



## Concept Paper

### Stakeholder Discussions on “Need for *Guidelines for Corporate Governance for Non-listed Companies in Pakistan*”

There has been considerable debate in our country on corporate governance following the release of the Code of Corporate Governance, issued by the Securities and Exchange Commission of Pakistan (SECP) in March 2002, and several other circulars, issued by the State Bank of Pakistan. All of these requirements have focused on the listed companies and entities in the financial sector. Non-Listed Companies (NLCs) constitute the bulk of businesses in Pakistan, numbering around 50,000 compared to only 650 companies listed on the country’s stock exchanges (based on mid 2006 figures). Notwithstanding the important role and contribution of NLCs in our economy, there has been no discussion on the need to improve their internal and external governance. Recognizing the significance of NLCs to the national economy, the representatives of the Pakistan Institute of Corporate Governance (PICG), the Pakistan office of the Center for International Private Enterprise (CIPE), and the Institute of Chartered Accountants of Pakistan (ICAP) have held two meetings and a roundtable, with a view to initiate a dialogue between various stakeholders, regulators, and policymakers on the need to develop guidelines for a Corporate Governance Framework focusing on non-listed companies.

#### Relationship of Corporate Governance to Corporate Performance and Value

There is now a worldwide consensus, supported by empirical evidence gathered in the form of numerous research reports, that adopting the basic principles of corporate governance, namely fairness, transparency, accountability, and responsibility, improves company performance and competitiveness – that there is a positive relationship between good governance and performance.

By adopting good corporate governance principles, companies can often command higher valuations, improve their profitability faster, and gain better access to outside capital than their poorly-governed peers. Good corporate governance is considered a key factor that can help developing countries aiming for higher investment and capital formation, attract greater interest from local and foreign investors, and reduce their vulnerability to financial crisis. It will also assist NLCs in smoothly adopting the code of corporate governance when they become listed.



## **Corporate Governance Debate and Reforms**

Triggered primarily by large corporate failures and mega scams, there has been wide-ranging debate on corporate governance between politicians, academics, regulators, and the investment community in virtually every corner of the world in the past ten years. The movement that started with the publication of the Report on Financial Aspects of Corporate Governance by the UK's Cadbury Committee in 1992 prompted companies worldwide to assist in developing corporate governance principles and codes. The creation of a basic corporate governance code sparked sweeping reforms, both in developed and developing countries.

In Pakistan, this movement was initiated by ICAP. Through an extensive consultative process with stakeholders such as the SECP, listed companies, corporate lawyers, and chambers of commerce, ICAP organized an international conference on corporate governance in 2000. The conference was followed by the creation of ICAP's committee on corporate governance, which was responsible for drafting the Code of Corporate Governance. The approved code was subsequently incorporated as part of listing rules of the stock exchanges through a directive of the SECP (under the Securities & Exchange Ordinance, 1969 in March 2002), thus making corporate governance requirements mandatory for all listed companies.

Despite the recognition of good governance practices as a key step in improving company performance and leading to rapid economic development, debates and reforms throughout the world have focused primarily on improving governance of listed companies. Until very recently, there has been no or little discussion on whether and to what extent corporate governance principles can be beneficial in enhancing the efficiency, performance, and growth of NLCs.

## **Recent International Dialogue on Corporate Governance for Non-Listed Companies**

Realizing the important role that NLCs play in economic development, the "International Experts Meeting on Corporate Governance of Non-Listed Companies" was organized by the OECD in Istanbul, Turkey in April 2005 with the support of the Government of Japan. As a result of this meeting, the Global Network of Corporate Governance of Non-Listed Companies was launched, bringing together policymakers and practitioners from around the world. The objective of this forum was to gather global experience on the pitfalls of "over-regulation" and facilitate communications with policymakers on the corporate governance needs of NLCs.



The April 2005 meeting was followed by an OECD focus group meeting in Paris in December 2005. While the Istanbul meeting greatly contributed to better understanding of corporate governance challenges for non-listed companies globally, participants noted that many issues remained unresolved and that further discussion and research was necessary in order to implement the suggestions from the Istanbul meeting. Key issues discussed in the December focus group meeting included:

### **Purpose of the stakeholders discussions and the Roundtable**

- Legal and regulatory frameworks
- Transparency and disclosure
- Ownership structure and financing

There are two key reasons advanced in favor of good corporate governance, especially in the context of emerging markets, in addition to the reducing the risk of fraud and misappropriation by management and majority shareholders against the interest of minority shareholders. These are:

- **Improving access to capital.** Much attention to corporate governance issues in emerging markets among policymakers and academics has focused on the role governance can play in improving access to global portfolio equity for *companies in emerging markets*. An increasing volume of empirical evidence indicates that well-governed companies receive higher market valuations. However, improving corporate governance will also increase capital flows to companies in developing countries: from domestic and global capital, equity and debt, and public securities markets and private capital sources.
- **Improving performance.** Equally important and irrespective of the need to access capital, good corporate governance brings better performance. Improved governance structures and processes help ensure quality decision-making, encourage effective succession planning for senior management, and enhance the long-term prosperity of companies, independent of the type of company and its sources of finance.

The purpose of the current focused discussions being organized by CIPE, PICG and ICAP, is to initiate dialogue between the business leaders, providers of capital, accountants and auditors, regulators and other stakeholders on possible ways in which Corporate Governance of NLCs, a large number of which are family owned and managed, can be improved with a view to enhance their competitiveness thereby improving their value for the stakeholders as well as their contribution to the country's economic development.



CIPE has invited Chris Pierce, CEO of Global Governance Series Ltd. of the UK to share his expertise. Mr. Pierce is a specialist in leading Global Governance leadership programmes and a specialist on this subject. He is also the Director of the Global Governance Leadership Program run by the Global Corporate Governance Forum. He is an Executive Fellow of the Henley Management College, and a Director on a number of Boards in the UK & overseas. Chris is based in GGS office in London and works world-wide.

It is expected that the discussions will generate enough interest among the participants in preparation of Guidelines on Corporate Governance for NLCs.