ENHANCING CORPORATE GOVERNANCE THROUGH INDEPENDENT DIRECTORS

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The importance of good corporate governance in the economic landscape of a country need not be stressed more. Modern day economies are assessed as much by the quality of the governance standards of their legal entities as by the financial value they create. The fact that the UN Principles for Responsible Investing, UNPRI, recommended the inclusion of the Environment, Social and Corporate Governance disclosures as part of corporates' annual reports is a strong indicator of how much governments, regulators and investors increasingly recognize the importance of non-financial benchmarks to judge the performance of a corporate entity and its contribution to the nation's economy.

While Corporate Governance has been there through the history of corporate sector, in its earlier form of accounting standards and board disclosures, the reforms in enforcing stronger Corporate Governance standards gradually gathered pace with each corporate failure or scandal. This is evidenced by the enactment of the Australian, Hong Kong and Singaporean Corporate Governance codes after the Enron and WorldCom debacle, and the enactment of the OECD Principles of Corporate Governance after the Parmalat Fraud case. In the UK, the Cadbury report followed the famous Robert Maxwell case. The UAE issued its first Corporate Governance code in 2009 which was revised during 2016. The adoption and compliance with the UAE's Corporate Governance code has been on the rise since its launch.

The responsibility for ensuring good governance and long term sustainability in companies lies squarely on its Board of Directors. The stronger, more efficient, diverse and independent the Board is, the better will be governance of the entity. However, in the MENA region, the governance has mainly been directed in the corporates by the promoters and owners of businesses.

The MENA region has high concentration of family owned businesses. Such businesses were historically limited in their operations to one or two countries. In such circumstances, it was justifiable that owners appointed themselves on the Board of Directors as the role of Directors was seen to belong to the owners and no need was felt for independent people to be on the Board of Directors and for them to exercise the authority of the Board. Nonetheless, with the increasing diversity and cross-border nature of businesses' activities, it has become increasingly challenging for families and promoters to provide sufficient direction to businesses. Therefore, the need for independent directors emerges as a must. Independent Directors, being experts in chosen areas, are better equipped and positioned to provide the required guidance to businesses.

The OECD Principles of Corporate Governance note that independent Board members can contribute significantly to the decision making of the Board. They can bring an objective view to the evaluation of the performance of the Board and management. In addition, they can play an important role in areas where the interests of management, the company and its shareholders may diverge such as executive remuneration, succession planning, changes of corporate control, take-over defenses, large acquisitions and the audit function, to name a few.

The opinion is divided however, whether the requirements for better corporate governance, including guidance for composition of the Board and its committees, meetings, quorum, financial audit, CSR, along with the criteria for being considered "Independent Director" should be mandated by regulators or should it be left to corporates to decide. In view of the growing and emerging nature of corporate world in the MENA region, in my view, government authorities are in a better position to analyze the global trends, assess their impact and customize them to local economies and the overall objectives of the country. While the guidance from the authorities may indicate the structural components for effecting stronger governance, it should be left to the companies to populate the structure. For appointment of Independent Directors, attention must be paid to confirming the eligibility of individuals in terms of bringing value to the Board as well as ensuring the independence of the selected individuals. To achieve this, especially in the regional context, the criteria of independence should not be limited to non-share-holders and non-family relatives of the directors and shareholders. Furthermore, the value which the individual brings to the company in terms of experience, expertise, and most importantly diversity, should be key determinants in the selection process.

Globally, the trend has been to make corporate Boards as diverse as their operating environments and to make diversity a key criteria for selection of the Independent Directors. Diversity is determined on the basis of nationality, age, language, ethnicity, gender, education, experience, etc. A Board built on such parameters not only provides a different dimension to its decision making process, but it can potentially lead the company towards greater business opportunities as well. Extending the reach of the company through its Independent Directors is an advantage, which is further enhanced by the professional review and oversight which such Directors bring to the company.

Promoters should not feel uncomfortable with the presence of Independent Directors on Boards. Several studies have proved that companies with greater percentage of Independent Directors have better enhanced the value for their shareholders. Such companies have also been more sustainable in the longer term. There are several global corporates which have businesses spanning continents and have shown growth for several decades, which are fully managed by professional and independent Boards. The robust Corporate Governance frameworks put into practice by such companies, with the approval of shareholders in the General Meetings, become the guiding force to ensure the sustainability and growth of such corporates.

In terms of diversity, a lot of discussions also focus on maintaining the gender balance on company Boards. While traditionally, men have dominated the corporate Boards, it has been observed that women directors bring a fresh and different perspective to the decision making process, and thereby, enhancing it. When women have exposure to the frontline of economic activity through participation on corporate Boards, this enhances the general well-being of societies and boosts their future prospects. The UAE Government has shown a great deal of interest in gender parity and implements several programs to encourage women participation in boards. Hawkamah's Women Director's Program

was launched in 2015 to train women who aspire for Directorial positions and enhance the capabilities of those who already sit on corporate Boards.
In theory, Independent Directors are supposed to be the ones who speak their minds independently during board meetings. In reality, that depends to a large extent on whether companies really adhere to corporate governance or they merely follow a “box-ticking” exercise. In such case, while the number of Independent Directors may meet the regulatory requirements, by virtue of their selection and appointment to the Board, or for personal interests, the Directors feel indebted to the shareholders and hence tend not to voice their independent opinion. This goes against the very logic of making the Boards independent and does not contribute to enhancing the value of decision making within the board. Directors who speak their minds during board meetings are those who overcome this hesitation, voice their opinions and thereby, provide their own perspective during the Board’s decision making process.

While the idea of better corporate governance is well established, and the MENA countries have issued their own codes, mainly based on the OECD guidelines, the challenge reported by corporates is to find suitable independent candidates. To that end, Hawkamah has done some very good work over the last ten years. Its various Director Development Programs are instrumental in developing the required oversight and decision making skills of candidates who represent a rich pool from which Independent Directors can be drawn by companies. Through board briefings and retreats, Hawkamah guides directors as to how to be truly independent thinkers and stresses the importance of this to create effective boards.

Having a centralized database of potential Directors makes it easier for companies and board recruitment agencies to assess the profiles of available candidates and to place the right person on the right board. It would be useful if such a database can be structured to also capture the performance of Independent Directors in terms of their contribution to the Boards on which they sit. This could be done for example through recording Independent Directors’ attendance in Board meetings, participation in Board committees, contribution to professional and academic institutions; accuracy of their disclosures of conflicts of interest, and the record of their voting in Board matters. The availability of such information, in addition to the financial performance of the companies on which they sit, can be a good tool to assess the directorial profile of any person. As the database gains acceptance and as it develops, it will become a key reference point to determine the reputation and the remuneration of the Independent Directors.

My expectation and aim towards looking forward to seeing the companies in the MENA region derive their value as much from operational performance as from their enhanced governance practices.