SOE Governance Reforms in the MENA Region

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on behalf of Dr. Nasser Saidi,
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at the Global Network of SOEs Meeting
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Excellencies, Ladies and Gentlemen,

On behalf of Dr. Nasser Saidi, the Executive Director of Hawkamah Institute for Corporate Governance, who is also the co-chair of the MENA-OECD Working Group on Corporate Governance which is part of the MENA-OECD Investment Climate initiative, I would like to express our gratitude for giving a platform for Hawkamah to highlight some of its joint work with the OECD, particularly on state-owned enterprises of the region.

Indeed when Hawkamah was started in 2006 with the support of the OECD, World Bank, International Finance Corporation, Center for International Private Enterprise, Dubai International Financial Centre, Union of Arab Banks, among others, the vision was to build a regional institution that will aim to bridge the corporate governance gap that takes into consideration not only international best practices, but the actual implementation of these international best practices and guidelines taking into account local business culture, local laws and regulations, and local institutions.

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Through international and regional partnerships, task forces, research and benchmarking, assessments and advisory, and capacity building programmes, Hawkamah has endeavoured over these past four years to practically identify what exactly these gaps are and work with various institutions—both regional and international, regulators and companies, boards and individual governance stakeholders—to start bridging this gap.

One prime example of the joint work Hawkamah and OECD are doing is that of the regional task force of state-owned enterprises. During Hawkamah's first annual meeting, which coincided with the MENA-OECD Working Group on Corporate Governance's meeting, a Dubai Declaration was issued calling for a more sector focused approach on corporate governance (banks, capital markets and listed companies, family-owned enterprises, state-owned enterprises, media and academia). This Dubai Declaration, which has since been updated to the Doha Declaration two years later which reflected some of the region's lessons learned from the financial crisis, has been the focus of Hawkamah's advocacy and efforts in bridging the corporate governance gap in the region.

Around late 2007, OECD and Hawkamah mobilized their respective resources to constitute a regional Task Force on Corporate Governance of SOEs. The purpose of the task force is to bring together experts from all MENA jurisdictions to eventually develop a MENA Policy Brief on Corporate Governance of SOEs, identify priorities and propose concrete recommendations.

In order to understand the 'lay of the land' on corporate governance practices of SOES, we developed a survey based on the OECD CG guidelines for SOEs. The survey was circulated to 12 MENA jurisdictions (Ministries and regulatory agencies from Bahrain, Egypt, Iraq, Jordan, Kuwait, Lebanon, Morocco, Oman, Pakistan, Qatar, UAE, Yemen), of which five have responded (Bahrain, Egypt, Iraq, Lebanon, Oman and Pakistan). We combined both the primary sources we received with some of the secondary data we have acquired from other countries in each of our respective organization's work and produced a draft "Stocktaking Report on Corporate Governance Practices of SOEs in the MENA Region"

This Task Force has since had three meetings—the first one in Doha in November 2008 to initiate discussions on the task force and introduce the survey, the second in Dubai in November last year to share the Stocktaking Report, and the third one in Paris just yesterday to discuss next steps on the draft report—and we are planning on engaging more countries, more regulators and more stakeholders into this process as we move forward.

Corporate Governance Reforms are in the Process

And we have reason to believe that countries of the region are focusing on the need to address corporate governance. Since Hawkamah got started, we have been tracking the development of corporate governance codes in the region primarily led by capital market authorities, stock exchanges and central banks.

The Gulf countries have been active over the recent years in developing corporate governance codes. Oman has been ahead of the curve with the Omani Capital Market Authority announcing corporate governance standards for listed companies as early as 2002. Bahrain has put draft corporate governance codes for public consultation, Qatar issued a corporate governance code in 2009, while in the United Arab

Emirates, the corporate governance guidelines introduced by the Emirates Securities and Commodities Authority in 2007 will become mandatory for listed companies in the second quarter of 2010. The Central Bank of UAE has also recently issued draft corporate governance guidelines for bank directors in the Emirates, while the Capital Markets Authority in Saudi Arabia has started a gradual process of making some corporate governance regulations compulsory. The recent development in the Kuwaiti parliament calling for the establishment of a capital market authority marks a positive step towards the evolution of Kuwait's capital markets. Hawkamah also helped establish the Mudara Institute of Directors, designed to be a membership organization to build the capacity of directors in the region.

In other parts of the Middle East, Egypt has been one of the leaders in the region in creating corporate governance frameworks, and developing supporting institutions such as the Egyptian Institute of Directors to address some of the corporate governance challenges faced by that market. Similar initiatives have been started in Morocco, Tunisia, Lebanon, Palestine, and Jordan. Syria, as well, is in the process of developing a corporate governance framework.

Challenges on Corporate of State-Owned Enterprises

Initiatives like these mark important milestones in the development of corporate governance in our region. Important as it is to have such guidelines in place, challenges remain.

The region's state-owned enterprises are becoming significant players in their respective domestic stock markets. However some markets in the region exempt some of the listed state-owned enterprises from requirements on transparency and disclosure. This needs to be settled, and **all listed companies**

even if they are SOEs should be subject to the same standards of disclosure and transparency full stop.

Another set of issues that needs to be addressed is that of **development and disclosure of ownership policy**. Few countries in the MENA region have a clear ownership policy, much less a published one. In those MENA countries that have ownership policies, they are typically entrenched in Prime Ministerial Circulars, Royal Decrees, and a number of other laws which specify financial control of the state over SOEs. Clear and published ownership policies provide a framework for prioritizing SOEs' objectives and are instrumental in limiting the dual pitfalls of passive ownership or excessive intervention in SOE's management.

Related to the ownership policy is the need for the region to **define and streamline the legal status of SOEs and ensure the separation of ownership from regulation**. In the region, SOEs are often established under a combination of relevant company law and special statutes. We also need to start looking at the separation of ownership from regulation and other state function. All too often, particularly in the Gulf, some of the SOEs are also the regulators of their respective industries.

Another issue is that of accountability, particularly on reporting and Audit. The ownership entities are accountable on how they carry out their ownership functions and therefore must report on the overall performance of SOEs held by them and on their own performance. This accountability should be towards bodies representing the interests of the general public, which would include the State Audit Institutions. State audit institutions who are guardians and protectors of the State and public interests can and should adopt corporate governance principles in their review of and assessment of SOEs. Imposing SOE Corporate Governance principles on SOEs would be a natural extension of the role and mandate of State Audit Institutions, going beyond the strict and traditional boundaries of financial audit and recognition of the fact that better corporate governance results in improved financial and risk management and results. Hawkamah has reached out to a number of State Audit Institutions in the region to work with them and incorporate corporate governance in their audit framework. We note, for example, that Oman and UAE are now doing this.

It is also important for the ownership entity to ensure that **all shareholders are treated equitably**. The minority shareholders should be protected from abusive actions by the controlling shareholder and should have an effective means of redress. Moreover, the minority shareholders should have access to all necessary information to be able to make informed investment decisions. Having said that, it is important that any special mechanism for minority protection is carefully balanced. It should neither prevent the state as a majority shareholder from exercising its legitimate influence on the decisions nor should it allow minority shareholders to holdup the decision-making process.

Let me now focus on the issue of the Board, **particularly Board nomination and assessment**. Very few countries have nomination committees in place. The nomination process for SOE board members in most of our countries involves the finance ministry and line ministries. Representation of the state on boards where it has a minority holding depends on the requirements of the company and the benefits that such representation might provide to the company. The focus for reform in the region on boards is the transparency of the nomination process, ensuring that the nominations are made based on competence and experience, ensuring that there is a separation (maybe independence) between management and Board, there is some sort of self assessment to reflect on the added value the Board has given the SOE and lastly ensuring that the people that are taking on Board responsibilities fully understand and comprehend their fiduciary duty to the company.

One of the main focus of Hawkamah's advocacy is to convince regulators and governments that it makes sense to send a strong message to our board rooms that having qualified directors serving in our boards are as important as the corporate governance frameworks and disclosures that need to be put in place. We advocate that regulators and governments endorse the idea of a professional director that goes through an accreditation and certification body, similar to what we would expect of our accountants, auditors, financial analysts, lawyers and other professionals.

Underlying all of these items I mentioned is the need for the region—on a country by country basis—to **develop code of corporate governance for state-owned enterprises.** We note Morocco and Egypt have been leading the way on this issue, and we urge other countries to consider developing SOE codes in order to have a uniform framework of what governments expect of their enterprises, which should include more transparency and disclosure, frameworks for board nomination, delineating the SOE's responsibilities to various stakeholders, etc.

Conclusion

The region's State Owned Enterprises (SOEs) are a major and pervasive part of the economic system. SOEs in the MENA region are active across a wide spectrum of industrial and financial sectors and represent a major portion of the economy's infrastructure and of stock market capitalization.

Improving the corporate governance of SOEs will lead to mutually reinforcing multiple rewards of significant efficiency gains, improvement in the quality of public services, greater transparency and better protection of the State's interests. Improving the performance of SOEs results in improved fiscal outcomes, insofar as government budgets are all too often called to the rescue of large SOEs. We have seen this particularly happen during the current financial crisis. We need to reinforce the SOE's ownership function, try to delineate and avoid the mixing of political or social policy and business decisions, improve transparency, empower SOE boards and improve their accountability.

Just as there have been positive movements for reform in the region, much more needs to be done. The work of the regional Task Force has just begun. We hope in the next Global Meeting of SOEs we are able to report to you great strides in the improvement of SOE corporate governance in the region.

Thank you for your attention.