

CORPORATE GOVERNANCE DEVELOPMENTS IN THE SAUDI ARABIA AND MALAYSIA

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ABSTRACT

In the past few years, there has been an increasing concern over the discrepancy of standards of the corporate governance amongst the developed and the developing countries since they affect their competitive advantages economically. In 2017, Saudi Arabia and Malaysia have amended their codes on corporate governance, in order to promote ethical behaviour, transparency, accountability and investor stewardship. In this paper, the researchers analyse the important features of these new codes of Saudi Arabia and Malaysia. They use a comparative approach to identify the advantages and limitations and also to determine areas for improvement. This paper finds that several transformations were already taking place in both jurisdictions. However, there are many areas that require continuous development, especially those related to the independence of the board, gender diversity problems, and impartiality in the decision-making process. The researchers suggest that many recommendations regarding the manner in which the two countries can address the loopholes and thereafter, improve their corporate governance codes in order to be on a par with international standards.

Keywords: *Corporate governance, Investments, Directors' duties, Gender issues.*

INTRODUCTION

The concept of corporate governance has been recognised since the development of the joint stock companies and was considered an

important component of corporate law and practice. These corporate governance systems were developed over many decades to tackle the systemic crises or the corporate failures. In the past few years, there has been an increasing interest in corporate governance amongst the developed or the less developed nations. After the economic collapse and the financial crises affecting many countries like USA, Russia and other countries in Latin America and East Asia, several corporate governance regulations were presented to deal with the restructuring efforts aimed at corporations.¹ The various collapses and crises were attributed to a lack of investor confidence, inadequate corporate transparency or disclosure and a lack of structured corporate governance.² In addressing these issues, many reform measures had to be carried out to strengthen the existing guidelines and codes regarding corporate governance.

The corporate governance is vital for the economic development and establishment of financial market stability. In the past few years, increasing global financial crises have highlighted the significance of corporate governance. Due to economic liberalisation and globalisation, the corporate governance-related components were considered as an important contemporary tool.³

Corporate governance needs to be developed further in Saudi Arabia to help the country facing the competitive challenges that can affect the country in the future. There are several rules and regulations that contributed to the development of corporate governance in Saudi Arabia. The development of corporate governance is divided into two stages. The first stage began when the Ministry of Commerce and Industry in 1985 issued the Disclosure and Transparency standard.⁴ This led to the recognition of corporate governance and this disclosure and transparency standard is considered to be one of

¹ Demirag, I. & Solomon, J. (2003). Guest Editorial: Developments in International Corporate Governance and the Impact of Recent e-Events. *Corporate Governance: An International Review*, 11 (1): 1-7, 1.

² Ho, S. & Wong, K. (2001). A Study of the Relationship between Corporate Governance Structures and the Extent of Voluntary Disclosure. *Journal of International Accounting, Auditing and Taxation*, 10 (2): 139-156, 140.

³ Al-Mutairi, O. (2003). Apply the Procedures Governing the Companies in Saudi Arabia. *Arab Journal of Administrative Sciences, Arabic Ed.*, 15 (3); 1-50, 5.

⁴ Meteb, M.A. (2012). The Importance of Corporate Governance in Saudi Arabian Economy. *Journal of WEI Business and Economics* 4 (1): 1-25, 18.

the most important elements of corporate governance best practices.⁵ The second stage of the development of corporate governance in Saudi Arabia witnessed the enactment of Capital Market Law of 2003 and the issuance of regulations by the Board of the Capital Market Authority established by the Capital Market Law.⁶ The Board of the Capital Market Authority has used the powers given to it and issued regulations regarding corporate governance. The most recent development of corporate governance in Saudi Arabia is the released of Regulations on corporate governance in the year 2006.

The Saudi Arabian government may review and learn lessons from other jurisdictions. In order to remain competitive in the changing economic climate, the Saudi corporations have to implement and adapt the best corporate governance practices for the purpose of fulfilling the arising demands and opportunities. In a similar development, the Malaysian Code on Corporate Governance (MCCG) was amended to reflect the internal standards and universal principles of the Corporate Governance.⁷ Hence, any adherence by these companies to the MCCG would help them remain on par with the international governance standards.⁸ In 2017, both Malaysia and Saudi Arabia amended their corporate governance codes, for the purpose of promoting accountability, ethical behaviour, transparency and stewardship of the investor capital. Further, these amendments increase the distribution of the responsibilities and rights amongst the participants in a company. They also outline the processes and rules that are needed for controlling, risk-management and decision-making purposes.⁹

In this paper, the researchers discuss the important features of these new codes of the corporate governance in Malaysia and Saudi Arabia. They also attempted to highlight the loopholes and the areas that need further improvements. For this purpose, they overviewed

⁵ Ibid.

⁶ Falgi, K. I. (2009). *Corporate Governance in Saudi Arabia: A Stakeholder Perspective*. Unpublished PhD.UK. University of Dundee and Meteb, M.A. (2012). The Importance of Corporate Governance in Saudi Arabian Economy. *Journal of WEI Business and Economics* 4 (1): 1-25, 18.

⁷ Christopher, S. and Ong, L. (2017). The Malaysian Code on Corporate Governance 2017, available at <https://www.christopherleeong.com/media/2803/clo-2017-05-the-malaysian-code-onf.pdf> (accessed 9 April 2018).

⁸ Ibid.

⁹ Ibid.

the corporate governance and also discussed the various theories. Thereafter, they examined the development of the corporate governance in the two jurisdictions and also highlight the provisions in the new codes. Finally, the discussion compares both codes of Malaysia and Saudi Arabia in order to identify their similarities and determine the areas which need further improvement to attain the global corporate governance standards.

AN OVERVIEW OF CORPORATE GOVERNANCE

The codes on the corporate governance include the regulation of the relationship between the executive directors, board, shareholders and the stakeholders. They also help in establishing the processes and rules which would facilitate decision-making and add further transparency so that the rights of all stakeholders and shareholders could be maintained. This would help in achieving competitiveness, transparency and fairness during the exchange in a business environment.¹⁰ The corporate governance includes the manner in which the company is controlled and directed so that it displays an optimal performance. It also describes the way the board and the management were held accountable to allow the shareholders to derive a maximum advantage from the corporate performance.¹¹ Towards this end, it is important to display a higher level of transparency in the process of directing or controlling a company, so that the vital corporate information can be reliably disclosed to the potential or existing shareholders.¹² Goo and Carver argued that corporate governance highlights the relationship between all participants since it determines the direction and performance of the corporations.¹³ These basic participants include the management, shareholders, the board of directors along with the employees, suppliers, customers, creditors and the total community.¹⁴

The corporate governance helps in improving the management and enables a prudent distribution of all company resources, which further

¹⁰ Part 1 Preliminary Provision of the Saudi Code on Corporate Governance 2017.

¹¹ Goo S. H. & Carver, A. (2003). *Corporate Governance; The Hong Kong Debate*. Asia: Sweet & Maxwell, 4.

¹² Ibid.

¹³ Ibid.

¹⁴ Monks, R. & Minow, N. (2004). *Corporate Governance*. Oxford: Blackwell Publishing, 10.

improves the corporate performance. All the earnings derived from the management will improve performance and increase the value of the shareholdings.¹⁵ In contrast, improper corporate governance results in very poor earnings and management, which could affect the share value and lead to the liquidation of the company.¹⁶ In the presence of ineffective corporate governance activities, the investors tend to withdraw all their savings, which can significantly decrease the share prices and liquidity which caused the whole investment turn unattractive.¹⁷

The corporate governance provisions describe the significance of the relationship between all shareholders and stakeholder groups, or the board of directors and the top management of different corporations. Hence, the corporation regime offered many considerations for the regulators, related to their effectiveness to the shareholders, local community, employees and the environment.¹⁸

Based on the practices in the developed and developing countries, there are generally two prevailing views regarding the corporate governance system. A few countries tend to follow the Anglo-American shareholder model while some other countries follow the Continental European and Japanese stakeholder model.¹⁹

The corporate governance regulations used in Saudi Arabia are based on the Anglo-American shareholder model. Many studies found that corporate governance acts as an important tool to develop and control businesses. Corporate governance includes many principles which are anticipated by the shareholders. This tool encourages a complete disclosure of corporate information, that in turn helps them to deter the wrongdoings committed by the chief executives and the board of directors. While there are many factors contributed

¹⁵ Mobius, M. and Chan, D. (2000). Corporate Governance in Hong Kong – Gaps that Need to be Filled” in Chee Keong Low (ed), *Financial Markets in Hong Kong*. Singapore: Springer, 30.

¹⁶ Ibid.

¹⁷ Goo S. H. & Carver, A. (2003). *Corporate Governance; The Hong Kong Debate*. Asia: Sweet & Maxwell, 5.

¹⁸ Solomon, J. & Solomon, A. (2004). *Corporate Governance and Accountability*. England: John Wiley & Sons, Chichester, 2.

¹⁹ Aguilera, R., Williams, C., Conley, J. & Rupp, D. (2006). Corporate Governance and Social Responsibility: A Comparative Analysis of the UK and the US. *Corporate Governance: An International Review*, 14(3): 147–158, 149.

to the significance of corporate governance, at the same time, the fact that there is a lack of control strategies and adequate regimes in place also have negatively affected the business activities of the global stock markets.²⁰

Corporate governance is vital for the domestic corporations and is also necessary to prevent further withdrawal of the foreign investment which are vital for the economy and quality of the institutions for governance.²¹ There is a lot of discussion regarding what is included in the effective corporate governance and the factors that are necessary to attract additional external investment and to warrant the sustainable development of a country's total economy. Effective corporate governance correlate strongly with corporate performance because: 1) corporate governance encourages additional external investment in the different organisations; 2) it decreases the capital costs; 3) it encourages further reforms that can improve the operational performance, and; 4) it decreases the risk of contagion from the financial distress.²²

The disclosure requirements are an effective market-led technique of achieving all the results. The corporations and organisations must present a descriptive and coherent statement which includes all the elements of a corporate governance structure and practice. This statement must also describe the operations of the shareholder meetings and its important powers, the operation and the composition of the board and all other committees, along with a reference to the code on the corporate governance that can be used at the national level, which is complied with by the company or used as a reference to explain if there is a deviation.²³

There is an increasing awareness about the correlation between an effective corporate governance framework and the improving

²⁰ Ibid; El-Khudery. M. (2005). *Corporate Governance*, Arabic edition. Egypt: Arab Nile Group, 6.

²¹ El-Khudery. M. (2005). *Corporate Governance*, Arabic edition. Egypt: Arab Nile Group, 6.

²² Grais, W. & Pellegrini, M. (2006). *Corporate Governance in Institutions Offering Islamic Financial Services: Issues and Options*. World Bank Policy Research Working Paper, No. 4052, 7.

²³ Bolkestein, F. (2003). *Modernising company law and enhancing corporate governance in the EU: The way forward*, available at europa.eu/rapid/press-release_SPEECH-03-298_en.doc (accessed 13 April 2018).

financial stability. The corporate governance and the financial stability form an indirect relationship, where the companies are not obligated to pursue any financial stability unless the regulations or legislation require it.²⁴

Additionally, corporate governance is a vital element which helps in achieving economic growth and performance as well as to boost the investors' confidence. Hence, the supporting structures for controlling, determining and fulfilling all corporate targets and objectives must be put in place. It also triggers the creation of appropriate initiatives for the various members of the management and the administrative bodies.²⁵ Effective corporate governance in the company and the total economy is vital for the purpose of developing trust and confidence in the existing market economy.²⁶

Ross observed that the different corporate structures vary in many ways, though the major business goals remain universal. 3 major models are in existence in the current corporations; namely, the continental, Japanese and the Anglo-Saxon, models.²⁷ Out of these models, the Anglo-Saxon model has been developed in the US and UK, and the major controlling parties in the model include the shareholders and the board of directors. The Chief Officers and the managers possess a secondary authority.²⁸ The managers derive their power from the company board, which is theoretically dependent on the approval of the voting shareholders. A majority of the companies that follow the Anglo-Saxon corporate governance system control the shareholders' ability to display a practical and day-to-day control of the company activities. The Anglo markets also display a highly dispersed shareholder and capital structure.²⁹

The term "continental" refers to central Europe. Ross stated that the continental model was based on the fusion of the fascist and

²⁴ Lupu, L. (2015). The Indirect Relation Between Corporate Governance and Financial Stability. *Procedia Economics and Finance*, (22): 538-543, 540.

²⁵ Kocmanová1, A., Hrebíček, J. and Dočekalová, M. (2011). Corporate Governance and Sustainability. *Economics and Management*, 16, 2.

²⁶ Ibid.

²⁷ Ross, S. (2015). What are some examples of different corporate governance systems across the world? Available at <https://goo.gl/8HTqEr> (accessed 22 January 2018).

²⁸ Ibid.

²⁹ Ibid.

the Catholic influences seen in the early and mid-20th century. The German and Italian companies have used this model. According to Ross, in a continental model, the company entities are considered to be an organising vehicle between all the various domestic interest groups. Generally, banks play a vital role in the financial and decision-making process of corporations. They offer special protection to the creditors, especially the politically-connected creditors. Such companies consist of a Supervisory Council and an executive board, wherein the Supervisory council manages the executive board that, in turn, controls the company management. The domestic and the government interests severely affect the continental model, and a lot of attention is given to the corporation's responsibility to fulfil the governmental objectives.³⁰

The 3rd model includes the Japanese model, which displays a sense of mutual balance and responsibility. In Japanese, the term, "balance" refers to the loyalty between the various suppliers and customers. In actual practice, Ross stated that this balance is converted to a type of defensive posturing and a distrust of the newer business relationships compared to the old and existing relationships. The Japanese regulators play a vital role in the corporate policies since the major corporation stakeholders include the Japanese officials. Ross stated that in this model, the Japanese Ministry of Finance and Central Bank reviewed all relationships between the various groups and exhibited a total control over all negotiations. Based on the concentration of the power amongst the Japanese banks and corporations, the Japanese model showed a lack of transparency. The individual investors are perceived to be less important than the government, business entities and the union groups.

Finally, the differences between all the systems are reflected in their different objectives. The Anglo-Saxon model is more oriented towards the stock market, while the remaining two models focused on the banking and the credit markets. The Japanese model is rigid and concentrated whereas the Anglo-Saxon model is more flexible and dispersed.

³⁰ Ibid.

THE DEVELOPMENT OF THE CORPORATE GOVERNANCE IN SAUDI ARABIA

The Islamic principles as the foundation present within the business environment since they strongly believe in Allah, focus primarily on high ethical standards and protection of human rights. Hence, Saudi Arabia has adopted the majority of their auditing and accounting standards with influences of the *Sharia* principles. *Sharia* remains as the supreme law in Saudi Arabia, and the legislators' work is always in accordance with *Sharia* principles. Hence, rules enforced must not "contravene the spirit of Islamic law".³¹ As mentioned above, corporate governance is vital for any country, including Saudi Arabia. Protection of all rights of the parties is an important aim of the corporate governance, and the Islamic religion supports every process that attempts to fulfil this aim, as long as it does not violate any *Sharia* principle. Thus, the concept of corporate governance is not strange to the Islam religion. Lewis stated that Islamic corporate governance can be developed using two concepts³² - 1) Sovereignty of *Sharia* over the different aspects of life, like the social, economic and legal; and 2) Financial and the Islamic economic principles such as a prohibition of *riba* (usury) and an imposition of *zakat*, which can directly affect all policies and practices of the companies and also ensure the implementation of proper business ethics.

In 2006, due to the collapse of the Saudi Exchange, the country had lost about US\$450 billion.³³ This was a stunning blow to the broad Saudi economy, which showed low inflation and a stable growth. Oil exports form a major proportion of the national income of Saudi Arabia, however, accession to the World Trade Organisation (WTO) helped the country improve its foreign investment and increase the diversification of its economy.³⁴ The collapse of the Saudi exchange triggered the Saudi regulators to take steps to protect the

³¹ Al-Haddab, B. & Puig, G. V. (2013). The Protection of Minority Shareholders in the Gulf Cooperation Council. *Journal of Corporate Law Studies*, 13.

³² Lewis, M. (2005). Islamic Corporate Governance. *Review of Islamic Economics*, 5 (9): 5-29, 4.

³³ Al-Matari, Y. A., Al-Swidi, A. K. and Fadzil, F. H. (2012). Corporate Governance and Performance of Saudi Arabia Listed Companies. *British Journal of Arts and Social Sciences*, 9(1): 21-251, 242.

³⁴ Capital Markets Guide. (2008). Middle East: Towards Innovation and Transparency, available at http://www.gtpak.com/Publications/Downloads/memg_report_final.pdf (accessed 25 March 2018).

securities market and investors as an additional precautionary step in anticipation of possible future economic collapses.³⁵

One of the main steps implemented by the Capital Market Authority (CMA) board was the formulation of a corporate governance code, which must strictly be complied with by all the Saudi-listed companies.³⁶ The CMA implemented many steps for the purpose of decreasing the effect of the local retail investors, such as; firstly, the foreign residents in Saudi Arabia could invest in the economy. Secondly, the market was open for the Gulf Cooperation Council funds and nationals. Thirdly, the CMA limited the allowable participation of Saudi residents in the Initial Public Offerings at 30%.

The corporate governance in Saudi Arabia is in its infancy phase, and lacks accountability, and displays a weaker legal framework and inadequately protects the shareholders. The board of directors and the audit committees do not play an effective role in the corporate governance. In their analysis, Al-Matari *et al* stated that the audit committees in the Saudi industries were a vital component of corporate governance. However, they were inefficient as they could not fulfil their roles due to a lack of qualified and independent members.³⁷ The monitoring mechanisms will be more effective only if they are afforded with a higher authority and independence.³⁸

Saudi Arabia is a major ‘G20’ economy, the largest oil producer in the world and a home of some of the biggest global multinational corporations.³⁹ The repercussions includes that a corporate governance failure in Saudi Arabia may trigger a crisis to go beyond

³⁵ Al-Matari, Y. A., Al-Swidi, A. K. and Fadzil, F. H. (2012). Corporate Governance and Performance of Saudi Arabia Listed Companies. *British Journal of Arts and Social Sciences*, 9(1): 21-251, 242.

³⁶ Capital Market Authority. (2006). *Corporate governance regulations in the Kingdom of Saudi Arabia*. Riyadh, Saudi Arabia.

³⁷ Al-Matari, Y. A., Al-Swidi, A. K. and Fadzil, F. H. (2012). Corporate Governance and Performance of Saudi Arabia Listed Companies. *British Journal of Arts and Social Sciences*, 9(1): 21-251, 243.

³⁸ Ibid.

³⁹ Munisi, G. and Randoy, T. (2013). Corporate Governance and Company Performance Across Sub-Saharan African Countries. *Journal of Economics & Business*, (70): 92-110, 93.

the Middle East and may be extended to developing countries and the global economy.⁴⁰

DEVELOPMENT OF THE LAWS ON CORPORATE GOVERNANCE IN SAUDI ARABIA

The 1965 Companies Law was an important regulation for the Saudi companies. It was based on the British Companies Law and was issued in 1965 by the Royal Decree for the Saudi companies to comply with the rules and guidelines. Although this law was modified to accommodate the developments occurring within the Saudi companies, many experts were of the view that it was out-dated and could not satisfy the current requirements.⁴¹

This law was unchanged since 1965, and hence became out-dated. The proposed reform on Company laws was initiated in 2015 and the Ministry of Commerce exerted greater efforts in drafting new laws with improved features. This new law amended and updated the important institutional bodies, like the CMA. Furthermore, it was noted that this law was the sole responsibility of the Minister of Commerce, instead of the CMA, like the following 2016 Law.

The 2016 Companies Law came into force on 2nd May 2016 and presented many reforms.⁴² It has 226 Articles and replaced the 1965 Companies Law.⁴³ This 2016 Companies Law was amended in order to be in compliance with the *Sharia* principles.

⁴⁰ Al-Bassama, W. M., Ntimb, C. G., Opong, K. K. & Downs, Y. (2015). Corporate Boards and Ownership Structure As Antecedents of Corporate Governance Disclosure in Saudi Arabian Publicly Listed Corporations. *Business & Society* 1–43. DOI: 10.1177/0007650315610611, 4.

⁴¹ Al-Ghamdi, S. and Al-Angari, H. (2005). The Impacts of Implementing Quality Review Program on Audit Firms in the Kingdom of Saudi Arabia: An Empirical Study. *Journal of King Abdul-Aziz: Economics and Administration*, 19 (2) 48–77, 40.

⁴² This Companies Law was executed under the Royal Decree No. (M / 3) dated: 01/28/1437 and the Council of Minister Resolution No. (30) dated 01/27/1437.

⁴³ Issued under the Royal Decree No. (M / 6) dated 03/22/1385 AH, thereby eliminating all the conflicts; Alshowish, A. M. (2016). An Evaluation of the Current Rules and Regulatory Framework of Corporate Governance in Saudi Arabia: A Critical Study in Order to Promote an Attractive Business Environment. Faculty of Arts and Social Sciences, The Law School, Lancaster University. PhD dissertation, available at <http://www.lancaster.ac.uk/people-profiles/abdullah-alshowish> (accessed 4 April 2018).

The 2016 Companies Law was introduced to reconcile inconsistencies between the 1965 Companies Law and the 2003 Capital Market Law, with regards to the shareholding companies. It consists of many articles which highlight the responsibilities of the CMA and the Ministry of Commerce. This law is believed to be capable of dealing with the issues that decreased the effective working of companies because of bureaucracy.

There are similarities between the corporate governance and company law. The Saudi's New Companies Law provides that the general assembly meetings can be convened using the current communication processes, or the introduction of a novel and cumulative voting system for electing the members forming the board of directors;⁴⁴ general assembly of the shareholders, which establish the audit committee for supervising the company activities, wherein the executive board members were ineligible for the audit committee membership. Also, the chairman position cannot be combined with other executive positions.⁴⁵ This new company law consists of many detailed provisions that indicate the division of power in the company and the execution of this power. Though this law is generally flexible, some areas are still unregulated. In such cases, the governance codes are implemented for resolving the issues that carry risks. A few of these risks, which are not resolved by the company law, have been described below, followed by all governance codes used for resolving these risks⁴⁶.

In order to ensure the effective functioning of the board of directors, the provisions in the governance codes and the company law must be considered, since there is a symbiotic correlation between them. The new 2016 Saudi Company Law is capable of addressing several issues related to corporate governance. If the issues arise consist some risks, the principles under the governance codes are used to bridge the gaps where the risks occur. As mentioned before, the collapse of the Saudi Exchange in 2006 triggered the development of the new corporate governance codes to bridge the above-mentioned gaps. Thereafter, the 2006 Saudi corporate governance codes were

⁴⁴ Article 95 of the Saudi New Companies Law.

⁴⁵ Article 81 of the Saudi New Companies Law.

⁴⁶ Ndlovu, B. (2017). The Interplay Between Corporate Governance and Company Law, available at <https://www.linkedin.com/pulse/interplay-between-corporate-governance-company-law-bonani-ndlovu/> (accessed 12 March 2018).

amended in 2009, reflecting the new developments occurring in this area, in the hope that the Saudi companies stayed on par with the international standards. This law was later amended in 2017, and the existing status of the new Saudi codes on corporate governance is discussed below.

THE CURRENT SAUDI CODES ON THE CORPORATE GOVERNANCE

The CMA board of Saudi Arabia released a new corporate governance code in April 2017 for the joint stock Saudi companies, listed on the Saudi Exchange. This code replaced the 2009 code and provide the shareholders and the board members with higher clarity, more rights and transparency with regards to their responsibilities and duties. One of the main objectives of the 2017 code is to attract further foreign investments into Saudi Arabia. The 2017 code complements the CMA rules and the new 2016 Company Law, which is supervised by the Saudi Ministry of Commerce and Investment. The CMA implements this code to improve the regulatory oversight of all listed companies thereby improving its standards, similar to the other global exchanges.

The new Saudi corporate governance code is derived from the UK-based “comply or explain” compliance and the disclosure regime.⁴⁷ This code is different from that used in the Anglo-American countries, and requires all the companies to go above and beyond the restricted financial and regulatory features of the corporate governance as it addresses the interests of all the stakeholders, like customers, employees, creditors, suppliers and the local communities.⁴⁸ The “Voluntary disclosure” is defined as the voluntary corporate governance compliance and the disclosure regime including the “comply or explain”, which enables the managers and directors to comply with and disclose all corporate governance mechanisms used

⁴⁷ Organization for Economic Cooperation and Development. *Principles of Corporate Governance*. (1999). Available at [http://www.oecd.org/officialdocuments/publicdisplaydocumentpdf/?cote=C/MIN\(99\)6&docLanguage=En](http://www.oecd.org/officialdocuments/publicdisplaydocumentpdf/?cote=C/MIN(99)6&docLanguage=En) (accessed February 2018).

⁴⁸ Capital Market Authority. (2006). *Corporate governance regulations in the Kingdom of Saudi Arabia*. Riyadh, Saudi Arabia.

in the companies and to explain if they could not comply with the corporate governance provisions under the Saudi governance code.

SALIENT FEATURES OF THE SAUDI CODE ON THE CORPORATE GOVERNANCE 2017

Shareholder Rights

The new Saudi corporate governance code includes many provisions regarding the Shareholder's rights, such as - right against discrimination amongst the shareholders of one class; a fair treatment among the shareholders, unbiased distributions, right to vote in the general assemblies or the audit and board member selection, and equal rights for accessing the corporate information and communication.⁴⁹ Some mechanisms described the distribution of insolvency pay-outs and dividends.

Board of Directors

Article 16-41 in the new 2017 Saudi Code on the Corporate Governance provides a comprehensive set of rules and principles relating to the governing board of directors like the independent directors, Chairman, and board secretary. Some other rules regarding the board composition, formation, appointment, termination, membership conditions, responsibilities, independence, major functions, meeting-related procedure, distribution of competencies or duties, auditing, and training, etc. are included in the code. The Saudi new code 2017 ensures that the fiduciary duties should be based on the principles of honesty, loyalty and truthfulness.

This new Saudi code 2017 states that a majority of the company's board members must include the non-executive directors, while the total number of independent directors must be more than 2 or less than 33% of the board members, whichever is higher.⁵⁰ It is illegal to simultaneously hold the positions of the board Chairman or other executive position, like the Chief Executive Officer, Managing Director, or General Manager, though the Company's bylaws

⁴⁹ See Articles 4 to 15 of the Saudi Code on Corporate Governance 2017.

⁵⁰ Article 16 (2 and 3) of the Saudi Code of Corporate Governance 2017.

permit it.⁵¹ With regards to the board independence, the Saudi code 2017 states that the board must annually determine the degree of the member's independence and warrant that no circumstances or relationships affect the member's independence.⁵²

Conflicts of Interest

The Saudi new code 2017 on the corporate governance includes many provisions regarding the assessment, avoidance, and disclosure of any conflicts of interest in the board. One must establish the processes and policies related to the party transactions, conflicting scenarios (within the company or with its competitors), gift acceptance, conflicted people, and compliance with the authorities, renewal or termination of all board members, in accordance with the Companies Law.⁵³

Committees

Articles 83-88 of the Saudi new code 2017 describe all provisions associated with the composition, formation, responsibilities, membership, procedures, powers, policies, meetings or all announcements regarding the risk management, remuneration, audits, corporate governance or nomination. With regards to the constitution of the Remuneration Committee Article, Article 60 stated that:

- a) The Company board should set up a new committee, known as the "Remuneration Committee." The members of this committee must not be the executive directors, and there must be a minimum of one independent director amongst the members.
- b) The General Assembly of the Company, based on the board recommendations, must issue a regulation for this Remuneration Committee, which provides for its duties, rules and processes in selecting the board members, their membership terms and also their remuneration.

Article 70 of the Saudi new code 2017 describes the composition

⁵¹ Article 24(b) of the Saudi Code of Corporate Governance 2017.

⁵² Article 20(b) of the Saudi Code of Corporate Governance 2017.

⁵³ Articles 42 & 49 of the Saudi Code of Corporate Governance 2017.

of this Risk Management Committee, and states that the Company board must form a committee by resolution, known as the 'risk management committee'. The chairman and the board members are called the Non-Executive Directors, and must possess a proper knowledge about risk management and finance”.

With regards to the Audit Committee formation, Article 54 of the Saudi new code 2017 states that:

- a) The audit committee is formed through the resolution of Company's Ordinary General Assembly. The members of this audit committee must include the shareholders or other members if it includes no Executive Director and at least one of the members is an Independent Director. Further, the audit committee must include 3-5 members only, and one of the members must specialise in the field of finance or accounting.
- b) The audit committee chairman must be an Independent Director.
- c) The General Assembly of the Company must issue regulation for an audit committee, which includes the rules and processes for all duties and activities of the committee, rules for selecting the committee members, terms for their membership and nomination, their remunerations, and mechanisms for appointing temporary members, if the seat in this committee got vacated, based on the board recommendations.
- d) Any individual who worked or works in the finance department or executive management of the company, or was an external auditor for the company in the last 2 years, cannot become the audit committee member.

The Saudi new code 2017 further states that in the cases where conflicts arose between the audit committee recommendations and the board members, or if the company board is not ready to implement the committee's recommendations with regards to the appointment or termination of the company's external auditors, or determination of their remuneration, appointment of an internal auditor or their performance, the report presented by the board must include all the committee justifications and recommendations along with reasons for not following these recommendations.⁵⁴

⁵⁴ Article 56 of the Saudi Code of Corporate Governance 2017.

Stakeholders

Based on the Saudi new code 2017, the board of the listed companies must produce effective and written policies which can highlight the dealings with the different stakeholders, like employees and some incentives offered to them.⁵⁵ All these policies describe the manner in which the rights of the shareholders must be protected and also presents techniques for the purpose of dealing with the complaints, professional conduct, treatment of the employees, confidentiality of information, social contributions, and handling the non-compliance of the processes and policies. Furthermore, the employee incentive schemes and pay-outs should be documented.⁵⁶ Different policies must be presented to govern the ethical and professional corporate standards, social initiatives and social responsibilities.

General Disclosures and Transparency

The companies must disclose and present their accurate and updated information to the various stakeholders of the company, as mentioned in the Capital Market law and the Companies Law, as necessary.⁵⁷ The company board must maintain all the policies with regards to the information disclosure and offer a general board report along with the audit committee's report, and also maintain the information on the company website.⁵⁸ The remuneration of the executive committee and the board members should be disclosed as per the standard template, as mentioned in the Regulation.⁵⁹ All the company records (minutes, reports, documents, etc.) should be adequately maintained for a period of at least 10 years.⁶⁰

Article 13(d) of the Saudi new code 2017 states that the notice of the General Assembly meeting must include the place, date and the agenda of the meeting, for at least 10 days before the date. Further, the invitation must be published on the websites of the Company and the Exchange, and also in the daily newspaper which is distributed in the area where the Company headquarters are located. Article

⁵⁵ Article 83 of the Saudi Code of Corporate Governance 2017.

⁵⁶ Article 85 of the Saudi Code of Corporate Governance 2017.

⁵⁷ Article 89 of the Saudi Code of Corporate Governance 2017.

⁵⁸ Article 90 of the Saudi Code of Corporate Governance 2017.

⁵⁹ Article 90(8) of the Saudi Code of Corporate Governance 2017.

⁶⁰ Article 96 of the Saudi Code of Corporate Governance 2017.

13(d) states that the Company should also invite the Special and the General Shareholder Assemblies using contemporary tools and technologies.

THE DEVELOPMENT OF CORPORATE GOVERNANCE IN MALAYSIA

The economic crisis which hit many of the Asian countries in 1997-1998, encouraged the efforts at improving the corporate governance in Malaysia.⁶¹ Consequently, the country made many efforts for the purpose of restructuring and improving its corporate governance practices and framework, which as a result led to the introduction of the first code of corporate governance in March 2000.⁶² After the introduction and development of the MCCG in 2000, the country's administration made many progresses to improve the corporate governance standards.⁶³ The MCCG in 2000 was a hybrid in nature and similar to the UK code of corporate governance.⁶⁴ Using this process, the Malaysian companies need to apply comprehensive principles related to corporate governance set by the code according to the different settings of the individual corporations.⁶⁵ It was not compulsory to comply with the code. However, it was mandatory that the companies listed under the Bursa Malaysia (Formerly known as Kuala Lumpur Stock Exchange (KLSE)) to include a narrative statement in the annual report the manner in which they have applied the principles and the best practices as prescribed by the Code. They also must identify and offer reasons in the areas of non-compliance, along with the alternative practices that they have adopted.

⁶¹ Special Report on Malaysia. (2010). Evolution of Corporate Governance in Malaysia. *Journal on Corporate Governance in Asia*, 7 (3): 1-44, 20; Zulkafli, A., Abdul Samad, M. F., and Ismai, M. D. (n.d). Corporate governance In Malaysia, available at <http://www.gomalaysiatour.com/administrator/admin/pdf/4dcf82cb5b8dc.pdf> (accessed 7 April 2018, 1.

⁶² Special Report on Malaysia. (2010). Evolution of Corporate Governance in Malaysia. *Journal on Corporate Governance in Asia*, 7 (3): 1-44, 20.

⁶³ Monsod, A. (2010). Malaysian Corporate Governance. *Journal on Corporate Governance in Asia*, 7 (3): 1-44, 1.

⁶⁴ Zulkafli, A., Abdul Samad, M. F., and Ismai, M. D. (n.d). Corporate governance In Malaysia, available at <http://www.gomalaysiatour.com/administrator/admin/pdf/4dcf82cb5b8dc.pdf> (accessed 7 April 2018, 1.

⁶⁵ Ibid.

The other important reforms followed such as that the formulation of a 10-year master plan for the capital markets in 2001, along with the demutualisation of the stock exchange, Bursa Malaysia. The disclosure rules were further amended in 2004. Thereafter, in 2008, a department of corporate governance was established, and additional terms like the ‘corporate surveillance’ and the investigation division of the Bursa Malaysia were introduced for the purpose of implementing and monitoring the corporate governance policies of all the listed companies, which aligned to the corporate governance practices of Malaysia and on par with the international standards.⁶⁶

Earlier debate relating to corporate governance in Malaysia was limited to the agencies that were directly involved in law enforcement like the Kuala Lumpur Stock Exchange (KLSE), Ministry of Finance, Securities Commission (SC) and the Registrar of Company.⁶⁷ The major sources of the corporate governance reform agenda in Malaysia were derived from the MCCG, presented by the Finance committee on the corporate governance, Capital Market Master Plan (CMMP)⁶⁸ presented by the Securities Commission (SC) and the Financial Sector Master Plan (FSMP) by the Bank Negara Malaysia. They offer guidelines regarding the best practices and principles related to the corporate governance, and also provided a direction for the purpose of implementing and charting the future prospects of the corporate governance in Malaysia.⁶⁹

The legislative and the regulatory framework of the corporate governance in Malaysia were based on the SC Act and the then Securities Industry Act of 1983 (presently under the Capital Market and Services Act 2007). The Malaysian Companies Act 2016 was

⁶⁶ Ibid.

⁶⁷ Abidin1, N. Z. and Ahmad, H. N. (2007). Corporate Governance in Malaysia: The Effect of Corporate Reforms and State Business Relation in Malaysia. *Asian Academy of Management Journal*, 12 (1): 23-34, 34.

⁶⁸ It is important to note here that the Malaysia’s Capital Market Masterplan was drafted to guide the development of Malaysia’s Capital Markets during the decade of 2001 to 2010. For the Malaysia’s Capital Market Masterplan to project the economy of Malaysia, it requires RM 930 Billion in the new Capital Expenditures. See Ajit, R. & Yusof, Z. A. (2005). Development of the Capital Market in Malaysia, *Tokyo Club Foundation for Global Studies*, 7.

⁶⁹ Zulkafli, A., Abdul Samad, M. F., and Ismai, M. D. (n.d). Corporate governance In Malaysia, available at <http://www.gomalaysiatour.com/administrator/admin/pdf/4dcf82cb5b8dc.pdf> (accessed 7 April 2018).

introduced which provides provisions for the shareholders to take part and vote in the company meetings and shareholders ballot. The Malaysian Companies Act of 2016 allows shareholders to dismiss the board members any time during their office term.

The revised MCCG 2007 introduced many important changes in the Malaysian corporate governance, which include the definition of the eligibility criteria while appointing directors, board composition and the role played by the nominating committee, etc. The major responsibilities of the corporate governance department of the Bursa Malaysia included: formulation of short-term and long-term governance policies to achieve a higher standard; uplifting the corporate governance ratings at the international level; planning and implementation of appropriate measures to enhance the standards of the corporate governance amongst the listed companies; monitoring the standard of the corporate governance amongst others. Thereafter, the MCCG was again reviewed in 2012 to keep itself relevant and aligned with the internal standards and practices. The 2017 MCCG version, which succeeded the 2012 version, used a novel approach for supporting the internalisation of the corporate governance culture.⁷⁰

THE CURRENT MALAYSIAN CODE ON THE CORPORATE GOVERNANCE 2017

The new MCCG 2017 was sanctioned by the SC, Malaysia and came into effect on 26th April 2017 replacing the MCCG 2012. The new MCCG 2017 contains many principles for the purpose of improving the standards of the corporate governance of the Malaysian companies. The MCCG 2017 introduced the ‘Comprehend, Apply and Report’ (CARE) or the ‘apply or explain an alternative’ process, which is a deviation of the ‘comply or explain’ approach, used by the MCCG 2012.⁷¹ This approach offers a higher degree of flexibility while applying the best practices. Further, the MCCG 2017 is applicable to all the listed Malaysian companies, wherein some activities could be practised by only the ‘Large Companies’, which included the companies on the Bursa Malaysia Top 100 Index or

⁷⁰ Section 2.5 of the MCCG 2017.

⁷¹ Section 2.5 of the MCCG 2017.

companies with an RM2 billion market capitalisation.⁷² Furthermore, the MCCG 2017 encourages many non-listed corporations like the Government-linked Corporations, Small and Medium Enterprises, and the licensed intermediaries to implement the MCCG 2017, accordingly they are improving their transparency, accountability, and sustainability.⁷³ As per this code, the companies have to offer an explicit explanation in their annual reports with regards to the manner in which all activities were conducted, and also present some alternative activities to achieve the Intended Outcome, provide reasons for these alternatives and present an appropriate timeframe for their implementation.⁷⁴ The initial set of companies which are required to report their conformity with the new MCCG 2017 in their annual reports include the companies whose financial year ended on 31st December 2017.

The new MCCG 2017 provides 36 practices which support the 3 principles of broad and effective leadership; an effective auditing, risk management and internal control; and the corporate reporting and a relationship with the stakeholders. During the official release of the MCCG 2017, Tan Sri Ranjit Ajit Singh, Chairman of the Malaysian SC, stated that the new code is a vital component of Malaysia's journey towards the promotion of good corporate governance and for ensuring the resilience and sustainability of the capital market. This new code could act as a compass for the boards who wish to guide their companies in the forward direction and emphasise the relevance of corporate governance. The next section presents the salient features of the MCCG 2017.

HIGHLIGHTS OF THE SILENT FEATURES OF MCCG 2017

Independence of all Boards

In order to increase the independence of the boards, the new MCCG 2017 requires that a minimum of 50% of the board members must be independent directors, and in the case of the Large Companies,

⁷² Section 2.6 of the MCCG 2017.

⁷³ Section 2.7 of the MCCG 2017.

⁷⁴ Section 6 of the MCCG 2017.

the majority of the board members must be independent directors.⁷⁵ The MCGG 2017 requires that the independent director must not serve a term of 9 years.⁷⁶ In addressing the issues relating to the long tenure of the directors, the new MCGG 2017 provides that if a company wishes to retain their independent directors beyond 9 years, it is required to secure the approval of the shareholders, while the retention of the independent directors for a period beyond 12 years requires the shareholder's approval using the 2-tier voting process.⁷⁷ Additionally, for justifying the retention of the independent directors beyond the cumulative term of 9 years, the board must conduct a very intensive review and determine if the 'independence' of the director was impaired.⁷⁸ The results of the review must be disclosed to all shareholders so that they can make informed decisions.

Transparency in the Directors' Remuneration

Previously under the MCGG 2012, the boards were required to establish some transparent and formal remuneration processes and policies for the directors, which must be disclosed in their annual reports. The new MCGG 2017 provides that the company must mention these processes and policies on its website.⁷⁹ Furthermore, the MCGG provides that a detailed disclosure must be provided about the remuneration that has to be offered to all the directors, with respect to the fees, benefits, bonuses, and other emoluments, and also the amount of remuneration that is paid to the Top 5 people in the senior management.⁸⁰ The Malaysian Companies Act 2016 provides that all the fees of the directors and such benefits offered to the directors of the public company (unlisted or listed) must be approved by all shareholders in the general meeting. The disclosure requirements to be made under the MCGG 2017 means that the emphasis on the need to maintain transparency regarding the accountability and remuneration to the shareholders. Also, the Remuneration Committee must consist of only the non-executive directors. A majority of these non-executive directors are independent

⁷⁵ Practice 4.1 of Principle A Board Composition II MCGG 2017.

⁷⁶ Practice 4.2 of Principle A Board Composition II MCGG 2017.

⁷⁷ Practices 4.2 and 4.3 of Principle A Board Composition II MCGG 2017

⁷⁸ Guidance 4.2 of the Principle A Board Composition II MCGG 2017.

⁷⁹ Practice 6.1 of Principle A Remuneration III MCGG 2017.

⁸⁰ Practice 7.1; 7.2; and 7.3 of Principle A Remuneration III MCGG 2017.

directors, who can seek advice from other experts, as needed.⁸¹ The Guidance 6.2 of the Principle A requires that the directors who are shareholders must avoid voting in the general meetings held to approve their remuneration and fees.

Strengthening the Independence of the Audit Committee

The new MCCG 2017 provides that the Audit Committee Chairman must be the Board Chairman.⁸² The Practice 8.2 of the Principle B Effective Audit and Risk Management, Audit Committee MCCG 2017 provides that the Audit Committee should highlight the processes and policies for assessing the objectivity, suitability and the independence of all external auditors. This was recommended to be the “Step Up” practice for a committee, which comprises of only independent directors.⁸³

Risk Management Committee

The new MCCG 2017 provides that the board must develop a Risk Management Committee consisting of independent directors for overseeing the company’s risk management framework, policies and their implementation.⁸⁴ The Practice 9.2 of Principle B Risk Management and Internal Control Framework MCCG 2017 provides that the board must disclose all features regarding the risk management and the internal control framework along with the effectiveness and the sufficiency of the framework.

Participation at the General Meetings

Based on the 2012 code approach, which promoted a dynamic relationship between the company and all shareholders, the new MCCG 2017 further introduced many requirements aimed at improving this relationship, in the following manner;

⁸¹ Guidance 6.2 of Principle A Remuneration III MCCG 2017.

⁸² Practice 8.1 of Principle B Effective Audit and Risk Management, Audit Committee MCCG 2017.

⁸³ Practice 8.4 of Principle B Effective Audit and Risk Management, Audit Committee MCCG 2017.

⁸⁴ Practices 9.1 and 9.3 of Principle B Risk Management and Internal Control Framework MCCG 2017.

- a) Notice of the annual general meeting must be given a minimum of 28 days prior to the meeting date. The 2016 Companies Act necessitates a 21-day notice).⁸⁵
- b) All the directors must attend the general meetings for engaging with their shareholders (Practice 12.2 Part C Integrity in Corporate Reporting and Meaningful Relationship with Stakeholders, Conduct of General Meetings MCCG 2017).
- c) The listed companies, who have a large number of shareholders, conduct meetings in some remote locations for leveraging the technology for facilitating the electronic voting and for encouraging the remote shareholders to participate in the meetings.⁸⁶

Board Diversity

While pursuing the gender diversity agenda, the new MCCG 2017 provides that every company must take some steps to ensure that the women candidates are recruited for the board and Senior Management Positions.⁸⁷ The Guidance 4.5 of the Principle A Board Composition II MCCG 2017 provides that women are to constitute at least 30 percent of the board membership of large companies.

Relationship with the Stakeholders

The new MCCG 2017 provides that the board must maintain transparent, effective and constant communication with all the stakeholders, and all larger companies are required to adopt a more integrated reporting system based on the globally-recognised framework.⁸⁸ Furthermore, the new MCCG 2017 introduced many requirements which help in improving the participation and the engagement of the shareholders with the board members during the general meetings.⁸⁹

⁸⁵ Practice 12.1 Part C Integrity in Corporate Reporting and Meaningful Relationship with Stakeholders, Conduct of General Meetings MCCG 2017.

⁸⁶ Practice 12.3 Part C Integrity in Corporate Reporting and Meaningful Relationship with Stakeholders, Conduct of General Meetings MCCG 2017.

⁸⁷ Guidance 4.4 of the Principle A Board Composition II MCCG 2017.

⁸⁸ Practice 11.1 and 11.2 of Part C Communication with Stakeholders I MCCG 2017.

⁸⁹ Practices 12. 1 to 12.3 of Part C Conduct of General Meetings II MCCG 2017.

A COMPARATIVE STUDY OF THE CODE ON CORPORATE GOVERNANCE IN SAUDI ARABIA AND MALAYSIA

The new Saudi code 2017 and the new MCCG 2017 provide for the establishment of independent board that must consist of a majority of independent directors as board members. Both codes recognised the need for these companies to develop committees for remuneration, auditing, risk management to ensure adequate transparency, accountability and sustainability. Similarly, the Saudi 2017 and the MCCG 2017 codes mandate the board in maintaining the policies related to the information disclosure and state that the board and the audit committee reports must be published on the company website. Both codes state that the company board must disclose the remuneration of all board members and executives, as per the template. The two codes require the companies to maintain appropriate records for a 10-year period.

Though the codes consist some similar provisions, they still differ to a certain extent. The MCCG 2017 code deviated from the conventional process of 'comply or explain' to adopt the 'apply or explain an alternative' approach, known as the 'Comprehend, Apply and Report' (CARE) approach. On the other hand, Saudi Arabia still uses the 'comply or explain' approach. Despite the fact that these codes contain specific provisions to strengthen the relationship between a company and its stakeholders, the new Saudi code 2017 provides some broad provisions that increasing the shareholder rights. The Saudi code 2017 provides explicit and dedicated provisions for these rights.

The new MCCG 2017 provides better processes and rules prescribing the independence of the director by addressing issues relating to the effect of a longer tenure of the directors. The new MCCG 2017 discourages an independent director from having a tenure beyond 9 years. However, if the company wishes to retain a specific director beyond 9 years, the board needs to seek the shareholders' approval. The retention of the independent director for more than 12 years also requires the shareholders' approval using a two-tier voting process.

Irrespective of the consistency of the 2 codes with regards to the strength of the relationships between the shareholders and the

company, the new MCCG 2017 code states that the company must give a 28-day notice to the shareholders for any meeting, compared to 10 days mentioned in the Saudi 2017 code. Finally, with regards to the gender diversity agenda, the MCCG 2017 provides a better standard to improve women participation in the company’s affairs. The Saudi 2017 code does not address the gender issue by prescribing a specific percentage or quota for women with respect to the board or the Senior Management Positions. Table 1 compared the new Saudi code 2017 and the MCCG 2017.

Table 1: Comparison of the Saudi Code 2017 and the MCCG 2017

Saudi Arabia New Code 2017		MCCG 2017
1.	Use of the Comply or Explain Approach	Use of the Comprehend, Apply and Report (CARE) approach
2.	Offer explicit, dedicated, and broad provisions about the shareholders’ rights	Offer fewer provisions regarding the shareholders’ rights
3.	Do not offer any provisions regarding the process to be implemented if the company wishes to retain a director after 9 years	Offer a procedure to be followed if the company wishes to retain some director for more than 9 years
4.	Offers a 10-day notice period before any meeting	Offers a 28-day notice period before any meeting
5.	Offers no women quota or percentage for recruiting women in the board or for any senior management position	Accepts gender diversity agenda and offers better standard with regards to the participation of women in the company affairs

CONCLUSION

This paper discusses the corporate governance frameworks under the Saudi Arabia new code 2017 and the MCCG 2017. The two legal

frameworks have their similarities and differences. The study finds that the MCCG 2017 should provide more dedicated and explicit provisions with regards to the shareholders' rights as provided for under the Saudi code 2017. The stipulated rights are meant to safeguard the interests of all shareholders and in consequence they are encouraging external investments into the companies. At the same time, Saudi Arabia should also provide certain clauses as available under MCCG 2017 with regards to the independent directors who served for more than 9 and 12 years, respectively, in order to improve the independence of the company's board and ensuring an impartial decision-making. Saudi Arabia Code 2017 should also provide that the company to give a notice of 28 days before any general meeting, compared to a 10-day notice as is presently, to be equal to the MCCG 2017. Similar to that under the MCCG 2017, Saudi Arabia should encourage the companies to increase the participation and recruitment of women in the board and at senior management positions, thereby improving gender diversity, as already mentioned in the MCCG 2017.

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