



# Center for International Private Enterprise Bahrain Accountants Association

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## Survey of Corporate Governance Practices in the Private Sector in the Kingdom of Bahrain

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# Executive Summary

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## Research Objective and Methodology

- This is the first of two waves of research with the objective to measure the level of understanding of corporate governance, current compliance or willingness to do so and with which procedures.
- A second wave of research aims to measure the results of initiatives taken to progress the understanding and adoption of corporate governance.
- The results of this primary research are from 150 interviews with a cross section of large companies in Bahrain, skewed towards those operating in the more regulated Finance sector.

## Annual Reports

- Most companies compile an annual report, but this does not mean it is widely published.
- Some 72.4 % of businesses circulate the report among shareholders (average of 32) and Board Directors, but less than 1 % make this available to other stakeholders.
- Other than the financial results, most annual reports only provide basic information about the Board of Directors and organizational structure.
- Most (91%) companies have private shareholding with nearly 17 % of these constituting family businesses.
- Private companies have historically presented the mainstay of business in Bahrain, initiated by family companies. The business culture among private businesses in the Gulf is inherently discreet and this translates into sharing information on a “Need to know” basis. Board Directors shun scrutiny other than that by fellow shareholders.
- Unless obliged by law, most companies avoid sharing information they deem confidential out of an anxiety that this could be used to their disadvantage.

## **Annual Reports (Continued)**

- This business culture is clearly a potential obstacle to instigating effective corporate governance measures. They will be more acceptable with listed companies and those operating in a more regulated business sector such as Finance.

## **Board of Directors**

- The Board typically has five directors.
- Meetings of the Board of Directors are semi-structured. They are regular, but agendas are relatively “Loose”. The purpose of these sessions (they rarely happen without executive management) seems more for senior management to keep the Board of Directors informed at a high-level rather than in great detail.
- The larger the company, the more formal powers and duties are specified for Board Directors. The research deduces that generally these authorities and responsibilities are not documented in detail.
- Only in the more regulated Finance sector are specialised committees and independent management teams more common.
- In most many cases, the CEO is not only a Board Director, but is also the main shareholder controlling at least 40 % of ownership.
- Non-Bahraini Board Directors are rare.

## **Shareholders**

- The number of shareholders ranges from 1 to 550 with an average of 39, largely because the number of listed companies in Bahrain is modest.
- It is quite common across the industries for one shareholder to own a large chunk of shares, accounting 41.4 % and with a mode of 40%. It is likely that this is the CEO of the company.
- Practically all companies claim the voting rights are in proportion to shareholding. However, the research deduces that the CEO is also the main share holder and therefore with combined executive and ownership powers his influence holds sway.

- Shareholders who are not on the Board of Directors, may cast their vote for the choice of auditor and to approve distribution of profits. They have only modest influence in affairs relating to the Board of Directors.
- Companies do have procedures in place for assessing and approving transactions, but shareholders other than those on the Board have hold little influence over these transactions.

### **Transparency**

- While companies prepare annual reports, they are not fully published (72.4 %). Even then the research deduces that circulation of the report is limited to shareholders only (average of 39).
- Only half disclose business strategies and less than a third inform of the regulatory structure of the business.
- Hence, companies avoid sharing information they deem confidential, to which only Board Members are privy.
- Disclosure of information is commonly through periodic reports, but the research deduces that circulation selective.
- Very few companies opt for the more public modes of communication for sharing information such as the company's website, newsletter or even at general meetings and through published annual reports.
- Larger companies –especially in Finance -more likely engage large international audit firms, whereas local certified chartered accountants come to the fore with small to medium sized businesses.
- Internal audits are not usually through a third party. An in-house team focuses on financial performance and to ensure there is compliance with the law. Evaluation of internal controls and work procedures is lower on the priority list.

### **Corporate Governance**

- The larger the company, the greater the understanding of corporate governance issues with management. The Finance sector is more exposed to outside controls to comply with rules and regulation and is therefore more accustomed to (some) principles of corporate governance).

- Print media are the more effective sources of awareness, followed by conferences and seminars. The bigger the company, the more exposed to different sources.
- Respondents understand the spirit of corporate governance as regulations to secure a business' transparency, ethics, integrity and accountability.
- Views tend to be at an overall concept level (and at times fuzzy), rather than revealing a detailed knowledge of how corporate governance measures should be executed.
- Companies acknowledge the benefits of corporate governments to be in the areas of increased sustainability and greater access to capital. There is less conviction about its benefits in business performance and sharpening of the competitive edge.
- Companies concede the importance of external auditors, of encouraging shareholders to participate and to a lesser extent the separation of the Board and management. There is however resistance to the notion of including more independent Board Members and to disclosing salaries of Directors and senior managers.
- On the one hand, most companies applaud (96.7 %) the concept of corporate governance, but on the other hand private companies do not seem to be enthusiastic (yet) to adopt all measures fully.
- In short, private companies encourage raising the awareness and understanding of corporate governance for the listed companies and Finance sector, but they are not enthralled about regulations that potentially open the main shareholders (and therefore Board Members) to public scrutiny.

## **Conclusions**

- The Finance sector and listed companies are ripe segments for the introduction of mandatory corporate governance, but the private sector – which still represents the lion share of business in Bahrain – is likely to offer resistance. Board Directors shun scrutiny other than that by fellow shareholders. The CEO is also often the main shareholder and seemingly disinclined to embrace initiatives that could curtail the powers of the “Family baton” handed to him from previous generations.

- Curiously, many companies have readily adopted prescribed systematic business standards –at great expense -such as ISO as they believe their business stands to gain. They sharpen the competitive edge. Corporate governance does of course draw more deeply into the realm of what Board Directors consider confidential.
- Extending a motive to decision makers that corporate governance can actually help them grow their business –which they do not currently identify with -could nurture a positive “Pull” rather than a negative push through what they may consider “Government interference”.

### **Recommendations**

- The understanding of corporate governance is rather “Fuzzy” in conceptual terms such as transparency, ethics, integrity and accountability. Stronger communication to lift the tangible benefits of corporate governance could instill a more favorable disposition.
- Print media are more effective in reaching the decision makers, as well as through professional associations and electronic media.
- The more receptive companies to corporate governance regulations are:
  1. Companies listed on the stock exchange.
  2. Organizations in the Finance sector.
  3. Private companies with a large number of shareholders and with the absence of a CEO holding a majority stake in the company.
  4. Private companies in which the management is largely independent from the Board of Directors.
- Corporate governance measures relating to the financial performance of the company are acceptable and are indeed already mandatory
- Transparency of the company structure is in place at a general level, but measures to isolate accountability of individual Board Directors with details of individual remuneration packages is likely to offend and therefore met with resistance. Hence, some compromise in enforcing such regulations may mollify the notion that corporate governance represents an interfering nuisance.