

# Corporate Governance- Issues and Challenges in Pakistan

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## Abstract

**Purpose:** Pakistani companies are crucial for attaining the better position in the global market by adopting the actual concept of corporate governance. Corporate governance is a worldwide phenomenon. Corporate Governance is the system of rules, practices and processes by which a company is directed and controlled. This research paper focuses on the finding & reviewing of the issues and challenges faced by corporate governance in Pakistan.

**Research methodology:** keeping in view the objectives of this study, research design was adopted to have greater accuracy and in depth analysis of the research study. Available secondary data was extensively used for the study. The investigator procures the required data through secondary survey method. Different news articles, Books and Web were used which were enumerated and recorded

**Findings:** The causes of poor corporate governance in Pakistani companies are ineffectiveness of INED's in Pakistani companies, a lack of understanding, inadequately trained personnel, coverage, policy etc. further adds to the reach and effectiveness of corporate governance programs

**Keywords:** corporate governance, non executive independent directors (NED)

## Introduction

Corporate governance is a way of governing activities of a corporation for the well being of all stakeholders (not only for shareholders) that ultimately leads to better financial performance. It is the set of process, customs, policies, laws, and institutions affecting the way a corporation (or company) is directed, administered or controlled. "Corporate governance refers to the manner in which the affairs of a corporate body are or should be conducted in order to serve and protect the individual and collective interests of all stakeholders" (Butt 2008)

Corporate governance essentially involves balancing the interests of the many stakeholders in a company - these include its shareholders, management, customers, suppliers, financiers, government and the community. Since corporate governance also provides the framework

for attaining a company's objectives, it encompasses practically every sphere of management, from action plans and internal controls to performance measurement and corporate disclosure. Corporate governance became a pressing issue following the 1992 introduction of the Sarbanes-Oxley Act in the U.S., which was ushered in to restore public confidence in companies and markets after accounting fraud bankrupted high-profile companies such as Enron and WorldCom. Most companies strive to have a high level of corporate governance. These days, it is not enough for a company to merely be profitable; it also needs to demonstrate good corporate citizenship through environmental awareness, ethical behavior and sound corporate governance practices. It is analyzed that corporate governance is emerging as a basic component of success in terms of the functioning of the corporate sector in financial markets. In this regard security and exchange commission of Pakistan has taken several initiatives for the effectiveness of corporate governance in Pakistan. Above all it was focus that addition of the independent directors in the Pakistani companies is crucial for attaining the better position in the global market by adopting the actual concept of corporate governance.

Code of the Corporate Governance covers almost all those points which are mentioned in the Code and being practiced in the developed countries. SECP is also continuously making changes in the policies in order to achieve the maximum effectiveness and to incorporate the changing occurring in the global business market and its effects on the local market. It has received wide attention of policy makers in the developed and developing countries in recent years. It requires a more significant dimension in a developing country like Pakistan. But it is generally said that Pakistan has perhaps has the world most regulated corporate sector with more detailed reporting requirements than in any other country. Yet the standards of corporate governance in Pakistani companies are still poor.

### **Corporate governance in Pakistan**

The SEC, since it took over the responsibilities and powers of the Corporate Law Authority in 1999, has been acutely alive to the changes taking place in the international business environment, which directly and indirectly impact local businesses. As part of its multi-dimensional strategy to enable Pakistan's corporate sector meet the challenges raised by the changing global business scenario and to build capacity, the SEC has focused, in part, on encouraging businesses to adopt good corporate governance practices. This is expected to provide transparency and accountability in the corporate sector and to safeguard the interests of stakeholders, including protection of minority shareholders' rights and strict audit compliance. Parties involved in corporate governance include the regulatory body (e.g. the Chief Executive Officer, the board of directors, management and shareholders). Other stakeholders who take part include suppliers, employees, creditors, customers and the community at large. In corporations, the shareholder delegates decision rights to the manager to act in the principal's best interests. This separation of ownership from control implies a loss of effective control by shareholders over managerial decisions. Partly as a result of this separation between the two parties, a system of corporate governance controls is implemented to assist in aligning the incentives of managers with those of

shareholders. With the significant increase in equity holdings of investors, there has been an opportunity for a reversal of the separation of ownership and control problems because ownership is not so diffuse.

Corporate governance in Pakistan has recently started scratching the surface. Due to many distortions in economy, market forces do not reward good governances or punish unethical practices. The large part of the undocumented economy discourages promotion of transparency and accountability in the organization. Overall management structure is also not conducive to establishing the norms of good governance. Many companies in listed Stock Exchange are not fully practicing the code of good governance. Tightly held ownership, lack of professional skills, missing change agents, audit dependability and overall structural weaknesses are bottlenecks in developing the corporate governance in the organizations.

### **Objectives**

The Present paper is basically concerned with the following objectives.

- To study the Issues and Challenges of corporate governance in Pakistan.
- To implement corporate governance in Pakistanis companies.
- To review different international models of corporate governance from developed and developing economies.
- To make policy suggestions and recommendations based on alternative model for Pakistan.

### **Methodology**

Looking into requirements of the objectives of the study the research design employed for the study is of descriptive type. Keeping in view of the set objectives, this research design was adopted to have greater accuracy and in depth analysis of the research study. Available secondary data was extensively used for the study. The investigator procures the required data through secondary survey method. Different news articles, Books and Web were used which were enumerated and recorded.

### **Literature Review**

There is an emergent literature of different models of capitalism from alternative analytical frameworks showing the nature and extent of diverse forms of capitalism, their comparative strengths and weaknesses, and the prospects for institutional miscellany when confronted with mounting pressures for international economic integration (Deeg and Jackson 2006). The varieties of capitalism research articles illustrated by Hall and Soskice (2001) takes on a firm centered approach focusing on the incentives for coordination; a wider typology of governance mechanisms in terms of social systems of production is existed by Hollingsworth and Boyer (1997); and a national business systems approach of Whitley (1999) inspects the internal capacities of business corporations.

The Japanese model of corporate governance which developed under these situations has sometimes been explained as 'state-contingent corporate governance' (e.g. Aoki et al., 1994). Whenever firm performance is satisfactory, management acts independently or, some argue, is examined by the company's large and stable shareowners. When firm performance is poor, then creditors, and in particular, the firm's intervene, initiate a restructuring plan, and discipline the poorly performing management.

The function of the top institutional owners, such as Allianz, as spiders in the web of cross-holdings has been well identified (Story and Walter, 1997). Like other characteristics of ownership concentration however, the understanding of the dynamics of top holders and cross-holdings is at best scrappy. Many authors report on big banks and insurers selling their stakes and leaving boardrooms (O'Sullivan, 2000; Mülbert, 1998). Some of these stakes are not really sold but rather spun off to one by one managed holdings or investment funds, still controlled by the big actors (Jürgens and Rupp, 2001). This is one of the reasons why Doremus et al. foreseen that universal banks would maintain their position in the German market for corporate control (1998). Interconnected with the position of the top institutional shareowners, is whether the responsibility of cross-holdings, extensively reported to be significant in the past (Prowse, 1994; Wenger and Kaserer, 1998), has varied. In the light of the questionable research evidence, I anticipate that the power of the top institutional shareowners was maintained.

For the purpose of implementing corporate governance in Pakistani companies, these steps are required to remove the poor corporate governance in Pakistani companies.

- Identification of the causes of ineffectiveness of INED's in Pakistani companies.
- Changes that required to be introduced in the code.
- Steps to be taken to improve the standards of corporate governance.
- Handling these issues by other developing countries.
- Solution for Pakistani environment.

### **Causes of Ineffectiveness of Non-executive Independent Directors in listed companies of Pakistan**

As we know that board composition and independence are fundamental issues in corporate Governance. Board independence is very important for governance mechanisms. But in Pakistan there is no concept of independent non-executive directors. Besides, non-executive directors actually are not independent. Board independence is one of the most important elements of good corporate governance. Independent directors broadly fit into the overall structure of corporate governance, and are necessary to ensure effective, balanced board. An independent non-executive director is one who is independent of management. Under the combined code the director should not have been an employee of the group within the last 5 years, should not have a material business relationship with the company, should not receive any remuneration from the company other than fees, share scheme and performance related pay, should not have close family ties with advisers, directors or senior employees, should not have significant links

with other directors, should not represent a significant shareholder and should not have served on the board for more than 9 years.

In Pakistan independent non-executive directors are practically absent. Here a lot of companies depict a number of their directors as non-executive and pretence them to be independent, but in reality none of them is independent. There are following reasons for INEDs being ineffective in Pakistan's listed companies.

### **Companies owned by families of closed groups**

Mostly companies are owned by families or closed groups. And they usually try to stay away from such directors whom they are unable to control. Actually controlling shareholders are keen to run their company in their own way and they hate any kind of interference from outside. They are not prepared to grant any of their powers to outsiders. It all depends on controlling shareholders whether they really want to have independent non-executive directors on their company's board or not.

### **Companies not pay remuneration**

Another important cause of ineffective independent non-executive directors in Pakistan is that companies do not pay any compensation or remuneration to them. There is just a fixed fee for them for attending a meeting.

### **Professionals don't have plenty of time**

Good professionals are not keen to serve on the boards of listed companies just for getting only a meeting fee. In fact some of them don't have plenty of time to do so. To run the company successfully you need good people, and good people have no time for company matters as they are already busy with their work.

### **Mistaken belief in Pakistan**

There is a mistaken belief in Pakistan's listed companies that if they provide salary to INEDs it will take away their independence.

### **No long term benefit**

Independent non-executive directors are supposed to be professionals like external auditors or institutional investors. But in Pakistan they have no interest to serve as INEDs because they have no long term benefit and they are not happy with such a low fee.

### **Do not have adequate knowledge**

Unfortunately if there are any INEDs in Pakistan listed companies they do not have enough or

adequate knowledge to contribute efficiently in board proceedings.

### **No balance of power in the board**

Due to absence of independent non-executive directors in Pakistan listed companies there is no balance of power in the board.

### **Suggestions to cure the malady of INED's in Pakistan**

The Code of Corporate Governance by SECP is very young and so need to be developed more. SECP has developed the first code of corporate governance for Pakistan in March 2002 which is now available on its website after few amendments. It is vital that the Code be followed not only in letter but in spirit as well. There are few suggestions to cure the maladies found in Code of Corporate Governance:

- There are not enough INED's found in Pakistani companies. Only handful cannot have the ability to cater the proper working of organizations. There is a requirement in the code of corporate governance that the number of INED's should be half of the total number of directors on the board. In the board 1/3rd directors to be non-executive independent directors, while the Higgs Report recommends enhancing this ratio to 50% so such rule should be in the code now. Application of this rule to closely hold/ family owned private companies will help in ensuring corporate governance culture. The combined code of UK recommends the same as well that at least half of the board, including the chairman should comprise of non-executive directors. We think that this 'should' be substituted with 'must'.
- The issue with the working of INED's is that the amount of work they perform is not sufficient. At present no director is allowed to serve on more than ten Boards (rule iii). However, with increased responsibilities, it is extremely difficult rather demanding for a director to make useful contribution at ten Boards. In view of this problem, it is felt that that no director should be allowed to serve on more than 5 boards at one time. There bifurcation of working with different companies makes them unavailable for important decisions. This should be minimizing in order to be effective INED's. Moreover, there should be certain restrictions for INED's which makes them work for not more than 4-5 company boards at a time.
- On factual data, INED's are not paid much per board meeting (ranging from 500-5000 PKR). In many Western and European countries, INED's are paid handsome remunerations which ensure their motivation to participate positively in board meeting and thus effective decision making. On the contrary, INEDs in Pakistan loses their independence as they are much dependent on the income from any organization. Proper incentives and remuneration packages should be introduced on performance basis. Fixed pay often lessens motivation and attention.

- Skill and care duty is adopted to enhance the survival of any organization through the board of directors. If a person feels that he/she does not have the necessary skills and ability that can be reasonably expected from a director, he/she should not accept. Therefore, to remove this deficiency, professional and qualified INED's should be appointed.
- To handle the issue of ineffective boards in which the chairman and executive directors' involvement is more than other members, other types of board formation can be effective. Types such as two tier boards in which INED's can play important role. The upper tier should be comprises of INEDs mostly.
- Proper trainings should be incorporated for INED's when they join the company/organization. Induction should comprise of good orientation programs for directors especially INEDs which will enable them to get all the relevant information of the organization.
- It is generally acknowledged that implementation of the Code has resulted in greater financial discipline, uniform presentation of financial results and an organized and more disciplined corporate culture which has, to a great extent, bridged the gap between various stakeholders, the Board of Directors and the Auditors. Therefore, proper implementation of code of corporate governance is important for effective governance. It is the responsibility of the board to make sure its practical implementation.
- It is suggested that an Institute of Directors will need to be established, whose task would be to create a data bank of persons qualified and experienced enough to serve as directors. A number of organizations e.g. the SECP, the Institute of Chartered Accounts (ICAP), the Institute of Cost and Management Accountants of Pakistan (ICMAP) and the Management Association of Pakistan (MAP) can also play a supportive role in identifying professionals with suitable credentials to serve as independent non-executive directors.
- One area that needs to be given due consideration is training of directors so that they should continue to keep themselves informed about changes in legal, corporate, financial and other business areas to be able to serve their boards in an effective manner and make useful contribution. It has also been proposed by some professionals, that a minimum number of hours of training (say 10 hours) on issues such as governance, internal control, risk management, specific courses on the business of the Company etc. should be made compulsory.
- Holding of Annual General Meetings (AGMs) is one of the important forums for shareholders to assert their rights. According to SECP Annual Reports, the level of compliance with regard

to the timely holding of AGMs is quite high. This trend is rising by the time which is a positive sign. Thus holding of AGMs should be made compulsory all over the corporate sector.

- The newly appointed directors and employees should be asked to sign the Company's Business Ethics statement at the time of their appointment.
- The issue of fee charged by the External Auditors is also a big issue, so that fee must be capped by some reasonable amount.
- The audit committee should be comprised of the Finance literate members.
- Family members of the CFO, or CEO shouldn't be the part of Audit committee. Once the number of family members on the Board is restricted, only then would discussions at board meetings become meaningful and transparent and the Audit Committees would be able to play a significant role.
- There must be some criteria established regarding the Certification of the Directors and so as the authorized institutes.
- There must be some strict evaluation criteria for the board's performance and should be mentioned in the code.(who'll be authorized to evaluate)
- In the board meetings CFO or secretary finance is asked to attend the meeting but the purpose is not so much clear.
- Eligibility criteria for the Directors' should be more clarify.
- There is a rule regarding the vacancy filled by board but there should be some regarding the profiles of authorized directors so that vacancy filling process will not take much time.
- No. of Board meetings should be as per the size of business.
- The strict rule should be included in the code regarding the record keeping of the director's duties, board's meetings, committees and their members, attendance in meetings etc.
- The code should mention some rules to make the board bound to make different committees where required such as remuneration committee etc.



## **Steps for Improving the Standards of Corporate Governance**

Corporate governance may play vital role in raising the company's performance and strong indicator to the extent that the company is currently adding or having the potential to increase its production in future.

The corporate governance is emerging issue and getting interest of academics, practitioners and regulatory authorities after the 1997-1998 East Asian financial crises. OECD issued "principles of corporate governance" in 1998 to establish corporate governance standards. In the context of Pakistan SECP issued code of corporate governance 2002 for publically listed companies. Thus it is the ultimate responsibility of SECP to take these steps for the better governance in the country.

### **Board chairman as a leader**

The responsibility of chairman is to manage the board of directors. Chairman is the powerful person in the company. Good corporate governance is wholly depending upon/revolving around his shoulders. His strong decision making can play a vital role to run the company effectively.

### **Fairness**

There should be the equal consideration to all the stakeholders either they are minority shareholders or majority shareholders. Thus it is clarified that all the shareholders having equal importance for the company and we should consider them all in making strategic decision making for the company.

### **INED'S Skill, Experience and Courage**

The skills, experience and courage plays vital role if anything going wrong. Therefore they have to make them aware the current business environment and INED's are in better position to approach issues and speak up more freely.

### **Director access to information**

As the INED's are the members of BOD without executive responsibilities in the companies. They do judgments on the basis of their experience. So they should give complete authority to the information for the wellbeing of the company.

### **Board's role in making judgment**

The INED's are the members of the board of directors without executive responsibilities in the company. They bring judgment and experience to the deliberation of the board..

### **Relationship with shareholders**

INED's having non-employment status independent directors are supposed to identify with the interest of shareholders as well as operate in the best interest of the company in an unbiased way.

### **Director remuneration package**

Director's remuneration is set by the Remuneration committee. The committee decides how many the fees to be paid. The need of the remuneration committee was felt by taking the excessive benefits by the directors.

### **Relationship with External Auditor and company**

The relationship between Audit Company and the client should not be friendly but it should be on professional basis. External directors should have authority and free access to the information they are looking for.

### **Companies attitudes to ethical behavior**

The code of ethics is the set of rules and guidelines for moral behavior and explains the guidelines for employees to work. The code also strengthens the role of directors and plays vital role in setting the duties of board. For this PICG should work to develop a set of detailed guidelines for board members for defining their duties. The companies should follow code and work in a better way for the society from which the organization is generating its resources

### **Corporate Governance Index**

Corporate governance index is a tool to enable stakeholders gauge the state of corporate governance in individual companies and, overall, in a country. It indicates assessment of corporate governance practices and policies and reflects the relative level to which a company follows the generally accepted codes of corporate governance. Governance practices are measured through a survey of each company. Based on the survey findings an index is formulated. The purpose is to benchmark a company's investor right protection, disclosure quality, board effectiveness and other key features against the principles of transparency, accountability and responsibility. Different aspects of corporate governance are included in the index, such as board of directors, non-executive directors, board committees, internal audit, financial transparency and information disclosure, and stakeholders' rights. The Corporate Governance Cell is developing the methodology for formulating a corporate governance index for Pakistan. Once completed this methodology will serve as a foundation to commence research and formulation of the index.

- Protect stakeholders' interests.
- Assure real possibility to Shareholder's activism.
- Auditors should have to take action regarding interpretation of the rules by the court and make signification revision of the code by SECP
- Committees of the Board should act according to the rules and regulations of the board.
- Firms should not entirely run by families or close groups.

## Handling these issues by other developing countries

Many developing nations have not yet fully developed the legal and regulatory systems, enforcement capacities and private sector institutions required to support effective corporate governance. Therefore, corporate governance reform efforts in these nations often need to focus on the fundamental framework. It includes basic stock exchange development, the creation of systems for registering share ownership, the improvement of audit and accounting standards, and a change in culture and laws against bribery and corruption as an accepted way of doing business.

In the developing nations, governance codes are more likely to address basic principles of corporate governance that tend to be more established in developed countries through company law and securities regulation, such as the equitable treatment of shareholders, the need for reliable and timely disclosure of information concerning corporate performance and ownership, and the holding of annual general meetings of shareholders. However, in both developed and developing nations, codes focus on boards of directors and attempt to describe ways in which boards can be positioned to provide some form of guidance and oversight to management, and accountability to shareholders and society at large.

In developing nations, both voluntary guidelines and more coercive codes of best practice have issued as well. For example,

- Both the Code of Best Practices issued by the **Brazilian** Institute of Corporate Directors and the Code of Corporate Governance issued by the Corporate Governance Committee of the **Mexican** Business Co-coordinating Council are wholly aspirational and not linked to any listing requirements.
- Similarly, the Confederation of **Indian** Industry Code and the Stock Exchange of **Thailand** Code are designed to build awareness within the corporate sector of governance best practice, but are not, at this time, linked to stock exchange listing requirements.
- In contrast, **Malaysia's** Code on Corporate Governance, the Code of Best Practice issued by the **Hong Kong** Stock Exchange, and **South Africa's** King Commission Report on Corporate Governance, all contemplate mandatory disclosure concerning compliance with their recommendations.

### Kenya

Kenya is a country in East Africa. Potential gains or losses which hinge on proper management of corporations could be financially profitable or economically devastating. Interest by the general public in developing countries to invest in listed corporations is rising. For example, during June 2007, in Kenya, a country with a long tradition of a stock market

that is also undergoing the African Peer Review, an internet provider (Access Kenya), the first internet firm to list in East Africa, saw its listing on Nairobi's stock exchange oversubscribed by 363%. This oversubscription came from every category of investor – from individuals to institutional investors. Such a rise in public interest means more is at risk.

- **Steps taken by Private Sector Corporate Governance Trust (PSCGT) for handling corporate governance issues in Kenya:**

As part of a long-standing effort, the Private Sector Corporate Governance Trust (PSCGT) has launched an educational project to promote the importance of good corporate governance and the democratic principles of transparency, fairness, accountability and responsibility in Kenya's private sector. PSCGT will help foster sustainable economic development by working with shareholders and community leaders. This program will also assist in creating a new non-governmental association to defend shareholder rights in Kenya.

### **Thailand**

In Thailand, the Stock Exchange of Thailand (SET) first published 'Code of Best Practice for Directors of Listed Companies' in December 1997. However, most of the listed companies in Thailand are controlled by majority shareholders. The majority shareholders can appoint board members without approval of other minority shareholders through the majority vote. Therefore, the board of directors is often neither independent from management nor accountable to small shareholders. To tackle this problem, the SET requires that there must be at least two independent non - executive directors on the board in order to monitor the management of the company. An audit committee in Thailand is compulsory. In January 1998, the SET notified listed companies that they would have to form audit committees no later than December 1999, while newly listed companies would require them from the start. Such audit committees should comprise at least three directors, all of whom should be independent and at least one must have expertise in accounting or finance.

### **India**

In India, corporate governance initiatives have been undertaken by the Ministry of Corporate Affairs (MCA) and the Securities and Exchange Board of India (SEBI). The first formal regulatory framework for listed companies specifically for corporate governance was established by the SEBI in February 2000, following the recommendations of Kumarmangalam Birla Committee Report.

The Ministry of Corporate Affairs had appointed a Naresh Chandra Committee on Corporate Audit and Governance in 2002 in order to examine various corporate governance issues. It made recommendations in two key aspects of corporate governance: financial and non-financial disclosures: and independent auditing and board oversight of management. It made all its efforts to bring transparency in the structure of corporate governance through the performance of Companies Act and its amendments.

The 1991 crisis in India eventually led to the end of the license raj and economic liberalization.

### **Handling the situation after 1991 crisis**

Several positive developments have occurred on the corporate-governance front after this issue:

- The Securities and Exchange Board of India (SEBI) Act of 1992 created a regulatory body with the explicit mandate to improve the functioning of Indian financial markets.
- The incentives given state-run (public) financial institutions to monitor were improved. The resulting need to access public capital markets made them more aware of the bad loans on their balance sheets. Private-sector mutual funds were allowed to compete with the state monopoly.
- Restrictions on the entry of foreign investors were eliminated, and regulations on their investments were substantially clarified. Salient features included no limitations on minimum and maximum investments, no lock-in period for such investments, reduction in long- and short-term capital gains taxes

### **Handling the situation after Bhopal gas tragedy**

- The Indian Government passed the Bhopal Gas Leak Act in March 1985, allowing the Government of India to act as the legal representative for victims of the disaster representative for victims of the disaster.
- American legislators passed the Emergency Planning and Community "Right to Know Act" in 1986. Among other things, this law required industries to disclose the volume of certain this law required industries to disclose the volume of certain chemicals released annually by them into the environment.
- The Community Right to Know Act's approach provides citizens with access to information.

Development of norms and guidelines are an important first step in a serious effort to improve corporate governance. The bigger challenge in India, however, lies in the proper implementation of those rules at the ground level. More and more it appears that outside agencies like analysts and stock markets (particularly foreign markets for companies making GDR issues) have the most influence on the actions of managers in the leading companies of the country. But their influence is restricted to the few top (albeit largest) companies. More needs to be done to ensure adequate corporate governance in the average Indian company.

## **Sri Lanka**

In Sri Lanka, the concern for CG originated in the numerous company failures, especially finance companies, in the late 1980's and early 1990's, which caused investors to lose faith in the regulatory and semi-regulatory frameworks, as well as the standards of financial reporting. Accordingly, the Institute of Chartered Accountants of Sri Lanka set up a task force in 1992 (about the same time as the Cadbury committee in UK) to enforce Sri Lankan accounting standards, and then extended this initiative in 1996 (again before the East Asian financial crisis) to set up a committee to make recommendations on the financial aspects of corporate governance.

## **Solution for Pakistani companies**

- In developed countries handsome remuneration has been paid to INED'S, so they tend to be highly motivated and committed towards their organization, but the main issue is in Pakistan that most of the businesses are family owned, majority of the shares are held by one person, so they cannot afford INED because their personal interest can be suffered by doing so, most of the time the INED'S in Pakistani companies are hired on a relationship basis, like the brother of the main shareholder. So how is it possible that they will work without the influence of others, second, if the INED'S are selected, then the other issue is very minimal salary is paid in Pakistan, salaries are dependent on the number of meetings held by non-executive directors. These main hurdles are not making corporate governance successful.
- In developed countries, professional INED'S are hired, who have already worked as a professional INED in other companies. So they know how to handle the various issues of a company, and how to run governance, but as discussed earlier in Pakistan, companies are owned by a single person, and INED'S are selected on a relationship basis, so they are on paper INEDS but not actually, they are not enough educated to handle corporate governance issues, even if they are competent to handle different companies' meetings. So lack of education is another issue that is a great hurdle in the success of corporate governance.
- In Pakistan one thing they know is to simply pass a Law or prepare a code of conduct and to decorate it in their books of shelves, not put any focus on implications, by preparing a code of conduct, problems cannot be resolved until and unless it is properly implemented with its full spirit, developed countries not only prepare law, but also they are deeply concerned with its implications.
- The third issue in Pakistani context is that they treat all the directors on the same level, they do not make any difference in the liabilities of executives and non-executives, there were some cases in Pakistan, some wrong decisions are taken by management, but the entire board were

taken by the court. Such incidences further discouraged professionals from accepting to serve as INEDs.

- In Pakistan investing institution, did not take any part in voting, so major shareholder appoint IND's with their own will, on the other hand, in USA , the situation is entirely different, not only institutional investors take active part in voting the INEDs, but also fully support them, and after nomination, they also provide professional training to run corporate issues.
- Laws and codes are available but are not implemented in the true sense. In Pakistan majority Directors want to keep their companies affairs in their own hand. They are not interested to implement codes properly. They don't want to create culture of independent directors to protect their own interest.

### **Why the solutions adopted by the developed countries are not likely to be effective in the Pakistani milieu**

Corporate Governance is not as effective in Pakistan as in the Developed countries. The main reason of this ineffectiveness is the nature of the ownership of the companies. In the developed countries the owners of the companies have very minimum fraction of shares. After the origin and the realization of the importance of the Corporate Governance companies adopted the culture of Corporate Governance and get their best positions in their market as well as in the whole world. In the start it was quite difficult for them also but through the continuous effort and consciousness toward the whole stake holders they achieved their best. The major causes because of which Pakistan couldn't attain that position even after the implementation of same policies can be as:

- Inequitable treatment of Shareholders
- Insecurity of Interests of other Stakeholders
- Irresponsible Boards
- Unethical and disgrace Behaviors
- Lack of transparency in the Financial Disclosures

### **Inequitable treatment of Shareholders**

In Pakistan the business are family oriented and the whole power lies under the governing family. The minority shareholders do not have any right to participate in the decisions and they also do not unite to elect any nominee in the board for the protection of their rights and the interests. The owners or the majority shareholders always go for those decisions which are directly in favor of them. Inactiveness or the lack of unity in the minority shareholders and the negligible interest towards the matters of the company is the root cause of this discrepancy.

### **Insecurity of Interests of other Stakeholders**

Stakeholders other than the shareholders are not as powerful to protect their interests in the under developing countries like Pakistan. Employee's works for long hours on the minimum wages, suppliers and the customers are not satisfied with the behaviors of the company and the uppermost problems is the wastage which the industries are emitting in the environment. This injustice behavior of the one part of the stake holders toward the others is the main reason of failure of the Corporate Governance in Pakistan.

In Pakistan Individuals or the entities which are responsible for the rights of the human resource and the environment are not active. The reason behind this can be the irresponsible behaviour of Government toward these matters. Government must pay attention because of the increasing Global Warming due to the wastage emitted by the factories and the over utilized machinery used in the factories is going to be more dangerous for the human lives.

### **Irresponsible Boards**

Shareholders having the maximum percentage of shares are assumed to have the voting right and the selection of the Board of Directors. These shareholders are in the closed group and always elect the people as Directors which become always in the favor of them. Many times the Directors even do not know that they are the Directors of the company means companies just fulfill the requirement imposed by the law without realizing the worth of Independent Directors for the success of the company. The people so called Directors do not have any authority to take any action against the falsified actions taken by the company. It is said that the as per the requirement companies have the at least one third of the board of directors independent but it is only in words not in the spirit.

### **Unethical and Disgrace Behavior**

Ethics and the business are assumed two different entities. Companies do their businesses in their own way without considering the effects and take some other initiatives for the betterment of society and assumed that they are ethical and socially responsible. While in The Developed countries ethics are incorporated in each and every decision they made. Companies are not socially responsible and they do not put any attention towards the damages which are being happened because of their operations. Companies always prefer to minimize their costs and increase their profits. The fertile lands are being declared as the industrial and residential areas, chemicals are continuously damaging the fertility of the soil and the lives of the people who live near those factories are surviving through severe types of diseases.



### **Lack of transparency in financial Disclosures**

Companies do not portray the actual financial positions and always show the flowery picture which effect the decision of every person directly or indirectly associated with the company or interested to have any interaction in the company in future as well. Internal and the external auditors are always in the hands of the majority shareholders and do not oppose the expectations of the owners and they also earn handsome compensations for these favors.

These can be the uppermost reasons of the ineffectiveness of the policies in Pakistan which are common and being adopted by the companies in Pakistan as well as in the developed countries. There are some other problems as well but if the companies take initiatives for the resolution of these problems this will be the first step toward the culture of the Corporate Governance.

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