to understand corporate governance but should respect the Middle Eastern cultural environment. As a new board member if they push too hard, the implementation of corporate governance will backfire but if they don't push at all, the evolution will stall. But most importantly, the candidate needs to be trusted by the various parties and stakeholders and will need a large diplomatic skill-set to gently, but firmly move the organisation up the corporate governance curve.

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8. Establish an audit and risk committee and recognise that the governance of risk is a board responsibility

Due to the nature of the activities undertaken by this committee, it's suggested that the individuals on this committee have a strong understanding of internal audit, external audit, accounting principles, financial reporting and risk management expertise. It is generally recommended that the committee is comprised of a majority of independent non-executive directors who must oversee the principle elements of (a) financial statements; (b) internal controls; (c) risk management; (d) external audits; (e) internal audit and others.

Establishing a sound system of risk oversight, management and an effective internal control environment is another fundamental role of the board. Risk management supports better decision making because it develops a deeper insight into the risk-reward trade-offs that all organisations must continuously evaluate.

9. If it's a family business then establish a family constitution

A family constitution should outline the principles and policies that the family and its business subscribe to and must describe the roles and function of all parties including the shareholders, board, management and employees. By defining the manner by which family members may become involved in the business will contribute to the avoidance of many misunderstandings. As any family and its related business expand, it is important to recognise that the complexities increase exponentially. Less than five per cent of family businesses survive passed the third generation.

10. Realise that corporate governance is in your interest

Be it in the West or in the Middle East, good corporate governance bears similar key benefits namely (a) it should lead to better strategic decision making; (b) it should help in gaining access to cheaper credit and capital; (c) it should provide better valuation of your enterprise; (d) it should drive a stronger internal risk management and control framework; and finally (e) it should help you meet any regulatory compliance requirements.

In conclusion, any change requires courage and I firmly believe in the fact that change leadership should start from the top. As such, any New Year's resolutions relating to corporate governance should be driven by the board and its Chairman.

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The Arab Spring for corporate governance has started but whatever the outcome, I sincerely hope that the region retains its family values and Middle Eastern traits that my children are being raised with. Whatever the consequences, the implementation of corporate governance should not be at the cost of these traits and values. ■BME

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