

# **Alfaisal University College of Business**

**1<sup>st</sup> Annual Corporate Governance Conference:  
Importance of Good Corporate Governance for 2030 Vision**

**Corporate Governance Index: Description,  
Methodology, and Company Ranking**

**17 May 2017**

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**Welcome Message from  
HE Dr. Mohammed Bin Ali Alhayaza  
President of Alfaisal University**

Dear participants: It is my great pleasure to welcome you to Alfaisal University. You are with us to witness such a historic evening where the First Annual Corporate Governance Conference will be held under the title, “**Importance of Good Corporate for 2030 Vision.**”

Alfaisal University continues to be innovative in establishing programs and projects that serve the Kingdom of Saudi Arabia and its citizens. These programs often venture into the future and train its students to welcome the change and benefit from it. The initiative of College of Business (CoB) in establishing the first Corporate Governance Research Center (CGRC) in the Kingdom is an example. It is used to institutionalize the CG education and practices, and be of service to the public and private sectors. It received the endorsement of Saudi government agencies that deal with financial regulations, commerce and investment. It is coming at an opportune time for the country as the Kingdom is embarking on fundamental changes in its economy.

The Corporate Governance Team at CoB has been hard at work in putting this short conference together. In addition to releasing the CG process and index report for the companies traded on the Saudi Financial market, it is organizing discussions involving CG experts from the private and government sectors that connect CG to the realization of 2030 Vision. I hope you will enjoy these discussions. With that I wish to extend my sincere thanks to the organizers and speakers. While you are at Alfaisal University I hope you will have a great time.

**Welcome Message from  
Dr. Bajis Dodin, Dean  
College of Business  
Alfaisal University**

It is with great enthusiasm that I welcome you to Alfaisal University and to host the first annual mini conference on the “Importance of Good Corporate Governance for 2030 Vision”. Alfaisal College of Business with cooperation from SAGIA, CMA and MCI and strong support from Alfaisal University Administration has been working on establishing a Corporate Governance Research Center (CGRC). It is to be The Center for CG education and policy making. It started by establishing a CG Team and a process that was used to calculate of the CG Index for the companies traded on the Saudi Financial Market. The process builds on the CG principles developed by CMA and OECD. It also benefitted from the observations of many colleagues in the public and private sectors, and from the experiences of international experts on CG. I hope you will find in this conference something of lasting value.

In this conference we will first share with you the CG process and how it was implemented. Then you will hear from a world renowned expert on the Value of Good CG for the Investors and the Economy. These will be followed by two panel discussions: The first deals with the role of related government agencies in developing policy and CG principles that suit the Saudi and GCC environment and help the realization of Vision 2030; where the second panel focusses on the impact of practicing good CG in the private sector.

The conference is being held at an opportune time as the Kingdom of Saudi Arabia is embarking on huge change in its economy. We hope it will be an annual event that will attract the attention and participation of those interested in CG in the public and private sectors. It will be the focal point for the presentation and dissemination of CG research and development.

I wish to thank the support of Alfaisal University Administration and its President Dr. Mohammed Alhayaza, and the cooperation of SAGIA, CMA and MCI. I also wish to thank the CG Team of CoB and its international consultants Dr. Stephen Davis of Harvard University and Kobirate of Turkey. I hope you will enjoy all the segments of the conference.

## Part I. Corporate Governance: Definition, Importance & Measurement

### Introduction

Good governance is the key for Saudi companies in the increasingly global competitive market; particularly, when family-run businesses are in the transition to be integrated into the global market. Good governance provides assurance for long-term profitability and sustainability. It gives a positive signal to outside investors. Therefore, it is absolutely essential to develop sound corporate governance (CG) assessment tool to monitor and promote good governance among Saudi corporations. We believe a reliable CG index will raise Saudi Arabia's overall corporate governance standards and will provide possible financial and investment benefits as a result of making governance improvements. Because of these benefits, many countries around the world have set up CGIs over the past decade. We benefited from their experiences to develop an efficient CGI for Saudi companies. The index is expected to provide great help in monitoring and promoting good governance among Saudi corporations. Below, we provide what, why, and how of corporate governance before introducing our CG index project.

#### 1. What is corporate governance?

"Corporate governance involves a set of relationships between a company's management, its board, its shareholders and other stakeholders. Corporate governance also provides the structure through which the objectives of the company are set, and the means of attaining those objectives and monitoring performance are determined." **The Organization for Economic Co-operation and Development (OECD) (2015), G20/OECD Principles of Corporate Governance, OECD Publishing**

"Corporate governance is concerned with holding the balance between economic and social goals and between individual and communal goals. The governance framework is there to encourage the efficient use of resources and equally to require accountability for the stewardship of those resources. The aim is to align as nearly as possible the interests of individuals, corporations and society." **(Sir Adrian Cadbury, UK, Commission Report: Corporate Governance 1992)**

#### 2. Why is it important to have good corporate governance?

"Effective corporate governance ensures that long-term strategic objectives and plans are established, and that the proper management and management structure are in place to achieve those objectives, while at the same time making sure that the structure functions to maintain the corporation's integrity, reputation, and accountability to its relevant constituencies." **Director's Monthly**

"Corporate governance is not only a European challenge but an international one, because companies ultimately compete for financial resources on the global market. And corporate governance practices, which are strongly linked to local legal and regulatory environments, have a strong influence on strategic management style, as well as on decision-making at board, CEO and middle management levels. Thus, if organization follows strategy, strategy follows governance." **European Business Forum**

"The quality of the company's board has now become an important evaluation factor for institutional investors." **Russel Reynolds**

“Whenever an institution malfunctions as consistently as boards of directors have in nearly every major fiasco of the last forty or fifty years it is futile to blame men. It is the institution that malfunctions.” **Peter Drucker**

“If a few rotten apples can spoil the barrel, I think we have to look at the nature of the barrel, not just the apples. Organizational design, structure, and culture do play a role and almost always have in corporate scandals. Companies that get into trouble often do so because of minimal internal connections between many parts of the organization. With deficient information and knowledge, you can’t put all the pieces together or understand when something might be going wrong.” **R. M. Kanter**

### 3. **How** do we evaluate corporate governance?

We evaluate good corporate governance by creating an index which assesses companies in terms of their compliance to the related governance rules in the country and best governance practice around the world. Those rules are expected to promote equal treatment of shareholders; ensure transparency through constant flow of relevant information related shareholders and stakeholders; provide effective structure to hold decision makers’ accountability for their business decisions; and ensure responsible acts in terms of complying with related laws and regulations. The ultimate benefit of good governance is to develop efficient and effective rules and institutions for higher productivity and long-term economic success. Companies are expected to have strong-will, mechanism, and institutions to implement CG rules and report the outcome. Particularly, good governance offers solution for principle-agent problems and conflict of interest issues aligning the goals of everyone toward long-term corporate growth and profitability.

A major 2013 World Bank report<sup>1</sup> on developing CG index recommends the following eight steps to come up with an efficient CG index:

- 1) Use a wide initial consultation
- 2) Define objective of the index
- 3) Select the index approach
- 4) Customize the governance criteria for the country when adopting international standards
- 5) Build a transparent and credible evaluation process
- 6) Achieve maximum possible disclosure
- 7) Effectively monitor the index criteria
- 8) Develop the index.

We have followed the recommendation above in developing CGI for Saudi companies. We used wide range of consultation to make sure that we come up with best measurable criteria to evaluate corporate governance policy and practices. We collaborated with international consultants and worked with local partners to establish index with proper categories and variables. With this index, we aim to provide data-based independent guidance to Saudi companies helping them to adopt good governance principles. We believe that the adoption

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<sup>1</sup> Raising the Bar on Corporate Governance: A study of eight stock exchange indices, World Bank, June 2013.

of those principles would help companies to make better decisions and resolve challenges that could emerge between corporate executives, shareholders, and stakeholders in the course of doing business.

**Part II. Corporate Governance Index (CGI) Project Overview**

**1. Alfaisal University Corporate Governance Research Center (CGRC)**

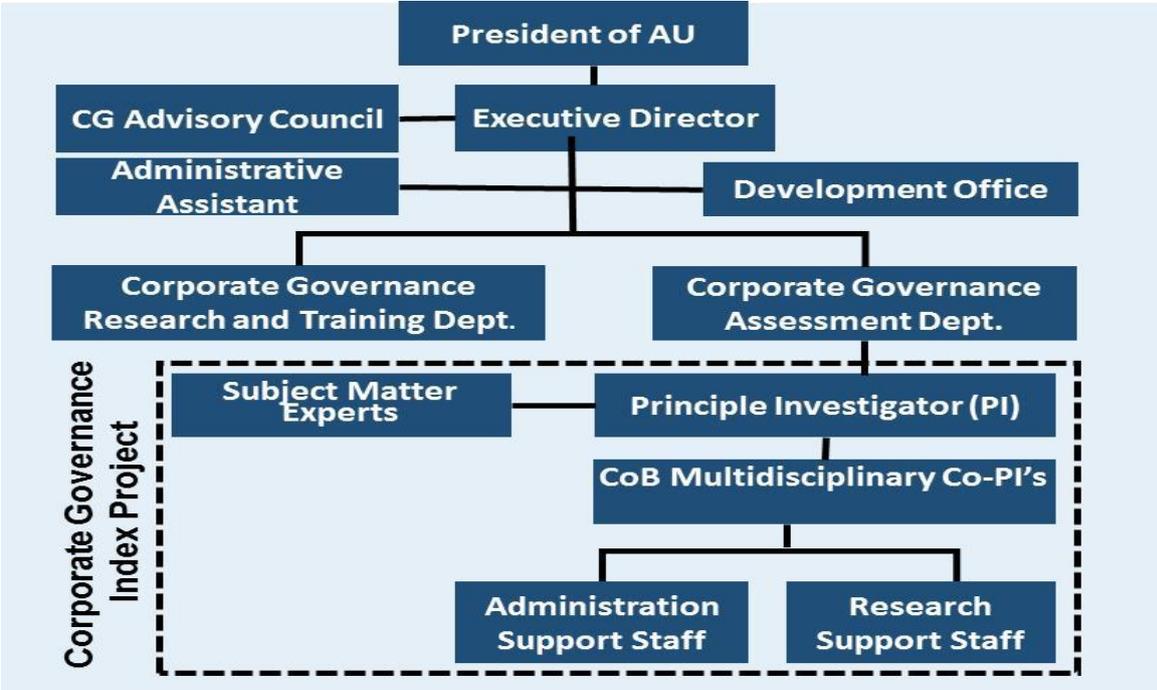
**Vision:**

We aspire for the CG Research Center to be the leading center in the Gulf Cooperation Council (GCC) region for impactful research on CG and for promoting best CG policies and practices.

**Mission:**

The mission of the center is to provide reliable and independent CG policies and practices through quality research and education that serves the GCC region and its economies.

The CGRC is in the process of approval. It has been approved by the College of Business; Council of Deans at Alfaisal University (AU), by Alfaisal University Council, and by AU Board of Trustees. It is expected to be fully operational by January 2019. The chart below shows the structure of the center once it is fully functional:



**2. CGI Project Overview**

Corporate Governance Office at the College of Business of Alfaisal University is undertaking a major study to develop a Corporate Governance Index (CGI) for companies trading on the Saudi Financial Market for the fiscal year of 2015. The project is partially funded by the Saudi Arabian General Investment Authority (SAGIA) and encouraged by Capital Market Authority (CMA).

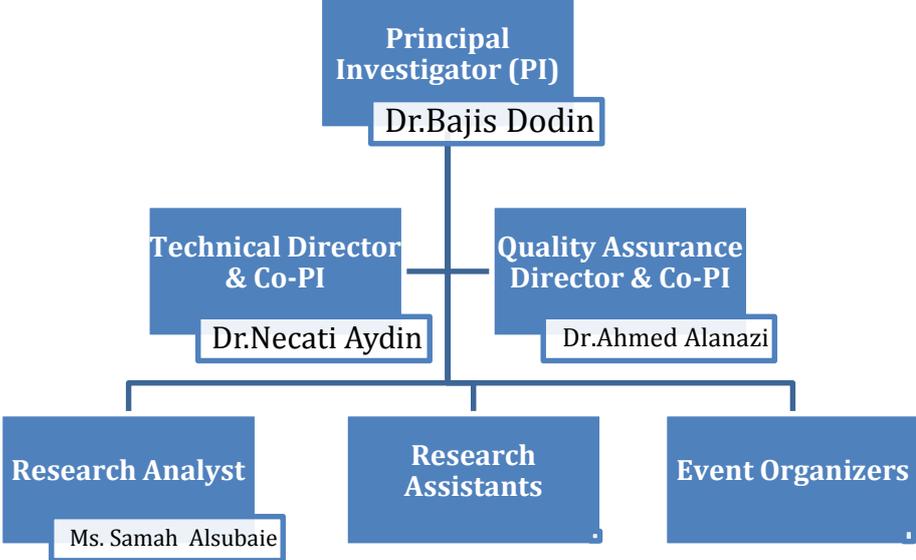
A dedicated team from College of Business at Alfaisal University is working with support from well-experienced consultants to develop this index. The CGI is based solely on good CG principles set by CMA and The Organization for Economic Co-operation and Development

(OECD). The goal is to rank the publicly traded companies in the Saudi market according to their compliance with those principles and performance.

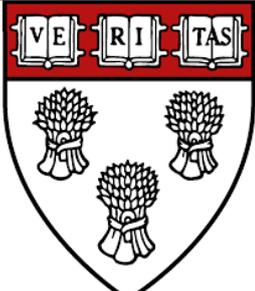
The CGI project is of three years duration. The first year, which ends in May 2017, deals with the calculations of CGI for the year 2015 of companies traded on the Saudi Financial market. The second year which is expected to end in February 2018 is expected to deal with the calculations of the CGI for companies traded in the GCC markets. Then the third year that is expected to end in January 2019 as it releases the CGI for major companies traded in the GCC markets and completes the formation of the Corporate Governance Research Center.

**3. Project Team**

**a. Alfaisal University CGI Team**

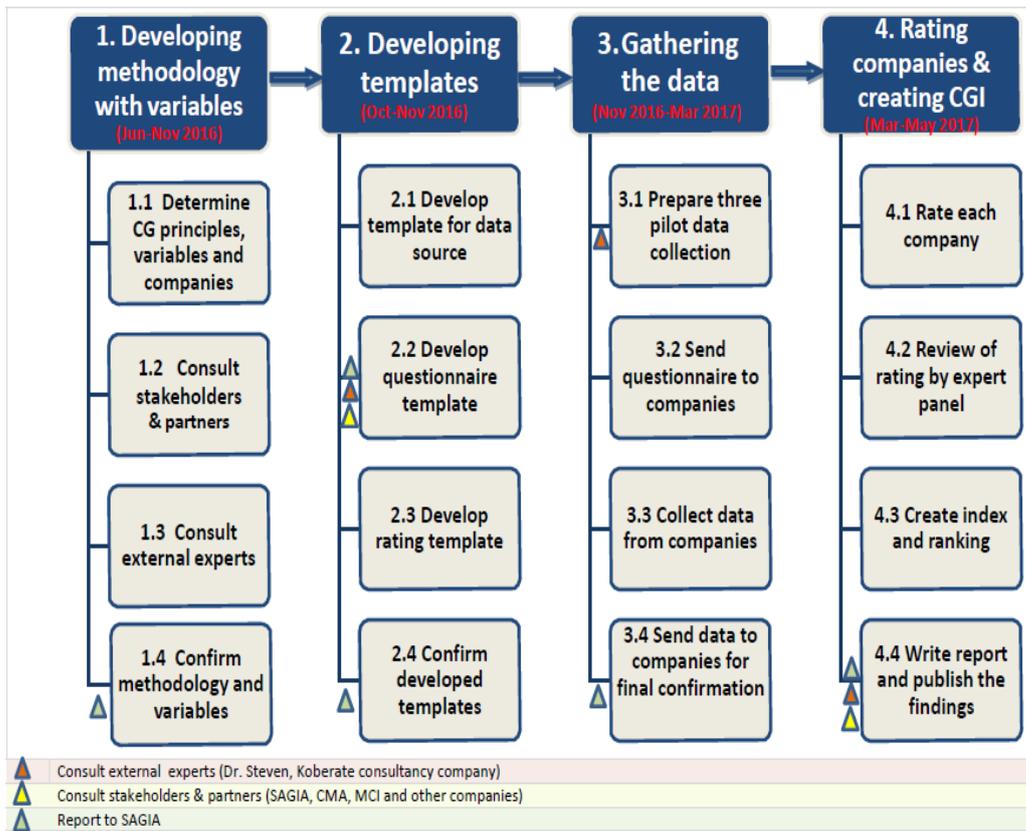


**b. External Consultants**

<p><b>1) Dr. Stephen Davis</b></p> <ul style="list-style-type: none"> <li>• Associate Director and Senior Fellow, Programs on Corporate Governance and Institutional Investors at Harvard Law School</li> <li>• One of the architects of today’s global corporate governance framework, based at Harvard Law School.</li> </ul>	 <p><b>Harvard University Program on CG</b></p>
<p><b>2) Kobirate Consulting Firm</b></p> <ul style="list-style-type: none"> <li>• Has been doing CG rating since 2008</li> <li>• Has developed a unique software for CG index</li> <li>• Has rated nearly 30% of Borsa Istanbul (BIST) Corporate Governance Index Companies, more than 50 Corporate Issuers and made more than 1000 Companies’ scoring processes.</li> </ul>	 <p><b>Kobirate Consulting Firm, Istanbul, Turkey</b></p>

#### 4. Project Flowchart and Timeline

## Project Flowchart and Timeline



## 5. CGI Methodology

### a. Process of Developing CGI Categories and Variables

1. Explored world-wide CGI practices

2. Collaborated with world-wide renowned Consultants

3. Engaged with local partners (SAGIA, CMA, SAMA, MCI)

4. Determined CG principles for the index based on CMA and OECD CG principles

5. Established four CGI categories with 117 variables through consultation

6. Developed CGI questions based on selected CG principles through consultation

### b. CGI Categories and Variables (117)

#### 1) The Board of Directors (39 variables)

Variables by Category	Number of Variables
Main Functions of the Board of Directors	13
Responsibilities of the Board	4
Formation of the Board	7
Qualifications of Independent Board Members	9
Committees Formed within the Structure of the Board of Directors	2
Nomination and Remuneration Committee	2
Meetings of the Board	1
Remuneration and Indemnification of Board Members	1

#### 2) Shareholders (30 variables)

Variables by Category	Number of Variables
Facilitation of Shareholders' Exercise of Rights and Access to Information	6
Investor Relations	3
Shareholders' Rights Related to the General Assembly	13
Voting and Minority Rights	3
Dividend Rights of Shareholders	4
Transfer of Shares	1

#### 3) Public Disclosure and Transparency (35 variables)

Variables by Category	Number of Variables
Policy and procedure	15
Board of Directors' Report	20

#### 4) Stakeholders (13 variables)

Variables by Category	Number of Variables
Stakeholders	13

### c. Company Selection for CGI and Company List

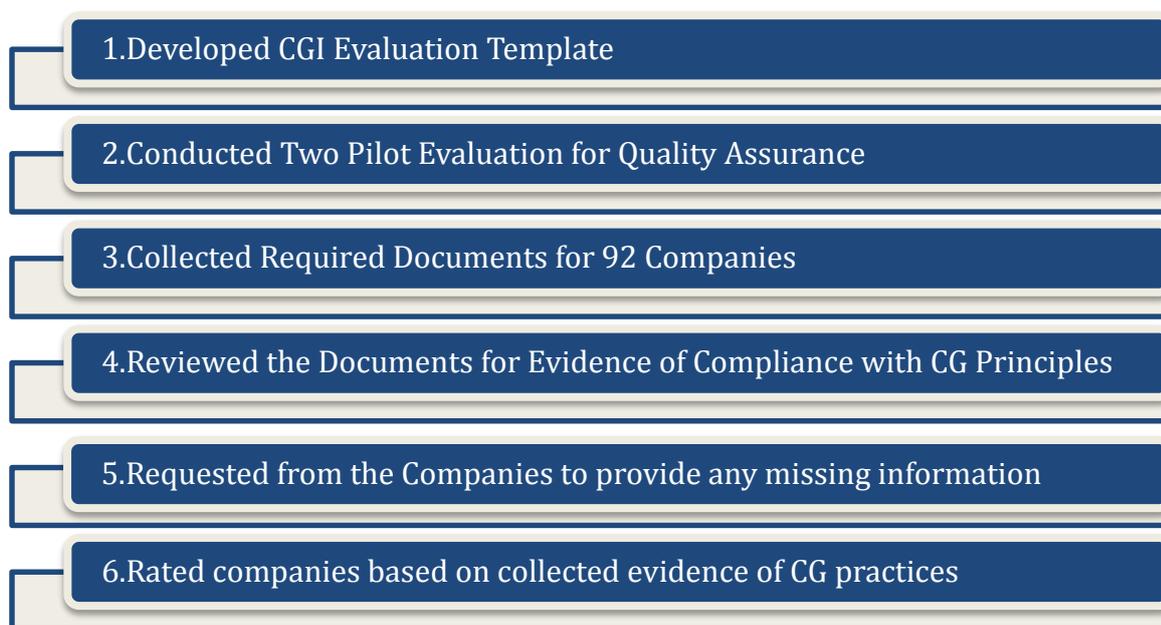
We used the market capitalization as the key determining criteria. The median market value was set as the threshold. The companies that have median market of value of 2 billion riyals were included. The

second criterion was that the company has to be listed in the market for a minimum of three years. This is to ensure enough time for the transition of the company from private ownership into public ownership. In total, 87 companies meet the criteria. Per suggestion from CMA, we also added five companies from those, which do not meet the criteria: The final list includes one red firm, one orange, one yellow, one from media sector that was excluded entirely, and one new firm. The 92 companies, which made to the list collectively, have a market value about SAR1.8 trillion which represents 95% of the total Saudi market value. We used the new Tadawul sectors classifications.

### List of Companies by Sector

	<b>Sector</b>	<b>Number of companies</b>	<b>Number of qualified firms</b>
1	Energy	4	3
2	Materials	42	25
3	Capital goods	15	5
4	Commercial and professional services	2	1
5	Transportation	4	3
6	Consumer durables and apparel	5	1
7	Consumer services	6	3
8	Media	2	1
9	Retailing	6	4
10	Food and staples retailing	4	2
11	Food and beverages	12	6
12	Health care equipment and services	5	4
13	Pharmacy, Biotech and life science	1	1
14	Banks	12	12
15	Diversified financials	4	2
16	Insurance	35	5
17	Telecommunication services	4	3
18	Utilities	2	2
19	Real estate management and development	10	9
	<b>Total</b>	<b>175</b>	<b>92</b>

## 6. Company Evaluation and Rating Process



## 7. CGI Quality Assurance Process

### a. Internal Quality Assurance



### b. External Quality Assurance

Review Items	Consultants	Feedback Requested
CGI Variables and Categories CGI Rating Methodology CGI Company Selection Criteria CGI Pilot Evaluation	Dr. Stephen Davis & Kobirate Consultant Team	SAGIA, CMA, SAMA, and MCI

## 8. Rating Methodology and Scale

The corporate governance assessment is based on 117 measures within four categories. Each category is evaluated over 100 points. The final CG score is the weighted average of four

categories over 100 points. The CG score reveals the compliance of companies to good corporate governance principles which are determined by CMA and OECD. The four categories and their weight on the final CG score are as follows<sup>2</sup>:

- Board of Directors and Executive Management (35%)
- Shareholders’ Rights and General Assembly (25%)
- Public Disclosure and Transparency (30%)
- Stakeholders (10%)

The lowest cumulative CG score is zero which means no compliance to good corporate governance principles measured through 117 variables. The highest cumulative CG score is 100 which mean 100% compliance with the assessed principles. The first table below provides rating methodology for all categories based on the compliance to CG principles while the second table shows CG rating scale:

Categories	Variables	Earned Points			Cat. Total	Weight	C. Total
		Yes	Partial	No			
	#						
BoD (m.) <sup>3</sup>	14	0.5	0.25	0	100	.35	100
BoD (v.)	25	1	0.5	0			
SHR (m.)	0	NA	NA	NA	100	.25	
SHR (v.)	30	1	0.5	0			
PD (m.)	13	0.5	0.25	0	100	.30	
PD (v.)	22	1	0.5	0			
STR(m.)	0	NA	NA	NA	100	.10	
STR(v.)	13	1	0.5	0			

BoD: Board of Directors; SHR: Shareholder rights; PD: Public disclosure; STR: Stakeholder rights; m: mandatory compliance; v: voluntary compliance; Cat: categorical; C: cumulative (normalized)

**CGI Rating Scale**

Score	Letter Grade	Description
90-100	A	Excellent
80-89	B	Very good
70-79	C	Good
60-69	D	Fair
Below 60	F	Very weak

<sup>2</sup> The weight of sub-categories is determined based on their relative importance, number of criteria, empirical evidence, and international practices.

<sup>3</sup> Following CMA recommendation, we give more weight to voluntary CG principles. A company gains half point if a CG principle is mandatory while full point if it is voluntary.

**Part III: Executive Summary of CG Ranking**

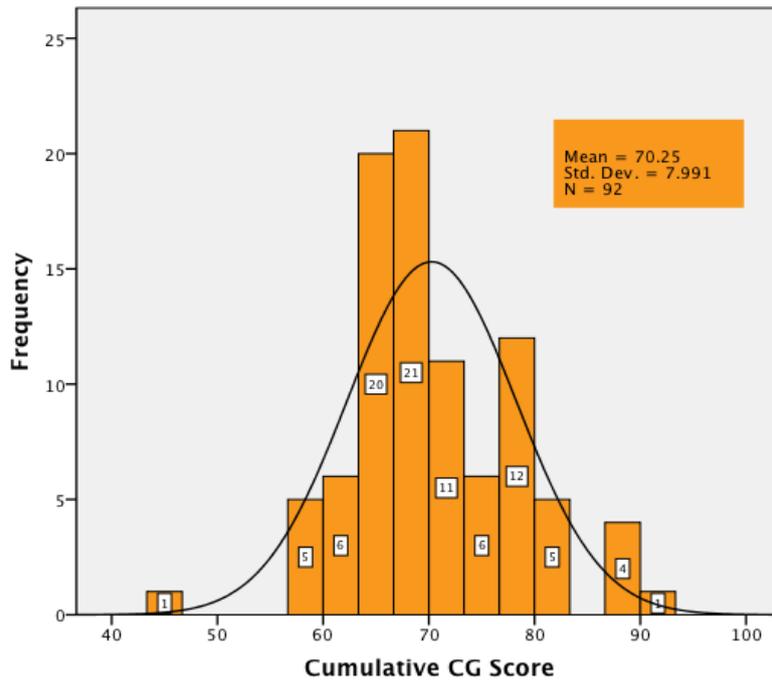
**A) Overall Findings**

The overall CG score is a composite score of four categories based on the weight stated before. The table below shows the mean, median, standard deviation, minimum score, maximum score, and percentiles statistics for the assessed companies. The cumulative CG scores range from 46 points to 92 points with a mean of 70 and standard deviation of 8. This shows that companies vary significantly in terms of their CG practices. While the half of companies scored 70 or above the other half scored less than 70. This means that overall companies are doing fine in terms of corporate governance even though they have significant room for the improvement. As shown in the frequency distribution graphs below, the scores for subcategories reveal that companies are particularly doing well in terms of the CG principles related to board of directors and shareholders’ rights. However, they need great improvement in the areas of public disclosure and transparency, and stakeholders. **(Please note that the full list of company ratings will be available on our Corporate Governance Center’s website a day after the conference.)**

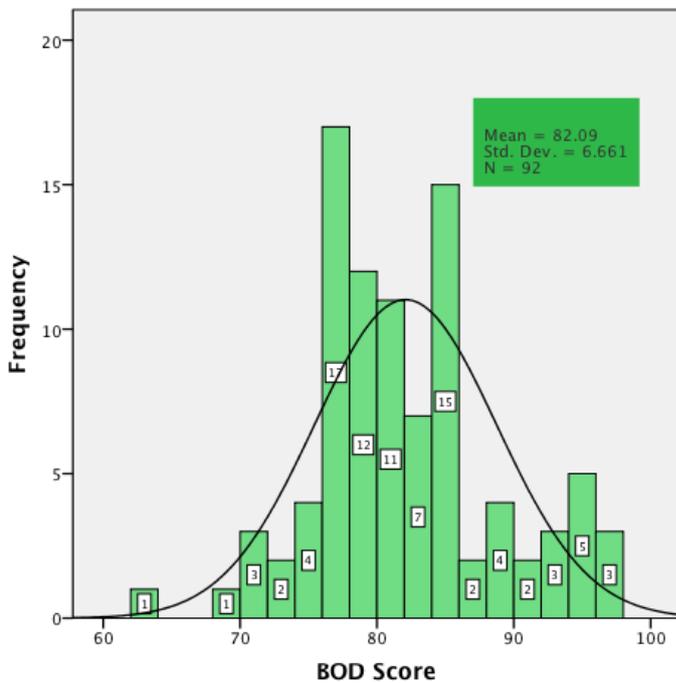
**Table 1. Summary Statistics of CG Assessment**

		<b>Cumulative CG Score</b>	<b>BOD Score</b>	<b>Shareholders Score</b>	<b>Public Dis. and Tran. Score</b>	<b>Stakeholders Score</b>
N		92	92	92	92	92
Mean		70	82	81	59	32
Median		69	81	83	58	31
Std. Deviation		8	7	11	13	17
Range		46	33	70	60	81
Minimum		46	63	28	30	8
Maximum		92	97	98	89	88
Percentiles	10	61	75	72	43	12
	20	64	78	77	47	15
	30	65	78	78	53	23
	40	67	79	80	54	23
	50	69	81	83	58	31
	60	71	83	85	61	35
	70	74	84	85	67	38
	80	78	87	88	70	46
	90	80	93	92	75	54

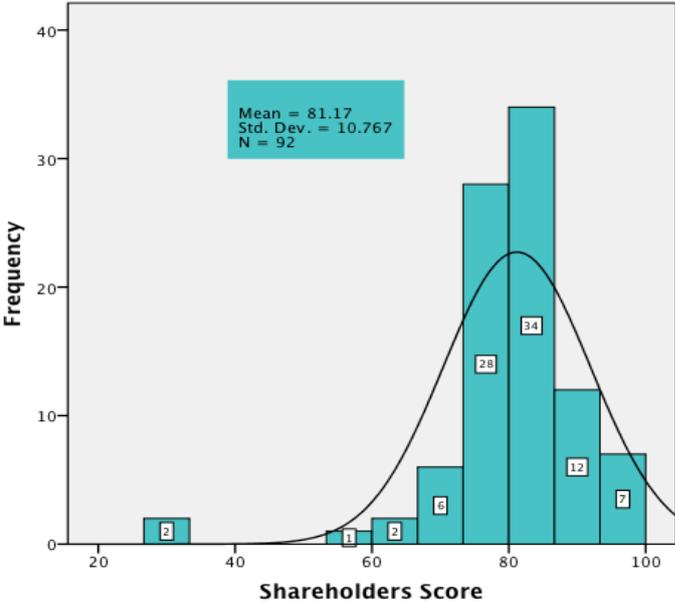
**Figure 1. Cumulative CG Score Distribution**



**Figure 2. Board of Directors (BOD) Score Distribution**



**Figure 3. Shareholder Rights Score Distribution**



**Figure 4. Public Disclosure and Transparency Score Distribution**

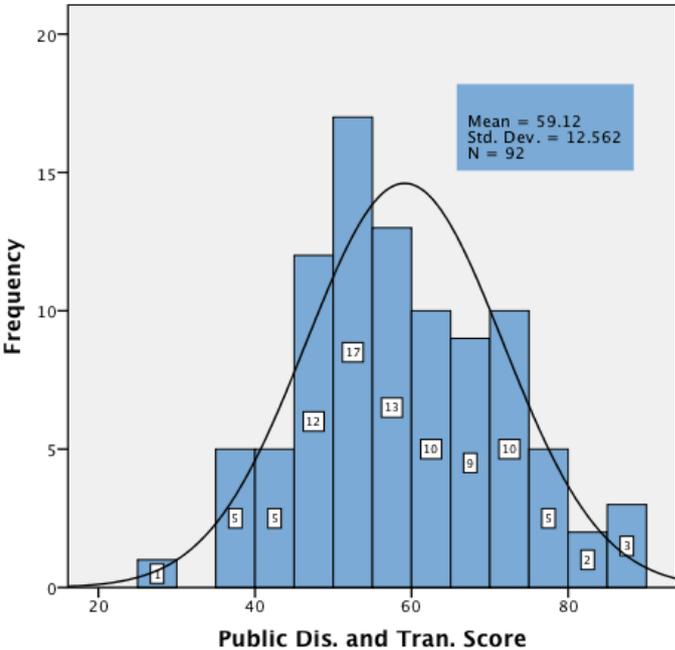
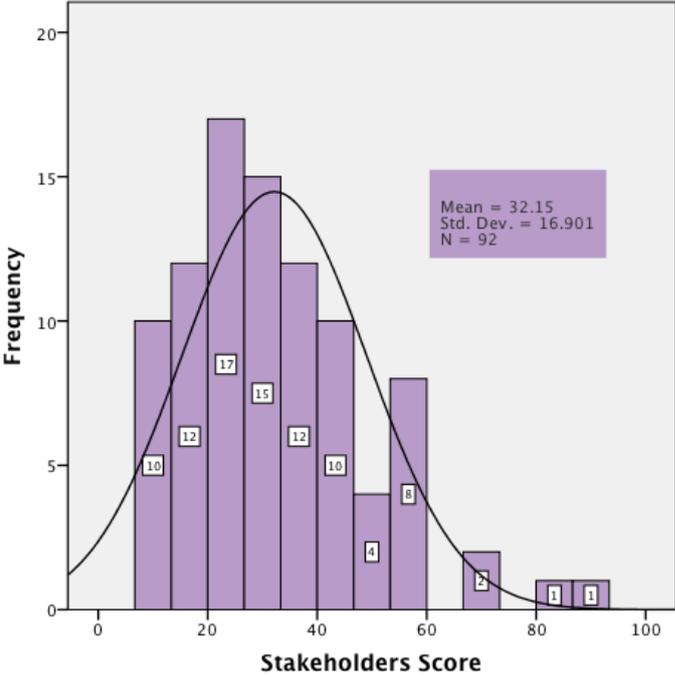


Figure 5. Stakeholders Score Distribution



## **B) Overall Strengths and Weaknesses of CG within Four Categories**

The CG score reflects how well companies follow the CMA corporate governance principles as well as relevant international principles related to board of directors, shareholders rights, public disclosure and transparency, and stakeholders rights. The first year assessment indicates that internal control systems have been established. The corporate governance systems work well overall although they need improvements. Rights of shareholders are treated fairly. Public disclosure and transparency activities are conducted at high level. Rights of stakeholders are treated fairly. The structure and working conditions of board of directors are in compliance with corporate governance principles. Our assessment based on publicly available documents related to the shareholders rights revealed both strengths and weaknesses of the companies in regard to the corporate governance practices.

The detail learned lessons regarding both strengths and weaknesses of the companies are discussed below within the four categories of corporate governance principles.

### **1) Board of Directors (BOD)**

We used 39 variables to assess companies in terms of their compliance to the principles related to the Board of Directors. For the scoring of each variable, we collected evidence from publicly available documents to assess practices in respect to relevant corporate governance principles. The strengths and weaknesses of the companies in the area of board of directors are discussed below.

The mean score for BOD part is 82 (out of 100) with standard deviation of 7 as shown in Table 1. This means that the companies did score B on average in terms of their compliance to the principles related to BOD. The BOD score is the highest among the four areas of the assessment. The review of publicly available documents shows that **most of the companies** in the study accomplished the followings in the fiscal year of 2015:

- Board of Directors has prepared a comprehensive strategy and business plan for the company; it has the explicit responsibility to guide, review and approve corporate strategy.
- Board of Directors undertakes regular assessments of its own performance.
- Board of Directors has established internal control systems and determined supervision rules for them.
- Board of Directors has adopted a “Conflict of Interest” policy covering board members and related party transactions.
- Board of Directors has prepared a Corporate Governance Code for the company.
- There are specific and explicit policies, standards and procedures in the Articles of Association about formation of the Board of Directors, election of its members and its working principles.
- The policies, standards and procedures about formation of the Board of Directors, election of its members and its working principles have been presented for the approval of General Assembly.
- Powers, duties and responsibilities of Board of Directors are described by the Articles of Association in a clearly separated fashion from powers belonging to General Assembly.
- Board of Directors has prepared an orientation procedure for all members, starting with non – executive members, in order to help them learn about company’s business, particularly financial and legal aspects of it.

- Board of Directors complies with the rule which states that, unless authorized to do so by the Articles of Association, it can't borrow for a term of more than 3 years, it can't sell or mortgage company's estates or cancel its debts.
- Board of Directors has a membership structure, which is in compliance with corporate governance principles.
- The Articles of Association specifies number of Board members; it states that a single term of service on the Board of Directors is 3 years maximum.
- Chair of the Board of Directors is a different individual from the CEO or General Manager.
- Article of Association specifies situations, which would lead to termination of board membership
- There is a provision in the Articles of Association stating that a corporate entity with the right to appoint a representative to the board cannot vote for other board members.
- Committees along its working principles for Audit, Nomination and Remuneration have been established in order for the board of directors to fulfill its duties efficiently.
- Remuneration Committee is composed entirely of non-executives; Articles of Association include criteria for remuneration of members of Board of Directors.
- Board of Directors holds its ordinary meetings upon request of chairperson.

## 2) Shareholders

We used 30 variables to assess companies in terms of their compliance to the principles related to the shareholders rights. Again the assessment based on publicly available documents related to the shareholders rights revealed both strengths and weaknesses of the companies as discussed below.

The mean score for the shareholders rights part is 81 with the standard deviation of 11 as shown in Table 1. Even though the score is quite close to that of BOD, it has relatively high standard deviation which indicates bigger variation among companies. Hence, some companies need improvements in the shareholders' rights. The score means that the companies are graded B on average in terms of their compliance to the principles related to the shareholders' rights. The review of publicly available documents shows that **most of the companies** in the study accomplished the followings in the fiscal year of 2015:

- The companies specify the procedures and measures to ensure shareholders' exercise of their legal rights in its articles of association
- All shares that make the company's capital are allowed to use all rights of being shareholder in an equal and fair manner; shareholders who own all shares are entitled to ask questions and to have access to information without having any prejudices against Company's interests.
- The companies maintain and regularly update a comprehensive website along a separate section on corporate governance on their website and in their annual report to shareholders.
- The companies produce their annual report in English as well as Arabic.
- The companies have an investor relations department. The name and contact information of the director of this department is disclosed to public.

- There is a separate section for investor relations in the corporate website.
- The companies hold a General Assembly meeting at least once a year or within 6 months after completion of its financial year
- The auditor has the right to summon General Assembly to meeting.
- Shareholders who represent at least 5 % of company capital have the right to summon General Assembly to meeting.
- The companies inform shareholders about the date, place and agenda of General Assembly at least 10 days before the meeting.
- The companies publish its General Assembly meeting invitation on the corporate website and on the Tadawul website.
- Shareholders are provided with the opportunity to vote by proxy at the General Assembly
- Shareholders are informed about meeting rules before the General Assembly.
- There are provisions in the Articles of Association and internal procedures to ensure choosing the most convenient place and time in order to facilitate participation of maximum number of shareholders to the General Assembly
- Shareholders are given the right to pose questions related to agenda items to Board members and representatives of external auditor at the General Assembly?
- Sufficient information is given to shareholders before the meeting about the items of agenda in order to make them informed enough to make a decision.
- All owners of shares comprising the company's capital have the right to attend General Assembly meetings and vote on resolutions there.
- The company applies no restrictions on the voting right.
- Cumulative voting is used at the General Assembly for voting on board member candidates.
- Board of Directors has prepared a dividend policy that protects the interests of the shareholders and company; Board of Directors' annual report includes dividend policy.
- The amount of dividend to be distributed has been approved by the General Assembly; the companies put its dividend policy to a vote by shareholders in the General Assembly
- The companies give shareholders the right to transfer their shares whenever they want.

### 3) **Public Disclosure and Transparency**

We used 35 variables to assess companies in terms of their compliance to the principles related to the public disclosure and transparency. The mean score for the public disclosure and transparency is 59 with the standard deviation of 13 as shown in Table 1. The average score clearly revealed that companies need major improvement this area of corporate governance. The score shows that most of the companies are failing to follow the recommended principles. Only thirty percent of companies scored C or above while the rest received a lower score. The small percentage of companies which scored high accomplished the followings in the fiscal year of 2015:

- They have prepared disclosure policy for public disclosures.

- They disclose shareholders structure on its website, including a list of largest equity owners.
- They publish Company's Articles of Association on their corporate website
- Material event disclosures are disclosed to shareholders and the public on the corporate website.
- Company's annual reports and financial statements are published on the corporate website.
- Corporate website has agendas, attendants and minutes of general assembly meetings.
- Dividend policy is published on the corporate website.
- Remuneration policy is published on the corporate website.
- The annual report includes Board Members' CV's and CEO succession plan.
- The Big Four accounting firms are hired to audit financial statements and accounting systems.

#### 4) **Stakeholders**

We used 13 variables to assess companies in terms of their compliance to the principles related to the stakeholders. The mean score for this category of corporate governance is 32 with the standard deviation of 17 as shown in Table 1. It is the lowest score within all categories. That is because all of those principles are voluntary. Some of them were not even stated in the CMA principles. We adopted them from relevant international (OECD) principles. Limited number of companies in our study scored B which shows that those exemplary companies accomplished the followings in the fiscal year of 2015 and can be used as examples for the other companies:

- They have prepared training and development policies for their employees.
- They have a policy of conducting periodic surveys of employees to test for morale, attitude, and confidence in management
- They have established mechanisms to solve conflicts between it and stakeholders or to solve complaints.
- They have corporate social responsibility policies and active projects.
- They ensure independent verification of its product / service quality.
- They have performance evaluation and rewarding criteria for its employees.

#### **C) Sectoral Analysis of Corporate Governance Indices**

Given the limited number of companies traded on the Saudi Financial Market for some sectors, we reduced the number of sectors from 19 to 12 by merging the relevant ones together. Table 2 and the following graphs (Figures 6-10) show the sectoral comparison for cumulative CGI scores and sub-categories.

The sectoral analysis reveals that the commercial and retailing sector has the highest cumulative CG score followed by the following sectors: energy and utilities; food and beverages & food & staples retailing; telecom & media; and banks & diversified financials. The real estate development and transportation sectors scored the lowest. It is important to note that the highest score is 82/100 which means that all sectors have long way to go to reach excellence in corporate governance. The lowest CG score is 65 out of 100 which might barely be considered as passing grade.

The CG score by categories reveal that generally all sectors are doing relatively well in terms of their practices related to Board of Directors and Shareholder's rights. However, they have relatively poor

performance in the areas of Public Disclosure and Transparency, and Stakeholders’ rights. It seems like companies generally follow the mandatory principles, but ignore advisory ones. Particularly, in the area of Stakeholders’ Rights, almost all principles are advisory. Thus, we see the lowest adherence to those principles. The sectoral performance within each category varies as well. For Board of Directors and Shareholders’ rights, all sectors except commercial and retailing sectors scored quite similar. In the area of Public Disclosure and Transparency, half of the sectors scored 19 and above out of 30 points while the other half scored below 17/30. In the area of Stakeholder’s Rights, only five sectors scored 3 to 5 out of 10.

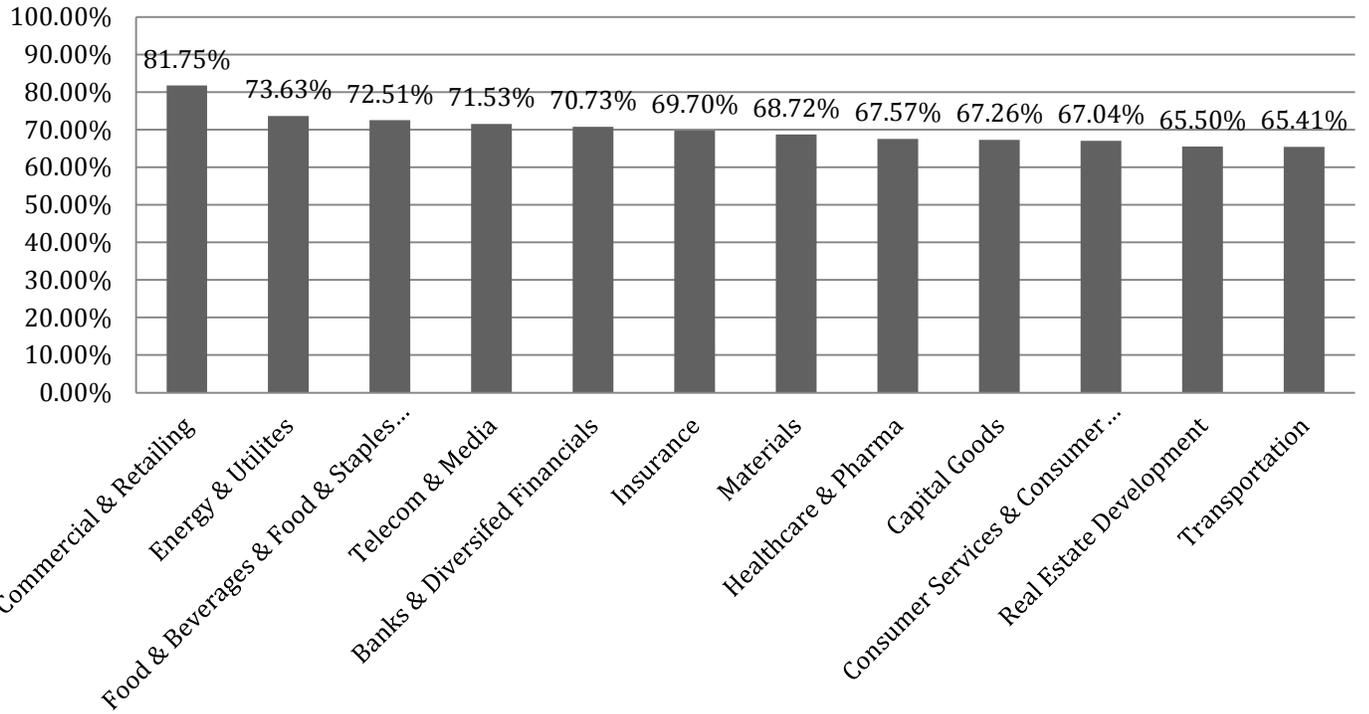
#### D) Corporate Governance Indices as a function of the Company Size

We also did comparison by company size as seen in Table 3 and Figures 11-15. We divided all companies into three categories based on their **market capitalization**: large, medium, and small. The companies with 60<sup>th</sup> percentile and above were considered to be large; those within 40<sup>th</sup> and 60<sup>th</sup> percentile were considered to be medium; and those below 40<sup>th</sup> percentile were considered to be small. It is clear that large and medium size companies have better corporate governance than small size companies. The cumulative CG score is almost same for large and medium size companies while six points less for small size companies. The sub-categorical comparison reveals that all companies had similar performance in terms of their adherence to the principles related to Board of Directors. For the Shareholders’ Rights and Public Disclosure small companies did score 2 points less compared to big and medium size companies. The gap was smaller for the Stakeholder’s Rights.

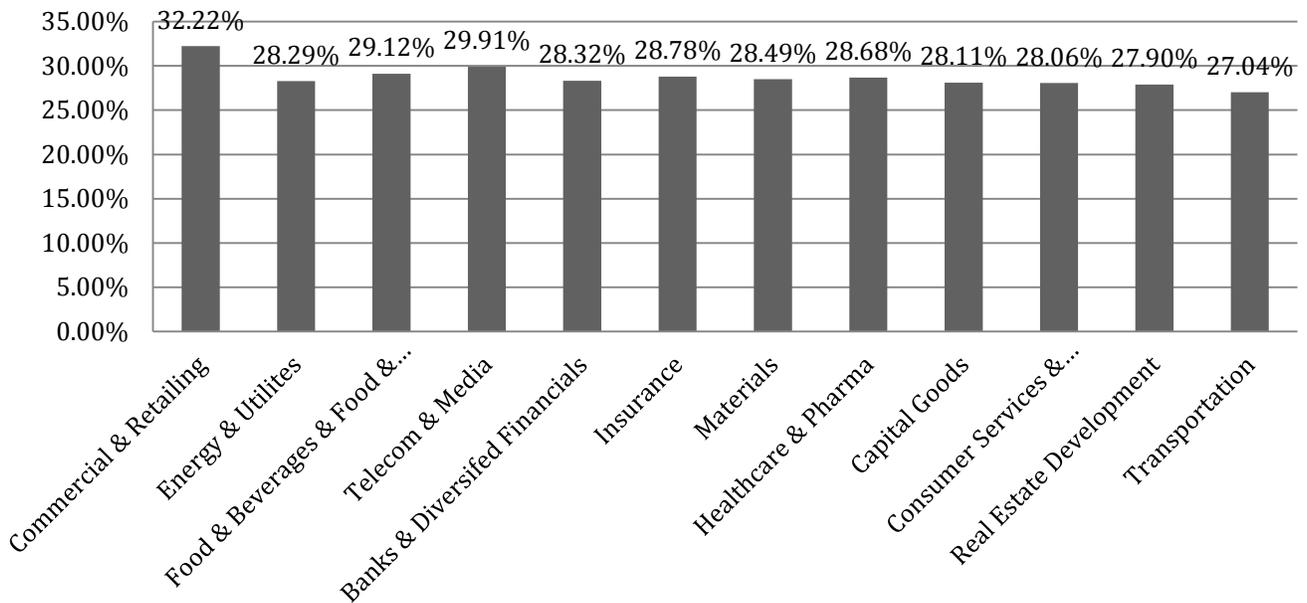
**Table 2. CGI Average Score By Sector and Category**

	Sector	Score	BOD	SH	PDT	ST	# of comp.
		100%	35%	25%	30%	10%	92
1	Commercial & Retailing	81.75%	32.22%	23.07%	22.17%	4.28%	5
2	Energy & Utilities	73.63%	28.29%	21.53%	19.04%	4.78%	5
3	Food & Beverages & Food & Staples Retailing	72.51%	29.12%	21.49%	18.60%	3.30%	8
4	Telecom & Media	71.53%	29.91%	20.97%	17.89%	2.76%	4
5	Banks & Diversified Financials	70.73%	28.32%	20.43%	18.88%	3.09%	14
6	Insurance	69.70%	28.78%	19.42%	18.74%	2.77%	5
7	Materials	68.72%	28.49%	20.32%	16.76%	3.15%	25
8	Healthcare & Pharma	67.57%	28.68%	19.27%	17.50%	2.12%	5
9	Capital Goods	67.26%	28.11%	21.00%	16.00%	2.15%	5
10	Consumer Services & Consumer Durables	67.04%	28.06%	20.35%	15.88%	2.76%	4
11	Real Estate Development	65.50%	27.90%	20.09%	15.67%	1.84%	9
12	Transportation	65.41%	27.04%	19.31%	17.02%	2.05%	3

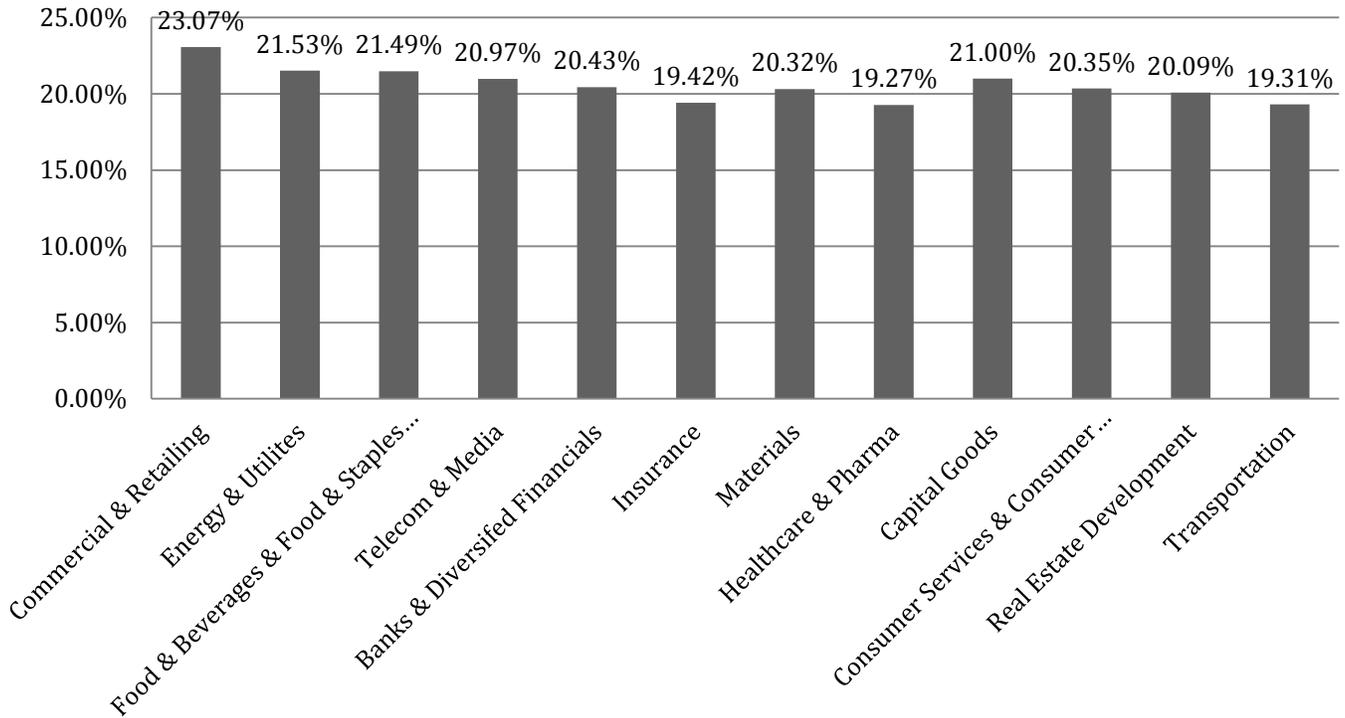
**Figure 6. CGI Average Score By Sector**



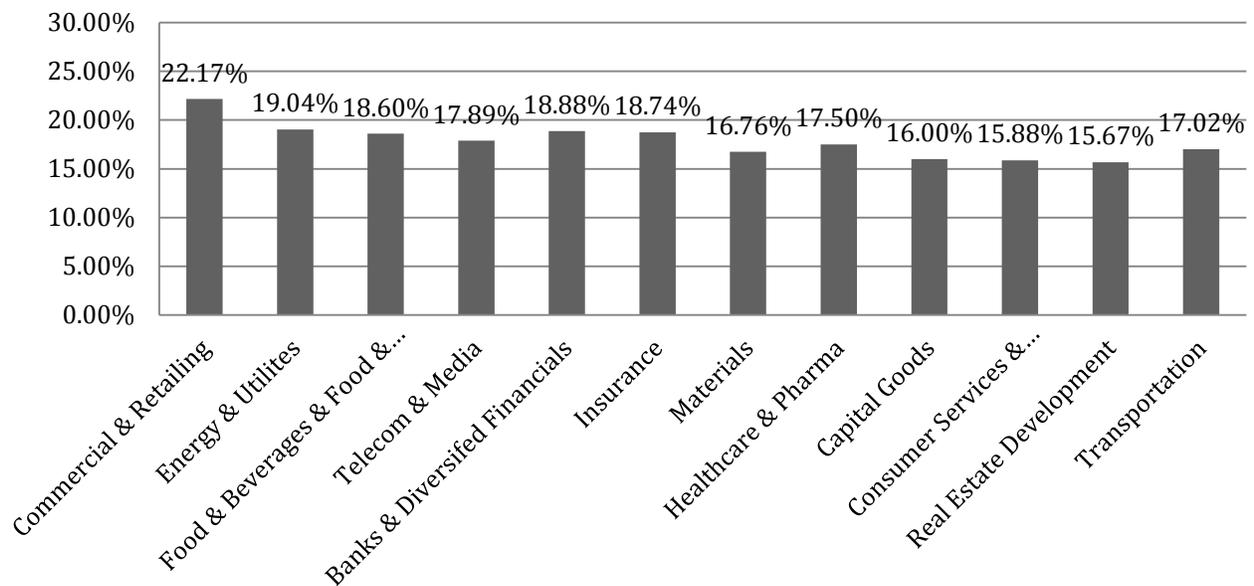
**Figure 7. CGI Average Score By Category  
Board of Directors**



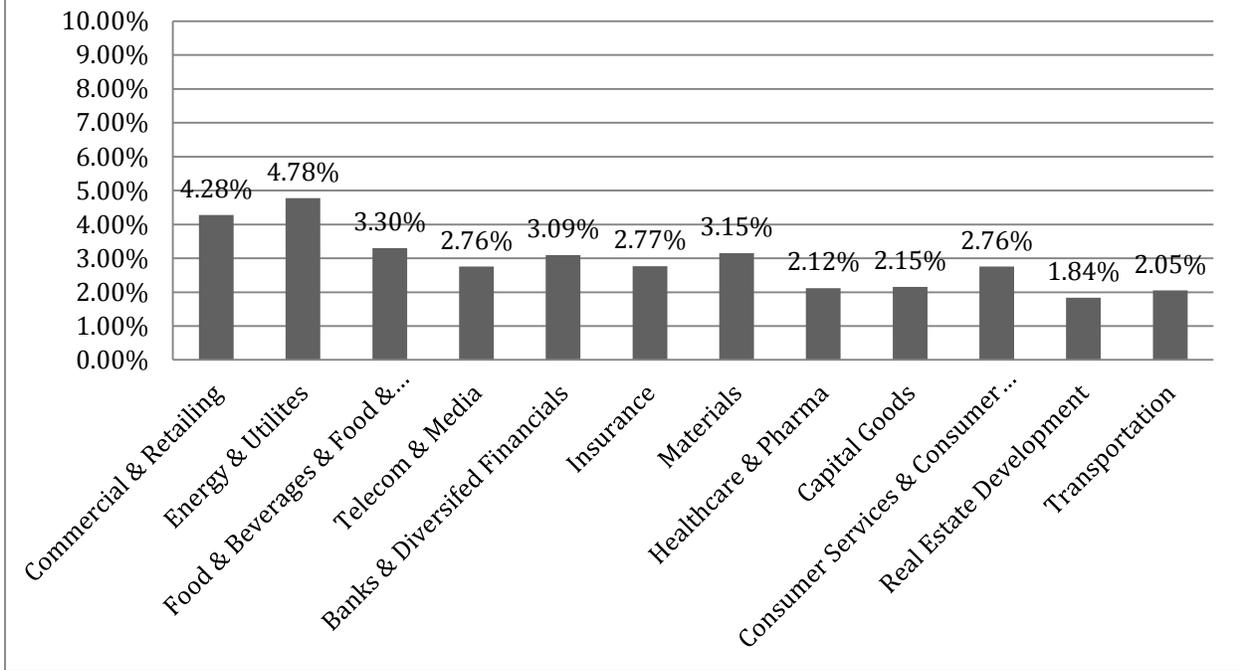
**Figure 8. CGI Average Score By Category**  
**Shareholders Rights**



**Figure 9. CGI Average Score By Category**  
**Public Disclosure and Transparency**



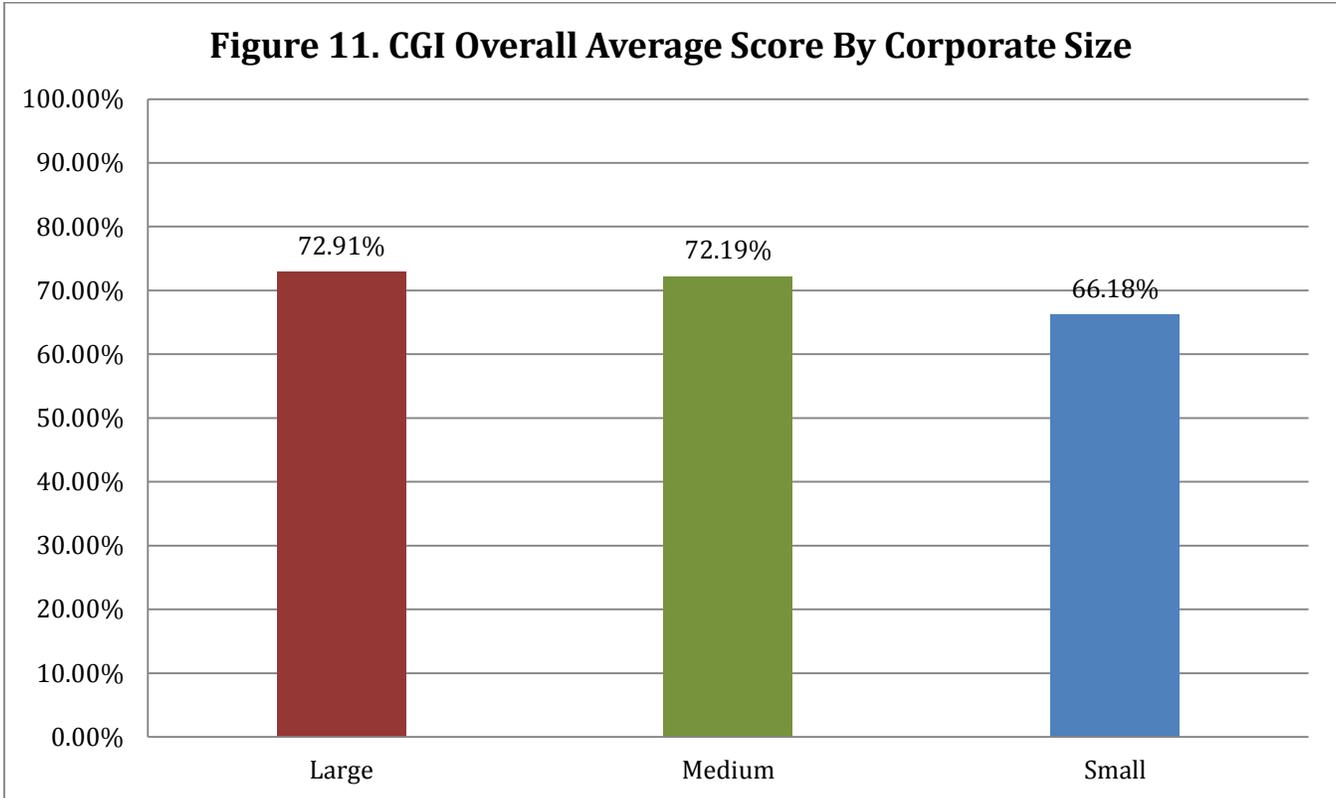
**Figure 10. CGI Average Score By Category Stakeholders**



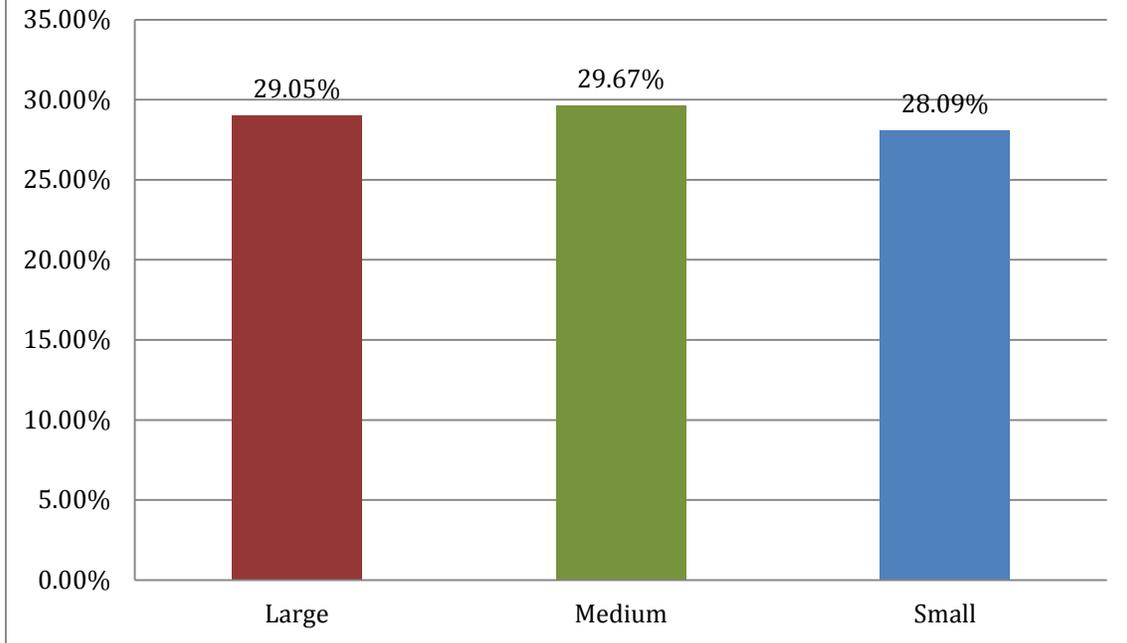
**Table 3: Company Distribution by Size**

Size	Score	BOD	SH	PD&T	ST	# of Comp.
	100%	35%	25%	30%	10%	92
<b>Large</b>	72.91%	29.05%	21.15%	18.87%	3.84%	39
<b>Medium</b>	72.19%	29.67%	21.03%	18.42%	3.08%	15
<b>Small</b>	66.18%	28.09%	19.12%	16.30%	2.67%	38

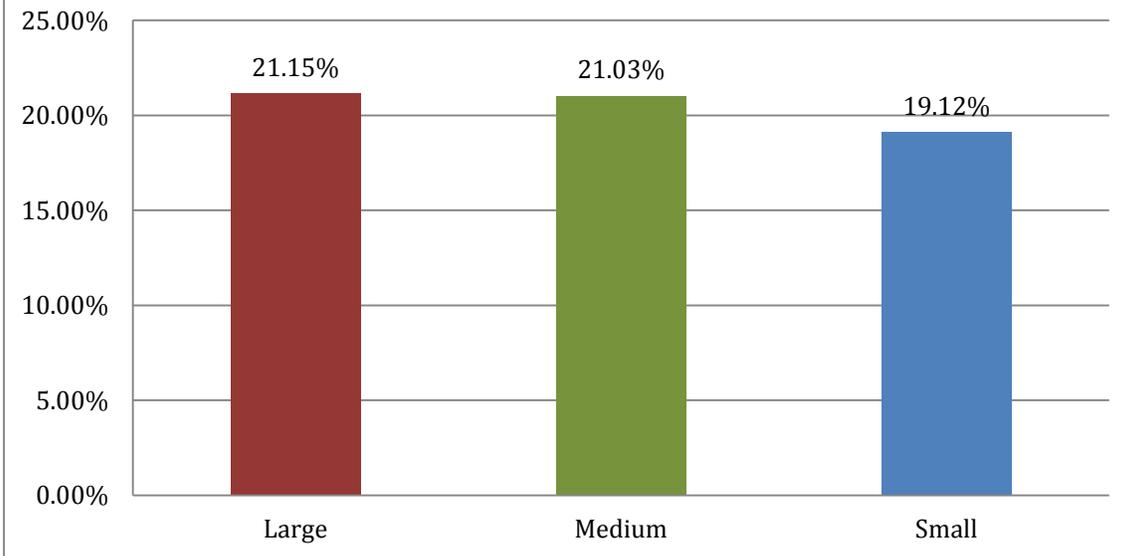
**Figure 11. CGI Overall Average Score By Corporate Size**



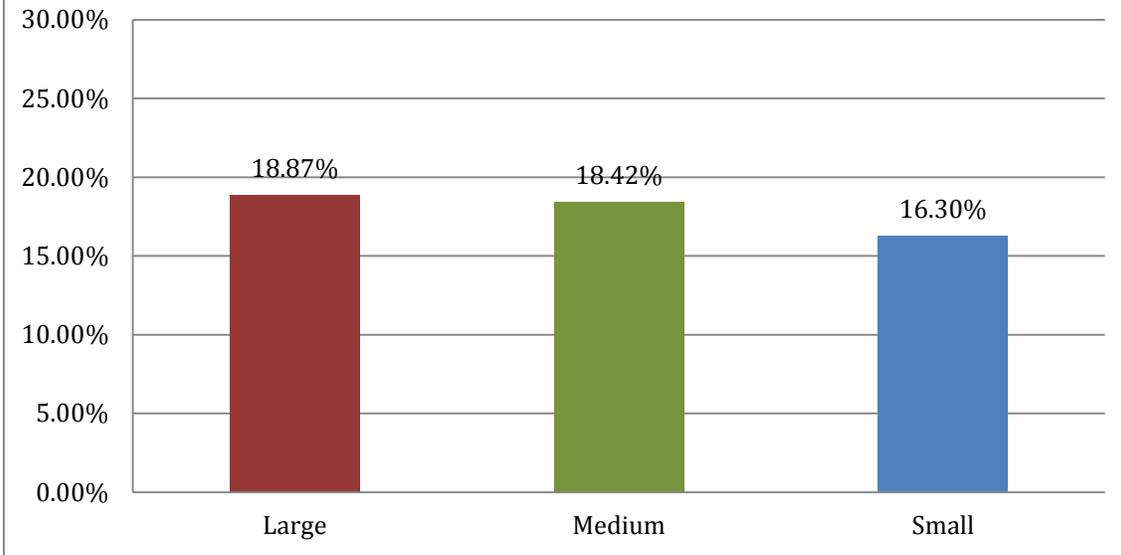
**Figure 12. CGI Board of Directors Average Score By Corporate Size**



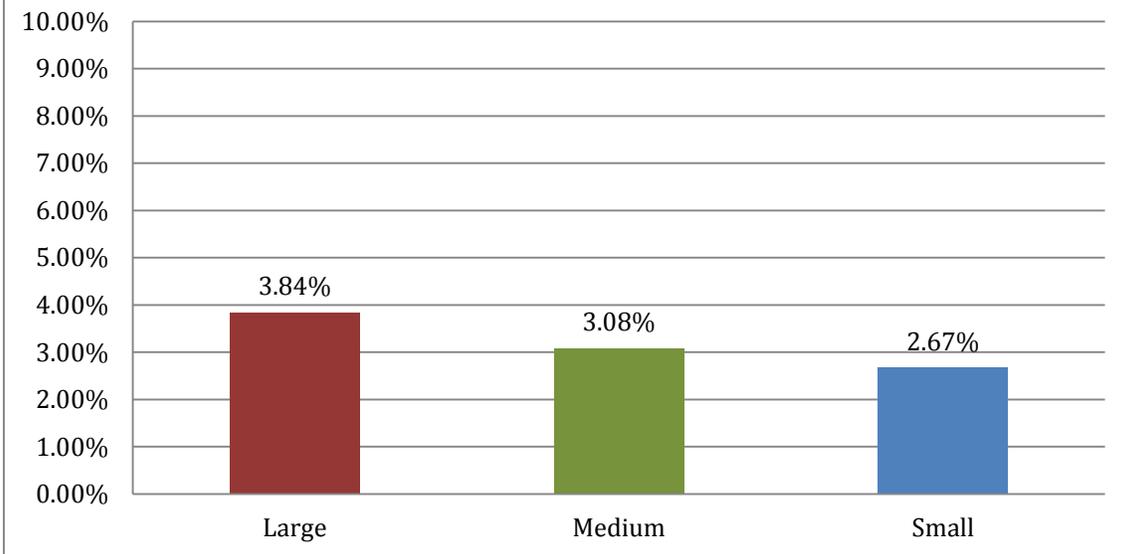
**Figure 13. CGI Shareholders Rights Average Score By Corporate Size**



**Figure 14. CGI Public Disclosure & Transparency Average Score By Corporate Size**



**Figure 15. CGI Stakeholders Average Score By Corporate Size**



## **Recommendations for the Improvement**

Even though the average cumulative corporate governance score is good, our study revealed that companies are relatively doing good in terms of corporate governance practices related to the **Board of Directors**, and **Shareholders Rights**. However, they did score quite poorly in terms of practices related to **Public Disclosure and Transparency**, and **Stakeholders**. The relatively higher standard deviation for these two categories also indicates that the good practices are not equally divided among the companies. We recommend the followings to further improve corporate governance practices:

- Increase oversight by CMA in terms of compliance to the relevant principles. In our assessment, we came across some discrepancies between what companies had as principles and did as practices. Good oversight might increase the compliance to the corporate governance principles
- Given the fact that most of corporate governance principles are voluntary based, it is important the government organizes workshops and conferences to increase awareness and facilitate sharing of best practices.
- Develop a certificate program for the training of company executives in regard to corporate governance principles and practices.
- Provide research grant to researchers to study the importance of good corporate governance. This will generate empirical evidence to encourage companies to comply with voluntary corporate governance principles.
- Pay great attention to the compliance to the corporate governance principles related to Public Disclosure and Transparency, and Stakeholders. The CMA might make some of those principles mandatory for companies to assure that companies are taking them seriously.
- Benefit from the practices of some of the companies that are scoring well on the four CG categories.
- Companies that are not scoring well on any combination of the four CG categories are encouraged to obtain a copy of its score card (report) from the CoB Corporate Governance Center. The report shows where such a company is not scoring well and where improvements are required.

## **Part IV: Customized CG Report**

### **1. Do you want a customized CG report for your company?**

We are happy to provide a customized CG report for your company. The report will include full assessment of the company's corporate governance practices within four categories (board of directors, shareholders' rights, public disclosure and transparency, and stakeholders' rights) using 117 variables. The cumulative CG score along with CG score by four categories will be provided. The report will provide detail graphical analysis of the company's corporate governance performance. It will include comparative analysis to reveal how the company performs compare to other companies. It will highlight both strengths and weaknesses of the company related to board of directors, shareholders' rights, public disclosure and transparency, and stakeholders' rights. Finally, the report will include key recommendations on how to improve corporate governance.

### **2. How can you order a customized report?**

To order the customized CG report for your company, please contact CG office at College of Business by phone: +966 -11 - 215 - 7682 or by email: saalsubaie@alfaisal.edu