Chapter 16
Current Board of Directors' Practices in Saudi Corporate Governance: A Case for Reform

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Abstract This chapter examines the current board of directors' practices in Saudi corporate governance. It highlights a variety of significant aspects of boards of directors, as internal institutions of the corporate governance system. For example, the chapter contains details of the board members' duties, the boards' responsibilities and creation of standards, the separation of the board members' powers, board membership categories, board meetings, board sub-committees (such as audit committees and nomination and remuneration committees) and board members' compensations. All these aspects are referenced from the Corporate Governance Code (hereafter CGC), the Company Law (hereafter CL) and the case law connected to them. The paper's methodology is analytical and adopted a comparative approach with the successful international corporate governance codes, such as the OECD principles of corporate governance, the UK Companies Act, the Cadbury report and the Greenbury report, in order to reform the board of directors' practices in the Saudi corporate governance framework.

16.1 Introduction

The corporate board is believed to be a significant entity of the internal institutional framework for corporate governance (Abdel Aal 2005). Therefore, the board should act appropriately, either toward stakeholder groups (including the shareholder group) or to the corporation. This paper will debate the main research question, which relates to the current practices of the Saudi corporate governance regarding the board of directors. This paper is therefore divided into a number of sections. The first section addresses the board members' duties, and the second considers the board's responsibilities. The creation of the board is examined in Sect. 16.3. The

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separation of the board members' powers is emphasized in Sect. 16.4, and board membership categories are discussed in Sect. 16.5. The board meeting is appraised in Sect. 16.6. Next, Sect. 16.7 analyses the board sub-committees by focusing on two substantive committees: the audit committee and the nomination and remuneration committee. The board members' compensations are explored in Sect. 16.8. Finally, a summary is given.

16.2 Board Members' Duties

16.2.1 General Overview

It is thought that due to the extensive power conferred on the corporation directors in addition to managing the corporation, there is an opportunity for directors to depart from the corporation's purposes and mismanage the corporation. As a consequence, international corporate governance principles have composed and identified a variety of board members' duties in order to ensure that these board members are directing the corporation properly and accurately as regards the corporation policies, and are satisfying the corporation targets. In particular, there are company law jurisprudences in which the law clearly states that the association between the corporation and its board members is a principal-agent association which encourages board members to owe the corporation, the well-known expression being 'fiduciary duty' (Kamal 2001). Board members are fiduciary agents; hence, their powers should be implemented not only as required by law, but also for the benefit of the corporation as a whole (Malcolm 1997).

This association between the corporation and the board members, based on the principle-agent association, is not referred to under either the CL or CGC provisions. Moreover, the fiduciary duty is not recognized by these pieces of legislation. This is supported by evidence that the idea of the fiduciary duty is immature in the Middle East. In the US, for example, the use of the term 'fiduciary' is evaded regarding board members of corporations. This is because board members have commitments that are related to the duty of loyalty; a duty to act responsibly with regards to the power they hold and to carry out their duty of care. Accordingly, use of the term 'fiduciary' to define numerous entirely different obligations simply complicates the issue (Al Rimawi 1999).

However, in literature, the fiduciary duty is divided into three major duties, comprising the duty of care, the duty of loyalty and the duty to act within one's power. This is sustained by the OECD principles of corporate governance (2004), which declare that there are two important origins of the fiduciary duty of board members: the duty of care and the duty of loyalty, providing that: "Board members should act on a fully informed basis, in good faith, with due diligence and care, and in the best interest of the company and the shareholders." (p. 59.)

This section will attempt to investigate whether the board members' duties provided for in the CGC and the CL are appropriate for guaranteeing that board members will not disobey the rules, or whether reform is required to enhance the current board of directors' practices in Saudi corporate governance. Accordingly, these duties will be covered by focusing on the duty of care, the duty of loyalty and the duty to act within one's power.

16.2.2 Duty of Care

The duty of care is one of board members' greatest duties in accordance with the power that they have to direct their corporation and to fulfill their responsibilities in the best interests of the shareholders and the corporation, equally. In so doing, board members should carry out their responsibilities with sensible care and skill in terms of making contractual decisions. Accordingly, their duty of care takes place within several international jurisprudences. For example, the UK Companies Act states that it is necessary for people to act with a degree of skill and care that may be reasonably expected from people of their knowledge and experience (Hicks and Goo 1994). The UK Companies Act, therefore, uses a subjective measure to decide whether board members are in violation of the duty of care that they owe to their corporation (Griffin 2006).

In the Saudi case, the board members' duty of care has not been clearly specified in either the CL or the CGC. This simply means that the Saudi regulator finds both pieces of legislation futile when it comes to stipulating the measure of care for the corporation's board members. To put it differently, it is difficult to hold board members responsible for violations of their duty of care under Saudi legislation, even though the CL has identified two primary board member responsibilities; namely civil and criminal liabilities against breaches such as management malpractice and cheating (Al Ghamdi 2007).

Additionally, Article 75 of the CL of 1965 stipulates that the corporation should be bound by all the acts performed by the board of directors within the limits of its competence. The corporation should also be responsible for damages arising from unlawful acts committed by directors in the administration of the corporation. It seems that under this Article, board members are immune when they make mistaken decisions, even if these decisions are made deliberately. Therefore, the Saudi regulator should clarify the board members' liabilities regarding duty of care under the CL, and add this to the CGC. As a matter of fact, the Saudi regulator can adapt the duty of care concept and definition from other international jurisprudences, such as the UK Companies Act of 2006, section 174, clauses 1 and 2 which point out the duty of care clearly and sensibly:

> A director of a company must exercise reasonable care, skill and diligence. This means the care, skill and diligence that would be exercised by a reasonably diligent person with the general knowledge, skill and experience that may reasonably be expected of a person

carrying out the functions carried out by the director in relation to the company, and the general knowledge, skill and experience that the director has.

16.2.3 Duty of Loyalty

The term 'duty of loyalty' is the principle of the fiduciary that the board member has a duty of loyalty, which is defined as the prevention of conflicts of interest and insider trading. It is affirmed that board members are expected to exercise a duty of loyalty toward the corporation and its shareholders. In addition, board members should not indulge in any conduct that would be unfavorable to the interests of the corporation. Consequently, the duty of loyalty is challenged by the well-known conflict of interest within board situations and insider trading (Al Ghazali 2008).

Conflict of Interest Within the Board

Conflict of interest within the board is generally understood to mean any situation that may affect the neutrality of a member's decisions due to personal interests (both material and moral) or those of his or her relatives (Al Ghazali 2008). In other words, a conflict of interest arises when the board member comes across circumstances where there is the possibility of formal exploitation or stimulus affecting private interest (Demski 2003).

The concept of conflicts of interest within the board came into legal existence in the eighteenth century, when the US court of law assumed the prohibition statute in a conflict of interest case, notwithstanding the operation's objectivity or wrongness (Marsh 1996). Soon afterwards, the UK House of Lords followed the US' attitude towards the board member's conflict of interest case (Pennington 1989). After this, the conflict of interest situation was not taken to be obstructive, as the case was deemed effective as long as it was agreed on by a majority of disinterested board members (Block et al. 1993). Current international practice is in support of certifying some conflict of interest cases. However, this support is dependent on particular restraints that should be implemented. Otherwise, board members found to be in breach of a conflict of interest will be considered guilty and punished, either by having a fine imposed upon them or by being given another sentence for their breach (Demski 2003).

Endorsements of conflicts of interest within the board (i.e. the duty of loyalty) by board members differ across various international legal structures. In some European legal structures, the preparation against breaches of conflicts of interest involves precise recompense for the corporation for the damage that occurs as a consequence of the conflict of interest within the board by the board member. Moreover, breaches of conflicts of interest within the board in the US and the UK are stricter than the compensation in some of the European legal structures, as stated above, because the US and the UK instruct a particular disclosure and transparency measure when there is a submission involving a conflict of interest within the board situation (Enriques 2002).

Conflicts of interest between board members and their corporations can occur in several ways, such as when there is a submission between corporations and their directors, or when there is a submission between the corporations and third parties, while at the same time a board member has a personal interest in the matter (Enriques 2002). It is argued that decisions taken in support of the corporation should be made exclusively for the profit of the corporation. Sensibly, these decisions taken should not be made with a view to obtaining particular personal subsidy for the board members and top executives. For example, the conflict of interest situation may occur when board members are selling their own property to their corporation, or because they are discussing a contract under which their corporation will fund them (Pettet et al. 2009).

There is a debatable viewpoint regarding conflicts of interest. This argument considers that those on the board who are likely to have a conflict of interest are notably the non-executive members, since they are not wholly independent. For instance, non-executive members often possess shareholdings and options in the corporation (Enriques 2002). Moreover, non-executive members may encounter a conflict of interest when taking a director's post in two competing corporations, as their responsibilities for one may conflict with those for another. It appears that non-executive members, who participate either commercially or for private gain by being non-executive members of a competing corporation, would be in danger of being found to be in abuse of their duty of loyalty. Therefore, they should cease any conduct that purposely harms the corporation (Pettet et al. 2009).

It is estimated that non-executive members are those who are encouraged to occupy the board and the board sub-committees' seats, either by the Saudi legislator or other international corporate governance legislators (Article 12-C of the Corporate Governance Code 2006). Therefore, being a non-executive member does not prevent the occurrence of conflict of interest cases which cannot be tackled in the absence of strong regulations governing these cases. Conflicts of interest within the board in the Saudi case, however, do not contest the argument that non-executive members are the most vulnerable to conflicts of interest within the board. This is obvious, as the board members, either executive or non-executive, in the law cases that will be analyzed in this section were in breach of conflict of interest within the board.

In particular, Saudi legislation has established the meaning of conflict of interest from the enacting of the CL of 1965. As a consequence, the clauses regulating conflicts of interest within the board found under the CGC are derived from Articles 68 and 69 of this law without modification. As a new restraint by the compulsory Article 10-B of the CGC, the corporation board should create a written rule that concerns any corporation assets and the illogical disposal of them stemming from dealing with related groups, and this should resolve conflicts of interest within the board and treat any probable submissions of the conflicts of interest of the board members.

Furthermore, Article 18-A of the CGC affirms that a board member may not have any interest, whether directly or indirectly, in the transactions or contracts made for the account of the company, except with authorization from the ordinary general meeting, which is to be renewed annually. Transactions made by way of public bidding are, however, excluded from this restriction if the board member has submitted the best offer. In particular, the board member should declare to the board any personal interest he or she may have in the transactions or contracts made for the account of the company. Such declarations should be recorded in the minutes of both the corporation general meeting and the board meeting. The interested board member may not participate in voting on the resolution to be adopted in this respect. More to the point, the board chairman must inform the ordinary general meeting, when it convenes, of the transactions and contracts in which any board member has a personal interest. Such communication must be accompanied by a special report for the company's external auditor. However, section 175 Articles 1 and 2 of the UK Companies Act outline conflicts of interest as follows:

> A director of a company must avoid a situation in which he has, or can have, a direct or indirect interest that conflicts, or possibly may conflict, with the interests of the company. This applies in particular to the exploitation of any property, information or opportunity (and it is immaterial whether the company could take advantage of the property, information or opportunity).

A well-known legal case of conflict of interest concerned a decision by the board chairman and the board members of the Saudi Chemical Company to purchase 15 % of the shares of one of the company's subsidiary groups without informing the company's general meeting, despite the chairman having an interest in the transaction. In addition, the Saudi Chemical Company failed to announce that the transaction was associated with a related group, either on its website or on the stock exchange website. As a result, the Capital Market Authority Board imposed a fine of $13,333 dated 2009 on the board chairman and each board member. The verdict was in connection with Article 28 of the Listing Rules (2004), which indicates that: "The directors of a company should exercise their powers and carry out their duties in such a way as to serve the interest of the company."

It is suggested that the fines enforced by the Capital Market Authority Board on each board member should have been higher. The board chairman, particularly, should have been fined $26,666, because he had an aggregate interest in the transaction and is supposed to be responsible for safeguarding the shareholders' interests. The sentence also seems strange in light of the fact that the board chairman was prevented from participating in the listed corporation's board meetings for a period of time, as this punishment is stipulated in the Capital Market Law (hereinafter CML). Article 59-A- of the CML (2003) assures that "Barring the violating person from acting as a broker, portfolio manager or investment adviser for such period of time as is necessary for the safety of the market and the protection of investors."

In this case, the Capital Market Authority Board punished the board chairman and the board members for being in breach regarding the conflict of interest situation. The board chairman and all the board members were not actually conducting insider trading, which is regulated by Article 50-A of the CML. Rather, they were simply trying to hide the transaction, because they did not first obtain authorization at the ordinary general meeting to complete the transaction. In addition, the board chairman was served by the board members to conduct this transaction because he had a personal interest, as stated above.

Nevertheless, Article 18-B of the CGC confirms that board members may not, without annually renewed authorization from the ordinary general meeting, participate in any business or enterprise that is in competition with the company, or engage in any commercial activities conducted by the company. Otherwise, the company has the right either to claim damages from them or to consider the operations they have conducted for their own account as having been conducted for the account of the company.

A classic law case concerned the *Methanol* Chemicals Company general meeting, which dismissed a board member suspected of a conflict of interest in 2008. In fact, the removal was enforced after the suspended board member was given a period of 3 months in which to finish his private competing application that was completed against the company's works, but failed to do so. The removal of the board member by other board members was consistent with Article 18-B of the CGC. It is astonishing that the board members of the *Methanol* Chemicals Company dismissed the board member on the grounds of conflict of interest due to having prior permission to act, as he had indeed obtained this from the company's ordinary general meeting. This notwithstanding, the decision was made without any interference from the Capital Market Authority Board. However, it appears that the Capital Market Authority Board should have imposed a fine on the removed board member.

Altogether, with regard to Articles 18-A and 18-B of the CGC, it can be supposed that the CGC has made some exceptions that are not counted as a conflict of interest within the board, as follows:

I. When the board member has received prior permission from the corporation's ordinary general meeting to act, which should be renewed on a yearly basis.
II. When the board member informs the board and the shareholders about any private undertakings and commercial agreements that he or she has accomplished for the corporation.
III. When the board member is the primary bidder through the general bidding.

It can be noted that the issue of informing the other board members and shareholders regarding conflicts of interest has been discussed internationally. For example, the declaration of a board members' interest has been conditioned under section 177, Article 1 of the UK Companies Act. It upholds that if a company's board member is in any way, either directly or indirectly, interested in a planned submission with the company, he or she must announce the nature and the extent of his or her interest to the other board members.

In particular, the CGC exclusions are strongly disputed, as they reflect good corporate governance practices. As Prairie (2007) maintained, the general bidding exception to be completed by board members when they are the optimal bidders is an unnecessary exception by the Saudi legislator. Prairie further stated that board members' offers in general bidding are undoubtedly likely to be the most successful offers to win the general bidding, because the board members are expected to be familiar with the corporation's information and affairs. It is consequently observed that these exceptional terms are not needed at all, as they damage equality and accountability, thereby permitting a monopoly by the board members. Additionally, the CGC has meaninglessly opened a door to board members to trade in their corporations' contracts. For this reason, it is considered that these exceptional terms should be removed from the CGC in order to avoid misrepresentation by the board members and top executives.

This is in accordance with the idea that the avoidance of conflicts of interest within the board (i.e. the duty of loyalty) would be accomplished by the board members being prevented from either going into a conflict of interest with the corporation or competing with the corporation (Shane 1999).

Once again, the conflict of interest permits unlawful monopoly by board members. The following instance is an example of conflicts of interest within the board. The *Herfy* Company announced its ordinary general meeting agenda, with the meeting due to be held on 29th March 2012. The general meeting agenda consisted of several issues, the most important of which was the approval of the transactions and contracts to be made with related groups during 2011, and licensing for the following year, including the approval of land leases and the rental of residential buildings worth an annual $208,000 from the chief executive, who was also a board member. The chief executive owned 20 % of the corporation's share capital and was therefore one of the corporation's major shareholders. Form this example, the conflict of interest within the board is very obvious; the chief executive stood to make private interest on his own behalf with the approval of the corporation's ordinary general meeting. In reality, there was no excuse for him to trade and take advantage of the company where he was the chief executive and held a significant number of shares.

Insider Trading

It is known that when board members trade in the securities of a company in which they are an insider, their actions are subject to rules under numerous diverse legal concepts. However, the board members have a fiduciary duty to this corporation, so if they practice information expected as a consequence of their inside capability for personal return, they are obliged to disclose their advantages to the corporation (Yoran 1972). In particular, Franks (1981) suggested that insider trading takes place when board members do not gain direct benefit from some other party to a contract. Instead, the board members use their knowledge and experiences to buy or sell shareholdings in the company or to deal on the stock exchange. Both Saudi legislation and Article 50-A of the CML have identified and defined insider trading as:

> Information obtained by the insider and which is not available to the general public, has not been disclosed, and such information is of the type that a normal person would realize that in view of the nature and content of this information, its release and availability would have a material effect on the price or value of a security related to such information, and the insider knows that such information is not generally available and that, if it were available, it would have a material effect on the price or value of such security.

The UK Companies Act, however, makes no mention of insider trading except that it refers to what was stated under section 52 of the Criminal Justice Act of 1993. This act defined this situation as follows:

> An individual who has information as an insider is guilty of insider dealing if, in the circumstances including when [the acquisition or disposal in question occurs on a regulated market, or that the person dealing relies on a professional intermediary or is himself acting as a professional intermediary] he deals in securities that are price-affected securities in relation to the information, and if he encourages another person to deal in securities that are (whether or not that other knows it) price-affected securities in relation to the information, knowing or having reasonable cause to believe that the dealing would take place in the circumstances mentioned above or he discloses the information, otherwise than in the proper performance of the functions of his employment, office or profession to another person.

Section 61 of the UK Criminal Justice Act further stipulates that the Secretary of State or the Director of Public Prosecutions has the right to consent to the handover of the insider dealing to the prosecution. It states that:

> An individual guilty of insider dealing shall be liable - on summary conviction, to a fine not exceeding the statutory maximum or imprisonment for a term not exceeding six months or to both; or on conviction on indictment, to a fine or imprisonment for a term not exceeding seven years or to both.

It is vital, when analyzing Saudi law cases, to understand how the Capital Market Authority Board and the Committee for the Resolution of Securities Disputes (hereinafter CRSD) are able to detect insider dealing. The first legal case of insider trading was issued by the CRSD, issued decision, No. 289-L-D1-2008, dated 8th July 2008, which punished a board member of the Saudi Hotels and Resorts Company with a combined punishment that prohibited the defendant from working with listed corporations for 3 years and imposed a fine of $26,666. The punishment was in accordance with Article 59-A of the CML, which stipulates that:

> If it appears to the Capital Market Authority that any corporation or person has engaged, is engaging or is about to engage in acts or practices constituting a violation of any provisions of the Capital Market Law, or the regulations or rules issued by the Capital Market Authority, or the regulations of the stock exchange, the Capital Market Authority Board shall have the right to bring a legal action before the Committee for the Resolution of Securities Disputes to seek an order for the appropriate sanction that includes barring from working with companies whose securities are traded on the stock exchange.

This case, furthermore, corresponds to Article 59-B of the CML:

> The Capital Market Authority Board may request the Committee for the Resolution of Securities Disputes to impose a fine upon any corporation or person responsible for the violation of the Capital Market Law, its Implementing Regulations and the regulations of the stock exchange. The fine that the Committee for the Resolution of Securities Disputes

can impose shall not be less than $2.666 and shall not exceed $26.666 for each violation committed by the defendant.

In fact, while chairman of the Saudi Hotels and Resorts Company board; the defendant purchased a large number of shares from another corporation that was being taken over by the Saudi Hotels and Resorts board. Hence, he bought these shares in accordance with his position. Furthermore, he was the main official undertaking the negotiations, and signed on behalf of the aforementioned company. As a result, the punishment was in line with Article 50-A of the CML, which advocates that:

Any person who obtains, through family, business or contractual relationship, inside information is prohibited from directly or indirectly trading in the security related to such information, or to disclose such information to another person with the expectation that such person will trade in such security.

It is thought that the sentence and the fine were lawful as they punished the chairman of a listed corporation; a harsh punishment that was appropriate to his malpractice, imposed in a way that reflected his position regarding obvious insider trading. Nevertheless, the CRSD should have forced the company's chairman to repay the interest he gained from the transaction, but it did not do so.

The second legal case of insider trading was issued by the CRSD, issued decision, No. 323-L-D1-2008, dated 11th November 2008, demanding that a board member of the *Gassim* Agricultural Company repay the interest he accrued, comprising approximately $899,299, to the Capital Market Authority. The defendant was also prohibited from working in a listed corporation for 3 years and fined $26,666. The board member was sentenced in accordance with Articles 59-A and 59-B of the CML. Article 3-M of the Merger and Acquisitions Regulations provides further definition:

Such an insider trading would arise if the director had, directly or indirectly, an interest (including his shareholding in the offeree company, if the director is a director of the offeror company, or his shareholding in the offeror company, if the director is a director of the offeree company) or duty (including where the director of the offeror company holds a position of a director or a manager of the offeree company, and where the director of the offeree company holds a position as a director or a manager of the offeror company) which is material and which conflicts or may conflict with the interests of the company.

Thus, the defendant was a board member of the *Gassim* Agricultural Company. He purchased a large number of shares in another corporation when it was being taken over by *Gassim* Agricultural Company. He obtained these shares for six family members (his sons and daughters) in accordance with this submission. Consequently, the punishment was in pursuant to Article 50-A of the CML, and the sentence and fine are surely lawful. This case also confirms that insider trading can extend to board members' relatives even if the board members have nothing to do with the dealing themselves, because they are committing fraud and not considering the company's and the shareholders' interests at all in favor of their relatives' interests.

The most significant case of insider trading was the final verdict of the CRSD, dated 17th August 2009, which pronounced a combined punishment against a board chairman of the *Bishah* Agriculture Development Company. The punishment comprised a combination of imprisoning him for a period of 3 months, forcing him to repay to the Capital Market Authority a total amount of money equal to $14,050, fining him $26,666 and preventing him from working with listed corporations for 3 years. The board member in question was guilty of insider trading in this company by selling and purchasing shares while being the board chairman of this company. The verdict of the CRSD was in accordance with Article 50-A of the CML. Significantly, this was the first time that the punishment of imprisonment had been applied by the CRSD. There was strong rejection regarding this punishment by corporate governance observers in Saudi Arabia, who considered that the CRSD should not apply the punishment of imprisonment. That is to say, they believed that as the CRSD is a quasi-judicial committee, it should not be allowed to impose harsh punishments such as imprisonment.

By law, Article 57-C of the CML provides the CRSD the right to sentence individuals who have caused a lot of damage to the stock exchange, and who have committed insider trading, to imprisonment for a certain determined time of not more than 5 years, as is usually mentioned in the final verdict of the case. However, Article 59-B of the CML offers the CRSD the right to impose a criminal sanction like imprisonment in order to resolve any violation of the CML and the Implementing Regulations. In fact, the final verdict of the CRSD was given after allowing the accused person a period of 30 days to appeal in front of the Appeal Committee for the Resolution of Securities Conflicts, which he failed to do. As a matter of fact, the defendant submitted the case before a general *Shari'a* court to be sued, but the court refused to accept and file the case. The case was rejected because the general *Shari'a* court is not responsible for these kinds of capital market cases, and because the Saudi regulator has assigned these kinds of cases to be heard by the CRSD. In addition, the defendant did not accept the idea that his case would be seen by the CRSD, which is a quasi-judicial tribunal. The defendant also refused to repay three times the sum he obtained from the transaction to the Capital Market Authority. In contrast, Article 64 of the CML provides the individual who has committed insider trading with a way to avoid imprisonment. It concludes that:

> A person charged with violation of insider trading may avoid proceedings before the Committee for the Resolution of Securities Disputes by reaching an agreement with the Capital Market Authority pursuant to which he agrees to pay the Capital Market Authority a sum not exceeding three times the profits he has realized, or three times the losses he has averted by committing the violation. Such arrangement shall be without prejudice to any compensation awardable as a result of the violation.

This case reveals the seriousness with which the CRSD treats any detected malpractice carried out by the board members or top executives of listed corporations. It holds that the violated board chairman deserved the combined punishment, as he breached lawful clauses of the CML. It seems that imprisonment can sometimes be a significant punishment used to tackle any irresponsible conduct that harms capital market equity, but it should be accomplished and imposed by the

Saudi Criminal Prosecution rather than the CRSD. Significantly, the punishment of imprisonment, as stated above, can be obviously found in other international jurisprudence against insider trading, such as UK jurisprudence.

16.2.4 Duty to Act Within the Powers

The board members' duties are essential corporate governance aspects because the board members in several jurisprudences hold extensive power. In addition, the board members' legal responsibilities are subject to being increased because of these duties in the company presentation (Yuwa 2006). However, the board members' extensive powers are in accordance with significant restrictions, such as those enforced by law, those enforced by the corporation constitution and those enacted by the general meeting determinations (Grantham 1993). In this regard, it can be seen that the board members' powers in the UK have been clearly limited under the UK Companies Act, which emphasizes the duty of directors to act within their powers. It provides that the board members' powers should be in line with the corporation management subject to the UK Companies Act provisions, the corporation articles of association and any resolution generated by the corporation's general meeting. Section 171, clauses A and B of the UK Companies Act insists that "A director of a company must: act in accordance with the company's constitution, and only exercise powers for the purposes for which they are conferred."

Comparably, Article 72 of the CL has recognized the board members' delegation and limitation of powers. It confines the board members' powers to the CL provisions, to the corporation's articles of association and to a resolution enacted by the corporation's general meeting. It also limits the board members' powers with regard to financial matters. It reads that with due regard to the prerogatives vested in the general meeting, the board of directors enjoys full powers in the administration of the company. The board should be entitled, within the scope of its capability, to delegate one or more of its board members to perform an act or certain acts. Nonetheless, the board of directors may not sell or mortgage property or the place of corporation, or relieve the debtors of the corporation from their obligations, unless so authorized in the corporation's articles of association and the provisions of the CL.

In particular, Article 13-B of the CGC gives the board of directors the right to delegate one or more of its responsibilities to other groups to fulfill. For instance, the board of directors can delegate some of its work to its sub-committees, such as the audit, nomination and remuneration committees. Nevertheless, permitting the board to delegate some of its responsibilities in accordance with Article 13-B does not mean that the supervision of these sub-committees and their works is decreased. It has been advised that the board must summarize the general procedures for founding such committees, demonstrating their responsibilities and supervision by the board. Specifically, the sub-committees must inform the board about their submissions and results in order to ensure that the delegated culpabilities are perfectly in place.

This means that the board has the right to delegate some of its jurisdictions to one or more of its sub-committees, thus fulfilling its role. In general, therefore, it appears that board sub-committees are not able, under any circumstances, to restore the board, because the latter shoulders the critical responsibility for the corporation's submissions and contracts, even if the board sub-committees are significant and are seen to be performing well (CGC 2006). Nevertheless, this right of the board is delimited by notable aspects; the delegation of determined work should be within the board's jurisdiction and should be based on the duration and form of operations. Otherwise, the delegation is null and void (Al Urban 2006).

On the other hand, Article 18-C of the CGC recommends that a company may not grant any cash loan whatsoever to any of its board members; nor may it guarantee any loan contracted by a member with a third party. Arguably, the CGC clause is fair, as it safeguards the shareholders' capital and secures the corporation's financial position in terms of random and superfluous private mortgages to the board members. Specifically, it is said that a corporation mortgage is open to abuse by a board member. The mortgage may be at an idealistically low rate of interest, and therefore mask compensation or a gift.

The prohibition against rendering a cash mortgage is clearly evident under section 197, Article 1 of the UK Companies Act, which asserts that a company must not offer a loan to a company's board member or one of its holding companies. The company may also not provide an agreement or security regarding a loan made by any person to such a board member, unless the submission has been ratified by a determination of the company's members.

16.3 Board Responsibilities

The Saudi regulator recognizes the significance of the board of directors as a body whose fundamental mission is to drive the corporation in order to achieve its social and commercial targets (Al Muneef 2006). This is obvious when reviewing the CGC and the CL provisions, which pay considerable attention to board responsibilities, and, in addition, guard the interests of the corporation, as well as those of the shareholders. It is also apparent that the Saudi regulator views the board as a good way of enhancing corporate governance practices among exchange and listed companies. Thus, Saudi consideration agrees with international corporate governance principles, which regard the board as the first means of applying good practices. The OECD principles of corporate governance maintain that:

> The corporate governance framework should ensure the strategic guidance of the company, the effective monitoring of management by the board, and the board's accountability to the company and the shareholders.

Moreover, the Cadbury report (1992) refers to the effectiveness of the board:

> Tests of board effectiveness include the way in which the members of the board as a whole work together under the chairman, whose role in corporate governance is fundamental, and their collective ability to provide both the leadership and the checks and balances which effective governance demands.

The board, in particular, has the freedom to oversee executive management, and with that, it should also consider the significant corporation functions and enhance its value on behalf of the shareholders. Furthermore, the board should observe all tasks completed by executive management with the intention of replying to any submitted enquiries from the shareholders (Heath and Norman 2004). The board, by way of illustration, acts as a watchdog by either accepting or refusing the corporation's policies, such as incentive schemes and contracts that would provide support to the executive managers instead of acting on the shareholders' behalf (Solomon and Solomon 2004). The board quality is specifically a demanding element, side by side with the corporate governance framework, which achieves strategic business flexibility (Hussain and Mallin 2003).

Nonetheless, Articles 10 and 11 of the CGC both assign several responsibilities to the board of directors in terms of running the company as a going concern. These board responsibilities are as follows: Firstly, the board members' jurisdictions are clearly stated in the company's articles of association. Additionally, these jurisdictions must be completed in a way that is liable and in good standing. The board decisions should depend on satisfactory information from the company's executive administration or from any other trust sources. This in fact goes together with demanding the duty of good faith from the board member. Comparably, this has been stated under section 172, Article 1 of the UK Companies Act, which reveals that "A director of a company must act in the way he considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole."

Secondly, Article 11-C of the CGC states that all the board members should act on behalf of both the shareholders' and the company's interests, so they should avoid isolation from the shareholders, either individually or as a group. It is therefore obvious that the Saudi regulator has a significant role in relation to the board and the board members' behavior, as the board members should avoid any segregatory conduct towards shareholders, specifically when obtaining information and annual accounts, as well as when voting at the corporation's general meeting.

Thirdly, Article 11-F of the CGC statuses the new board members should be trained – by the board if necessary – to ensure adequate awareness of their jurisdictions. The Saudi legislator pays great attention to the Cadbury report. It advises, in its suggestions for training new board members, that they should be entitled to attend various internal and external training programmes, and should be given an introduction to the corporation's interactions. It does not matter whether they are executive, independent or non-executive board members, as long as they do not have previous board experience. Board members are expected to be highly skilled in order to accomplish their obligations reasonably and properly (Carcello 2009). Certainly, a board which is comprised of highly skilled members such as lawyers, accountants and economists is able to gain several advantages on the corporation's and the shareholders' behalf (Filatotchev and Boyd 2009). In practice, the majority of listed companies announce on the exchange's website and on their own websites any vacant board member seats. Moreover, these listed companies have recently asked for highly qualified board members who are knowledgeable of the CL, the CML and the Implementing Regulations, including the CGC. This method is clearly supported by Article 29 of the Listing Rules, which advises that good-standing auditors, financers and accountants should occupy the board seats. For example, the *Nama* Chemicals Company lately advertised that due to the expiration date of the current board of directors, the company desires board members who are familiar with the above-mentioned regulations.

Fourthly, Article 10-A of the CGC shapes that the board must consent to and direct the company's technical policies. Therefore, the board:

1. Arranges a complete policy for the company, the primary work plans and the rule of risk management, as well as evaluates these policies regularly.
2. Highlights the most suitable capital formation of the company, identifies the company's financial aims as well as ratifies its budgets.
3. Expresses the basis capital costs of the company and acquirement with disposal of assets.
4. Sets the targets to be achieved and monitors the operation of these targets as well as the overall performance of the company.
5. Examines the managerial and purposeful formation of the company on a periodic basis.
6. Annually reviews the usefulness of internal control by ensuring the reliability of financial and accounting proceedings, including the preparation of financial reports.

Finally, Article 10-B-1 of the CGC assumes that the board creates a written policy that legalizes the relationship with all the beneficiaries of stakeholders, in addition to securing their rights. Clearly, this official objective of the CGC showcases the extent to which it has promulgated a diversity of worldwide corporate governance standards, as having a clear and positive relationship with all the stakeholder groups is one of the major OECD principles of corporate governance. The OECD states that:

> The corporate governance framework should recognize the rights of stakeholders established by law or through mutual agreements and encourage active co-operation between corporations and stakeholders in creating wealth, jobs and sustainability of financially sound enterprises.

In this respect, section 172, Article 1 of the UK Companies Act points out that:

> A director of a company must act in the way he considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole, and in doing so have regard (amongst other matters) to the likely consequences of any decision in the long term, the interests of the company's employees, the need to foster the company's business relationships with suppliers, customers and others, the impact of the company's operations on the community and the environment, the desirability of the company

maintaining a reputation for high standards of business conduct, and the need to act fairly as between members of the company.

Furthermore, such an approach should be clearly written down by the corporation board in terms of creating a legalized relationship with all the stakeholder groups. This can inspire the board to respect its statutory and contractual obligations for the benefit of all stakeholders; namely the shareholders, lenders, suppliers, borrowers, employees and society as a whole. Article 10-E of the CGC insists that this written policy, importantly, includes the following:

(a) Mechanisms for compensating the stakeholders in respect of breaching their rights under contract law.
(b) Tolls for resolving grievances or disagreements which occur between the company and its stakeholders.
(c) Frameworks for sustaining a satisfactory association between consumers and suppliers and ensuring the confidentiality of related information.
(d) A code of behavior that should be agreed with accurate professional and ethical principles for the company's executives and employees.

16.4 Board Creation Standards

In corporations worldwide, there are two common board systems. First, the dual board is separate in civil law countries, such as France and Germany. This board is divided into two bodies (two-tier). The former is the supervisory body, whose members are selected by shareholders in the corporation's general meeting, thus directing business decisions. The latter is the administrative body, which is charged by the supervisory body to carry out the business of the corporation. The dual board has clear advantages; namely, the distinction between the executive and non-executive members and the differentiation between the position of the board chairman and that of the chief executive. The dual board considerably assists all the benefitting stakeholders by permitting them to have their representatives sit on the board, which empowers the stakeholder groups to look after their interests (Maassen and Bosch 1999).

Secondly, and most importantly, the unitary board (one-tier) is extensive in common law countries, such as the UK, US, Canada and New Zealand. This board consists of executive, non-executive and independent members who should be appointed by the shareholders at the corporation's general meeting. Additionally, those board members' liabilities cover all the corporation's activities. It is worth observing that independent enquiries and a disconnection between the supervision with the administrative purposes are found in this board (Fannon 2005).

Regarding Saudi corporations' boards, most have adapted the unitary board, although the CGC and the CL give no preference as to board structure. Nevertheless, Article 15-C of the CGC advocates that board structures should be tested by the board's nomination and remuneration committee, which can make alterations if necessary. Subsequently, the board structures should be regulated by the CGC, thus lessening the possibility of any ambiguity and wrongdoing in this respect.

Article 12 of the CGC also acknowledges that the number of board members, which ought to be not more than 11 and not less than 3, should be clearly stated in the corporation's articles of association. This point is debatable, as Article 64 of the CL outlines just the minimum number, which is three board members, and leaves the maximum number open. In contrast, section 154, Article 2 of the UK Companies Act stipulates that public corporations should have at least two directors. As in the Saudi case, however, the maximum number is not defined. Arguably, insisting that the maximum number of board members should be no more than 11 is an innovative clause in the CGC, mimicking the international corporation board seats regulations, especially those found in the US (Charkham 2005). In practice, the listed corporations are obstructed by this CGC clause, as the number of their board seats fluctuates between 7 and 11. For instance, Al-Riyadh Development Company's board has ten members.

16.5 Separation of Board Members' Powers

It is becoming increasingly difficult to ignore the fact that spreading board members' powers across multiple members improves a corporation's targets, chiefly affecting its disclosure and transparency to all market contributors. It also makes the supervision undertaken by the board members more efficient. It is important to note that separating the roles of chairman and chief executive is considered good corporate governance practice, as it minimizes potential conflicts of interest. International corporate governance principles have recognized the importance of spreading the board members' powers, specifically those of the board chairman and the chief executive. For instance, the OECD principles of corporate governance presume that:

> Separation of the two posts may be regarded as good practice, as it can help to achieve an appropriate balance of power, increase accountability and improve the board's capacity for decision making independent of management.

More to the point, the Cadbury report (1992) recommends that there should be a division of accountabilities at the head of the corporation and that the character of the board chairman should, theoretically, be separate from that of the chief executive. Speck and Tanega (2005) remarked that the Cadbury report highlights that the board chairman should not be chief executive at the same time. As a matter of fact, the Cadbury report's recommendation was a consequence of the fact that in corporations where corporate governance was not applied correctly, it was easy to find individuals in the role of both board chairman and chief executive simultaneously, and thus in a position to suppress all board debate. It has been said that the separation of the board chairman and the chief executive posts in a single corporation has noteworthy effects on the corporation (Brickley et al. 1997).

Article 78 of the CL used to permit an individual to be both board chairman and chief executive simultaneously. However, this trend has since changed somewhat. Article 12-D of the CGC prevents the combination of this essential position with other executive positions on the board or top management positions in the corporation; namely the chief executive officer, managing director or general manager. It can be argued, therefore, that the separation of the overseeing mission and the managing mission inside the corporation set out by the CGC constitutes an imperative advantage. Furthermore, this ensures accountability and strong values, because the responsibilities of the top executives allow them to handle a diversity of obligations, including signing on behalf of the corporation, formatting commercial agreements and selling or purchasing the corporation's products. Consequently, it appears that by carrying out these responsibilities in accordance with the board controlling equipment and the spreading of the board members' powers, members would not be open to suspicion of corruption, malpractice and conflicts of interest in board situations.

Having identified the challenge to the separation of the board chairman position and other board executive positions posed by international corporate governance principles (including those of Saudi Arabia), Article 78 of the CL conceded that the corporation's board and the shareholders are equally in charge of selecting the board chairman, the chief executive and other members. However, this approach is ignored by the majority of listed companies, where the family and the government are seen to be the major shareholders or the corporations' owners. For example, *Al Sorayai* Group is a paradigm of the family listed company; the positions of board chairman and chief executive are held by the same individual family member. Government influences can be seen in the National Industrialization Company, in which the board chairman and chief executive functions are handled by one person. Regarding the separation of the board chairman and other board executive positions, it seems that the effectiveness of the concentrated ownership structure is obvious, as can be appreciated from the two examples above. It seems vital to engage in further explanation about the ownership structure concerning the Saudi practice of the separation of the board chairman and other board executive positions.

There are two significant global ownership structures. The former is the dispersed ownership structure found in common law country corporations, such as the UK and the US (Coffee 1999). The dispersed ownership structure is defined as when corporation shares are extensively owned by the public, and additionally when the management of the corporation has a smaller shareholding, which leads, to some extent, to what is frequently a nominated division of ownership and control. This corporation can thus be expected to have a dispersed ownership structure. The comprehensive nature of the dispersed ownership structure in common law countries is due to several successful factors, including the efficient general legal system, the influential corporate governance regime, the capable security market and finally strict disclosure and transparency requirements. The second ownership structure is that of concentrated ownership, where a small number of shareholders hold the highest proportion of shares. The concentrated ownership structure, specifically, can be understood in developing countries' corporations, including those of Saudi Arabia. It can be argued that the extension of the concentrated ownership structure in less-developed countries' corporations is a consequence of numerous factors, including the complicated general legal systems, the fledgling corporate governance regimes, the weak securities markets and the shortcomings in the conditions for disclosure and transparency (Kaur and Kaur 2009).

Bearing this in mind, there is a mirror association between a country's political and legal arrangements and its companies' ownership structures. Certainly, the latter ownership structure and other corporate governance shortcomings would be anticipated if a government were unfair, weak and undemocratic (Satkunasingam and Shanmugam 2004). However, there are also non-political circumstances that affect ownership structure, such as economic enhancement, technological progress, cultural change and legal reform (Roe 2003). It could be supposed that all these circumstances fit the Saudi context regarding ownership structure and corporate governance aspects. In particular, the Saudi ownership structure is without doubt concentrated ownership based on rich families and government effectiveness (Al Ajlan 2005).

The Saudi government has been the greatest investor in a variety of leading Saudi listed corporations. Stock exchange statistics estimate that Saudi government investment comprises approximately 45 % of the listed companies' shareholdings, and accounts for 8.8 billion shares with a market capitalization of $155.92 billion. Saudi government investment in the leading listed companies, which have been seen to be an operative cause in converting ownership to the concentrated model, is made by the governmental institutional investors; namely, the Public Investment Fund, the Public Pension Agency and the General Organization for Social Insurance. These bodies have invested on behalf of the Saudi government in a variety of listed corporations, such as SABIC and STC. They sometimes own a large percentage of the listed corporations' shares, as these corporations are considered by the government to be on-going concerns. Thus, the government can assure its investments when investing in these corporations through its institutional investors.

On the other hand, in the Saudi market, rich families invest in several listed corporations, and these families always withdraw potential opportunities to recoup on the listed corporations' affairs. Furthermore, a number of family enterprises, which used to be small ventures owned by rich families, have since converted to listed corporations. These listed family corporations can be seen in several stock exchange sectors, such as energy, agriculture, cement and transport. They are usually named after the founding family's name; for example, the *Halwani* Company, *Fitaihi*-Group, *Al Abdullatif* Industrial Investment Company, *Othaim* Company and *Zamil* Industrial Investment Company.

Returning to the impact of rich families and the government on the Saudi ownership structure, several corporate governance issues are endangered by the ownership patterns. The most likely corporate governance issues to be debated are the following:

1. Separation of the board chairman's position and other board executive positions.
2. Appointment and removal of board members.
3. Determined time of the board member in the board seat.
4. Unlimited board memberships.

In this regard, Articles 12-B and 12-H of the CGC discuss the fact that the corporation general meeting should appoint and re-appoint board members for the duration provided for in the corporation's articles of association. This duration should not exceed 3 years. In addition, board members should not appear as board members of more than five listed companies at the same time. The rich families in question have kept the majority of the transmitted listed corporations' shareholdings from their foundation in the stock exchange. Thus, these families' members have occupied these listed corporations' board seats for an undetermined period of time, and generally have positions on more than five listed corporations' boards simultaneously. Accordingly, members of these rich families are in breach of Articles 12-B and 12-H of the CGC. However, no law case or fine has been issued either by the Capital Market Authority Board or the CRSD (as judicial entities of the Saudi Capital Market) with regard to these families' members who are in breach. This approach can also be argued by the fact that in some countries, politicians and rich families are easily able to obtain business and positions. This is what happens in the vast majority of Saudi listed corporations, and absolutely fits the Saudi context.

It is also apparent that the Saudi government influences Articles 12-B and 12-H of the CGC, as the government is the major shareholder/owner of some brand listed corporations. Accordingly, the government places its representatives in these corporations' board seats regardless of their period of office, as well as placing representatives on the boards of more than five listed corporations. The evidence from Article 65 of the CL obviously shows that the listed corporations' boards' governmental representatives have the power to hand out board seats for undetermined periods.

There is expected debate concerning the ability of the government to enforce its representatives in the listed corporations' board seats for unspecified durations. Supporters of the governmental influences claim that due to the government owning large shareholdings in some listed corporations, it should have more than enough votes to elect and re-elect its representatives in these corporations' boardrooms. For example, the Saudi government appointed five out of the nine members in the Saudi Arabian Mining Company because the government owns 50 % of the shares in this company. Opponents of the governmental influences urge that allowing the board members to avail themselves of an unspecified mandate and duration deteriorates the board members' enthusiasm for corporation involvement. This results in a diversity of corporate governance aspects, as the majority of these corporations' boards' chairmen, members and chief executives are nominated by the government. As a result, it can be said that the government has more dominant power based on its investments and its board representatives. Hence, other shareholders will not have the same power as the government in these corporations. In particular, board members who are not appointed by the government will not be able to challenge the opinions of the elected board members in terms of decision-making.

Therefore, Article 65 of the CL, which permits the government to place its representatives for an undecided time and mandate, is not in line with good corporate governance practices. Thus, it should be removed from the CL in order to avoid being misused by government agencies. Article 12-H of the CGC, which does not allow board members to hold positions on more than five listed corporations' boards simultaneously, should at least be the reference for this matter, even if over five memberships are not recommended as an optimal practice.

16.6 Board Membership Categories

The CGC identifies three categories of board membership; specifically executive members, non-executive members and independent members. First, Article 2 of the CGC defines that the board executive members should have full-time administrative positions in the corporation and obtain monthly salaries. In this regard, the Cadbury report highlights significant elements with reference to the definition of executive members, such as the fact that their contracts should not exceed 3 years' duration without shareholders' endorsement. In addition, there should be full transparency and disclosure regarding the executive members' income. These conditions cannot be found under the CGC; therefore amendment of the CGC in accordance with these conditions is needed in order to achieve good corporate governance practices.

The precise role of the executive member is open to debate. The role of executive members is significant, alongside non-executive and independent members of the board of directors, in achieving optimal corporation performance. This is due to the fact that executive members are usually knowledgeable and experienced in terms of the corporation's affairs and investment opportunities. It is, however, argued that the executive members do not assess strategic decisions much more effectively than the non-executive members. This is due to the fact that the executive members are unlikely to challenge the chief executive strategic decision making during board meetings (Westphal and Zajac 1998).

Secondly, Article 2 of the CGC maintains that the non-executive board members neither have full-time administrative position in the corporation nor earn monthly salaries. In this respect, the Cadbury report (1992) outlined important issues with regard to the decision that non-executive membership should not be determined for a long period and that they should be independent of the corporation, apart from their payments and their shares. They should also be independent of management and free from any business or other association which could substantially conflict with the application of their independent judgment. Again, these conditions are not established under the CGC, so it should be amended in accordance with these conditions.

Article 12-C of the CGC indicates that non-executive members should occupy the largest number of board seats. Article 11-G of the CGC designates that non-executive members should additionally receive information about the corporation's submissions in a satisfactory manner, thus enabling them to enforce their jurisdictions efficiently. The general notion of placing non-executive members on the board is that, again, they do not have a full-time career in the corporation, so are not reliant on the corporation for their livelihood. As a result, non-executive members should not be influenced by other board members, including the chief executive, as they earn very little from the corporation. Therefore, they do not jeopardize their reputation or their total income capability by getting involved in any corporation mismanagement. Non-executive members, moreover, formulate independent judgments within the board; yet, they not only play a regular administrative role in the management of the corporation, but also exercise an intensive care purpose.

Finally, Article 2 of the CGC confirms that the independent board members enjoy full independence. Accordingly, there are official regulations which are emphasized in the CGC as breaching this independence:

1. If the member owns a controlling interest or holds the position of senior executive for 2 years in the company or in one of its subsidiaries.
2. If the member has ownership of 5 % or more of the company or its group by the board member or a representative of a legal entity which owns 5 % or more of the company or its group.
3. If the member is a board member of any company within the body of the company of which the member is scheduled to be a member of its board.
4. If the member has been an employee and a partner of the company or a partner of any other company including external auditors or senior suppliers for 2 years.
5. If the member is a relative (namely father, mother, wife, husband or child) of any board member or senior executive of the company or one of its subsidiaries.

The definition of the independent board member is still a doubtful concern among both legislators and the judiciary. This is supported by Brudney (1982), who emphasized that:

> No definition of independence yet offered precludes an independent director from being a social friend of, or a member of the same clubs, associations, or charitable efforts as the persons whose compensation he is asked to assess.

It is almost impossible to verify the independent nature of a company board member in Saudi Arabia. In particular, Article 15-C considers that the corporation board nomination and remuneration committee plays a significant role in terms of inspecting the independence of the board members. In addition, the (Capital Market Authority) general department of corporate governance pays great attention to this matter when reviewing the listed corporation boards' annual reports. Recent statistics from the general department of corporate governance show that there are 1,108 listed corporation board members: 606 independent members, 356 non-executive members and 146 executive members.

16.7 Board Meeting

Saudi board meetings are encouraged to be open to debate in order to support the board supervisory tasks as regards the listed corporation's dealings. As Al Urban pointed out, an open discussion brings to bear the facts and deals with management malpractice if and when it is uncovered. Nevertheless, Article 16 of the CGC has incorporated the following ideas on board meetings:

(A) The board arranges its meetings at the request of the board chairman who can convene the board for an immediate meeting following a written request by at least two board members.
(B) The board should minute the meeting discussions by reporting the agreeing and disagreeing votes.
(C) The board members should have plenty of time to fulfill their duties including preparation for the board and the board sub-committees' meetings.
(D) The board members should receive the board documentations in a suitable and timely fashion before the meeting, to enable them to study this material.

It could be argued that the CGC does not stipulate how many corporation board meetings must be held. This overlooked aspect is, in practice, under the board chairman's command in a variety of listed corporations, and its neglect has been seen as a disadvantage within the CGC, as it leaves the number of the corporation's board meetings during the fiscal year unspecified and weakens the board's overseeing role. This could lead to board executive members having ultimate power in the corporation, and thus the possibility of serious management misdemeanours. It is consequently recommended that the number of corporation board meetings should be incorporated into the CGC as a binding clause that should be taken into account by all listed corporations.

In addition, Article 80 of the CL specifies that meetings of the board of directors are valid only if attended by at least half of the directors, provided that the number of those present is not less than three, unless the corporation's articles of association provide for a higher number. In addition, the resolutions of the board must be adopted by a majority vote of the directors present or represented. In case of a tie, the chairman's vote carries, unless the corporation's articles of association provide otherwise. These prerequisites do not exist in the CGC; therefore, they should be added due to their necessity in terms of the board members' civil and criminal liabilities when shareholders litigate against board members.

16.8 Board Sub-Committees

16.8.1 General Overview

It is noteworthy that the CGC has comparatively benefitted from transnational corporate governance principles; chiefly the Cadbury report aspects on the formation of board sub-committees. In particular, the Cadbury report states that:

> The effectiveness of a board is buttressed by its structure and procedures. One aspect of structure is the appointment of committees of the board such as the audit, remuneration and nomination committees.

In addition, the mandatory Articles 12, 13, 14 and 15 of the CGC can be seen to encourage the setting up of board sub-committees. It is proposed under Article 13-A of the CGC that the board creates a sufficient number of committees pursuant to the corporation circumstances and requirements, as these sub-committees will support the board in carrying out its duties. Therefore, it is possible to criticize the scope of the CGC regarding this obligation; the CGC stems from this obligation in order to enable the corporation to determine which kind of committees are significant for its business dealings along with its general size and the magnitude of its operations. However, the CGC strongly states that there should be two obligatory sub-committees established by the board; explicitly the audit committee and the nomination and remuneration committee. This can be understood from Article 13-B of the CGC when it states: "The board shall approve by laws – all of the committees of the board, including inter alia, the audit committee, nomination and remuneration committee."

As a consequence, in addition to ensuring the formation of the board sub-committees – mainly the audit committee and the nomination and remuneration committee – Article 9-D of the CGC specifies that the corporation's board annual reports should contain the forenames of the chairmen and members of the board sub-committees, as well as the approximate number of their regular meetings.

16.8.2 Audit Committee

The idea of creating a board audit committee came into existence in 1978, when the New York stock exchange required all listed corporations to have a board audit committee comprising independent members. The idea also arose when the 1987 American Treadway Commission report settled that the board audit committee had a critical role to play in ensuring the integrity of US corporations' boards' annual statements (Cadbury report 1992).

It is understood that the audit committee aims to monitor the corporation's missions. It is therefore significant, as it constitutes a major internal supervision and auditing tool that improves and directs the decisions made by the board. The audit committee works for the benefit of the board by fulfilling an essential watchdog function that ensures accountability inside the corporation as well as protecting investors (Rezaee, Olibe and Minmier 2003). Additionally, Baruch (1980) stated that the audit committee's role is to observe the consistency of the corporation's accounting and auditing procedures, thereby safeguarding shareholders' interests.

It is expected that a productively operating audit committee will result in quite a few advantages. These advantages are assumed to include promoting the quality of financial statements, establishing a climate of self-control that lessens the chance of fraud, and empowering non-executive members to make independent decisions, play a constructive part and support the task of the finance director and external auditors (Cadburt report 1992).

The Saudi legislator, who took the significance of the audit committee into consideration even before passing the recent CGC, incorporated a piece of legislation (The Ministry of Commerce and Industry, Royal Decree, No. 903, dated 23rd January 1994) that actively encouraged listed corporations to establish an audit committee as one of the board sub-committees, based on its advantages in developing good accounting and auditing practices. This legislation also provided guidelines on the standards regarding an audit committee's membership and overall character, in terms of the choice of external auditors in the listed corporations. Article 14 of the CGC, in principle, has defined four compulsory elements in terms of structuring the audit committee membership:

(A) The audit committee must contain at least three members.
(B) The audit committee members should be non-executive and independent members.
(C) The audit committee members should have satisfactory qualifications and skills in the accounting, auditing and finance professions.
(D) The audit committee members should not have either direct or indirect interests in the corporation's submissions and contracts.

It is obvious that the requirement for an independent audit committee can be noted in Article 13-C of the CGC rather than in the previous legislation mentioned, as independent and non-executive members are highly encouraged to be members of the audit committee. This methodology means that audit committee members fulfill their obligations and submit their reports subjectively and without any prejudice from the board executive members.

A recent legal case concerned the existence of independent members on the board and its audit committee. *Banque* Saudi *Fransi* was found not to have any independent members on its board or its audit committee. As a result, the Capital Market Authority Board, (Issued Decision, No. 6-36-2011, dated 11 December 2011) fined the bank $13,333 in accordance with Article 12-E of the CGC. It contended that: "The independent members of the board of directors and its audit committee shall not be less than two members, or one-third of the members, whichever is greater."

This legal case clearly demonstrates that the Capital Market Authority Board is concerned about implementing good corporate governance practices in listed corporations' boards and audit committees. The presence of independent members is highly recommended by the CML and the Implementing Regulations. *Banque* Saudi *Fransi*, however, violated a binding clause of the CGC, so the condemnation was legislative. This legal case was, significantly, the earliest verdict regarding a board sub-committees' affairs. It is, however, suggested that the Saudi capital market does not have enough capable individuals to fulfill the character of effective independent members.

In this respect, a number of corporate governance studies have found that weakness in an audit committee is more likely if it does not have strong accounting, auditing and finance expertise. Empirical research suggests that there is a strong link between accurate financial accounts and an audit committee that has highly qualified professionals in accounting, auditing and finance. This ideology can be found under Article 29 of the Listing Rules, which advocates that highly qualified members in accounting, auditing and finance should occupy the board's sub-committee seats. It can also be seen in Article 14-A of the CGC, which includes the provision that one of the audit committee members, should be an expert in financial and accounting substances.

Conversely, the Saudi regulator makes no mention of inviting experienced non-members of the audit committee to attend audit committee meetings when necessary. In particular, Al Mataz (2007) indicated that outsider expertise in accounting, auditing and finances (i.e. people who are not board non-executive or independent members) should be part of the board audit committee in order to effectively achieve targets. This trend can be found in the Cadbury report, when it advises that:

> Membership of an audit committee is a demanding task requiring commitment, training and skill. The directors' concerned need to have sufficient understanding of the issues to be dealt with by the committee to take an active part in its proceedings. This is why committees should, if it is appropriate and within their power, be able to invite outsiders with relevant experience to attend meetings.

It can be further argued that audit committee members usually work part-time, namely as non-executive and independent members. This means that they do not have a strong relationship with the corporation staff, whereas board executive members often work full-time and certainly have a direct relationship with corporation staff (Monks 2001). This is one of the disadvantages of the Saudi audit committee, which may not protect shareholder interests in the face of mismanagement and negligence by board executive members (Al Twaijry et al. 2002).

Recent evidence suggests that the vast majority of the audit committees of listed corporations have failed to enforce one or more clauses of Article 14 of the CGC. For example, the corporation's general meeting, depending on recommendations from the board, forms the standards for selecting the audit committee members and defining the duration of their membership and their work plans. In practice, the listed corporations' boards usually nominate the audit committee members who should comprise an independent commission benefitting shareholders, and this election is usually carried out without the authorization of the corporation's general meeting.

The Capital Market Authority Board recently charged the Basic Chemicals Industries Company, imposing a fine of $13,333 because the company board failed to propose to the company ordinary general meeting the rules that should be in place for selecting the audit committee members, their membership duration and the audit committee approaches. In the second case, the Capital Market Authority Board penalized the *Taboo* Cement Company, which was charged with the same violation. The verdicts were in accordance with Article 14-B of the CGC:

> The general meeting of shareholders shall, upon a recommendation of the board of directors, issue rules for appointing the members of the audit committee and define the term of their office and the procedure to be followed by the committee.

In these cases, the fines issued were legislative because they were taken from the mandatory CGC provision. Nevertheless, the violated corporations' boards should form the audit committee and outline its responsibilities. They should also appoint audit committee members with regard to the relevant article of the CGC. The fines that were imposed by the Capital Market Authority Board, however, should have been $26,666 rather than $13,333, as the companies in question violated a significant CGC provision.

Then again, Article 14-C of the CGC has highlighted several essential functions of the audit committee, stating that it:

1. Assists and plans a written statement to the internal audit system and then controls the corporation's internal audit system in addition to certifying its usefulness.
2. Advocates the discharge and appointment of external auditors with their remunerations to the board.
3. Examines jointly with the external auditor the corporation audit plan.
4. Checks the external auditor's comments in the board's annual financial report and then provides opinions regarding this report.

These functions can be traced back to the Cadbury report. Nevertheless, there are a number of significant summits that should be regulated and added to the CGC from the Cadbury report concerning how the audit committee could accomplish its work successfully. For example, the Cadbury report affirms that the audit committee examines the half-year and annual reports before submission to the board, with major concern regarding any changes in accounting standards and adherence to stock exchange and legal requests. In addition, many virtual aspects have been specified under the Cadbury report. For instance, the report stipulates that the audit committee should meet at least twice a year, the external auditor and the finance director should regularly attend the audit committee meetings and other board members should have the same right. Nonetheless, the audit committee and the external auditor should have at least one exceptional meeting without these parties in order to ensure that there is no unsettled concern. From this discussion, it can be suggested that these essential clauses should be brought to the CGC in line with their professionalism for the formation of the board audit committee. The Saudi audit committee is principally a new experience. Therefore, the promulgation of successful international practices is needed in order for the audit committee to reach an adequate level of performance.

Alternatively, Article 14-C of the CGC provides the audit committee with the right to appoint and discharge the external auditors. It does not enforce any negative impediments, either by the board members or by the top managers, which would meet the external auditors when carrying out their obligations to the corporation and its shareholders. Article 230-4 of the CL has taken a valuable step towards the effective functioning of the external auditors. It also demonstrates that any board member, executive or employee who tries to obstruct the external auditors will be sued. It is thought that this clause should be codified under the CGC, as it ensures the usefulness of the external auditors regarding the fulfillment of their duties.

16.8.3 Nomination and Remuneration Committee

It is said that the board of directors cannot resolve the remuneration of the board executive members without a possible conflict of interest. In addition, the board members' remuneration should be taken into account in corporate governance progression, because the supervision of the corporation's popularity can have a contradictory consequence on determination within the corporation. Specifically, the interpretation which several US and UK corporations have settled on is the creation of a remuneration committee. This committee should consist of non-executive directors, who do not have personal financial interest, and adopt executive directors' remuneration on their behalf; it should refer directly to the shareholders for its pronouncements, whilst advancing the broader concern of the corporation. In other words, the speculative meaning of the remuneration committee is obvious, because if this sub-committee does not perform properly within the corporation, the executive members will reward themselves financially, which is not always in the interest of shareholders (Conyon and Peck 1998).

This notwithstanding, it is indicated that executive directors' compensation should be in line with the suggestions of the remuneration committee, which should consist predominantly of non-executive directors. Still, the independence of the nomination and remuneration committee can be held in doubt, as this sub-committee is established by the corporation board. It is additionally simultaneously in charge of handing out board members' compensations. It can be questioned in what manner the nomination and remuneration committee could prevent board members from deciding what their remuneration would be (Cadbury report 1992).

Nonetheless, Article 15-C of the CGC outlines the nomination and remuneration committee's prerogatives, stating that it:

1. Advises the appointment of a new board member who should hold a position of honor and honesty.
2. Updates the description of the essential capabilities and qualifications that are required for board membership.
3. Decides the strong points and weaknesses of the board as well as board construction and suggests remedies.
4. Examines the independence of the board's non-executive and independent members.
5. Ensures the absence of any conflicts of interest within the board.
6. Forms identifiable procedures regarding the board members' and top executives' remuneration.

In particular, the CGC overlooks an essential point with respect to the appointment of board members to the nomination and remuneration committee. This is that a board member should not be a public employee unless he or she has been appointed by the government as a governmental representative inside the board. This is so as to prevent outside pressure on the board member to gain advantage, either statutory or otherwise, and to prevent conflicts of interest. This point of view, principally, should be regulated under the CGC and should be part of the nomination and remuneration committee's responsibility.

While Article 14-A of the CGC has stipulated that the audit committee members should not number fewer than three, it makes no mention as to how many members should comprise the nomination and remuneration committee. This reflects good international practice, apart from this clause. In this respect, the Greenbury report (1995) insists that the remuneration committee should have three non-executive members, or at least two on the occasion of small corporations. The remuneration committee, however, should state, in its report to shareholders, any reason why this committee should consist of fewer than three members. Consequently, the CGC would gain an advantage when reforming its guidelines with regard to this overlooked aspect, in accordance with the Greenbury report suggestion.

Furthermore, the CGC does not stipulate anything about how the sub-committee members should be compensated. This is a major worry in terms of outstanding members of this sub-committee. The good practice containing this tendency would be derived from the Greenbury report's recommendation, which suggests that the members' indemnifications of the remuneration committee should typically be of an arrangement of stationary payments fixed by the board, entirely within the limits agreed in the corporation's articles of association, which should indicate the amount of time they dedicate to the corporation's undertakings.

16.9 Board Members' Compensations

The board members' indemnification is a statutory right based on the principle of no free fee for doing business. The function of the board members resembles the agent's function; acquiring an advantage for their agency's actions as long as these activities are legitimate (Al Jeber 2007). It is worth observing the UK Combined Code, which outlines the remuneration level – there is no piece of Saudi legislation representing this idea. Section 1 of the UK Combined Code affirms that:

> Levels of remuneration should be sufficient to attract, retain and motivate directors of the quality required to run the company successfully, but a company should avoid paying more than is necessary for this purpose. A significant proportion of executive directors' remuneration should be structured so as to link rewards to corporate and individual performance.

Board members' remunerations have recently caught the attention of the Saudi legislator. This is due to the fact that these remunerations used to comprise 10 % of the corporation's yearly net profits. There was, furthermore, a ministerial resolution, No. 1071, dated 5th May 1992, which used to be the second reference that measured board members' remunerations. Significantly, this ministerial resolution emphasized that the maximum non-executive and independent members' remunerations should be $53,333 for each member, as well as $800 fees for attending board meetings.

This ministerial resolution was unfortunately ignored by the vast majority of listed corporations. It is nevertheless debated, because it did not highlight a maximum level of remuneration for executive members, which should be a concern owing to their superior level of remuneration compared with that of non-executive and independent members. The Saudi Consultative Council, which has legislative power over the commercial and corporate rules, recently reviewed the maximum level of the board members' yearly compensation and declared that it should be no more than $133,333 for each member, including, significantly, executive members. Time will tell whether executive members will be paid no more than this maximum level of remuneration. This is a problematic area, because many worldwide financial markets have failed to set a limit for executive compensation, as governments are not willing to fix basic pay levels or even to supervise rates of increase in compensation in the private sector of market economies. In addition, checking the remuneration by non-executive and independent board members appears to have been entirely ineffective in this regard (Davies 2000).

On the other hand, Article 17 of the CGC gives no suggestions as to the maximum level of compensation for board members. In theory, it reassures the listed corporations before awarding the board members indemnification to submit a written record encompassing any such proposed compensation, which then needs to be voted on by shareholders during the corporation's general meeting. The CGC further requires that the corporation's articles of association describe the way in which board members are rewarded compensation – this may take various forms, such as salaries, bonuses and attendance payments.

Therefore, the Saudi model of distributing remuneration encounters some obstacles concerning the remuneration of directors and top executives. It is argued that a major difficulty that has been faced by international corporations is the tying of the remuneration of their directors and top executives to their actual presentation. Therefore, there is an international push to instigate 'say on pay' procedures in order to permit shareholders to remark on planned remunerations of directors and top executives (Tomasic 2011).

The CGC, in particular, advocates that the corporation board's annual report should include the board members' remunerations as part of its significant disclosure and transparency requirements. An investigation of 50 Saudi listed corporations' boards' annual reports reveals that the board members' remunerations are not clearly declared (Al Mataz 2007). This investigation finding is not surprising because of the ambiguity of almost all, if not all, listed corporations regarding their board members' compensations.

In addition to demonstrating and recognizing the practice of rewarding the board members, the Saudi Cable Company was chosen as an example in this regard. In 2009, this company distributed board members' remunerations of $2,809,000. Moreover, two executive members were given the largest proportion of this, being awarded $2,595,000 between them. Subsequently, the rest of money, totalling $214,000, was paid to four non-executive members. Importantly, these significant figures do not take into account the executive members' salaries and the non-executive members' meeting attendance payments. It is therefore suggested that these payments are examples of corruption within a substantial number of listed corporations. Worse, it seems that the Saudi Cable Company mentioned above is not prominent amongst these, and is one of the worst performing in the exchange. Given this company's board members' remunerations, how much remains to the shareholders and other benefitting groups of the corporation?

It is worth observing that even though the Capital Market Authority Board does not interfere directly in the compensations of listed companies' board members, the Capital Market Authority Board sent an official reminder to *Al Ahsa* Development Company about its breaching of Article 43 of the company's articles of association, as well as Article 74 of the CL. This Article stipulates that after distribution of a dividend of not less than 5 % of the company's capital to shareholders, the company can distribute the board members' compensations. Any determination of the compensation made in violation of this restraint is null and void. In brief, this company was making a loss, while at the same time distributing compensations to board members without distributing any profits to shareholders in accordance with its general meeting resolution No. 21, dated 4th May 2010.

It appears that the board members' compensations of almost, if not all, the listed corporations are considered arbitrarily, and should be less than their current massive proportions. For instance, 33 Saudi listed corporations in 2011 distributed compensation equal to $32,000,000 to their board members while making a loss.

Why should an individual (i.e. a board member) be able to gain in one fiscal year a total amount of money that would not be obtained over the course of the whole lifetime of a normal person? If these remunerations are actually deserved, then talking about the distribution of social justice and social profits is pointless. These indemnifications raise a critical question about the board members' loyalty. In general, therefore, it seems that the Saudi board members' remunerations bear a resemblance to other global corporations' board members' compensations based on the huge amounts of money paid. It is clear that these global compensations are, to some extent, justified, as they result from global corporations' productivity, whereas some Saudi listed corporations pay immense remunerations despite making a loss, as in the examples above.

16.10 Conclusion and Recommendations

16.10.1 Conclusion

This paper has analyzed the current board of directors' practices in Saudi corporate governance. The major aim was to study the board of directors in addition to clarifying a variety of indispensable features related to the board. The board duties, interpreted in Sect. 16.2, were shown to be the duty of care, the duty of loyalty and the duty to act within the power. The duty of care has not been explained in either the CGC or the CL. Therefore, the duty of care can be promulgated to Saudi legislation from other international companies' jurisprudences, such as the UK Companies Act. In addition, the duty to act within the constraints of their powers is mentioned briefly in the CGC and the CL. However, the board of directors is entitled to delegate some of its work to other board members and sub-committees, such as the Audit Committee and the Nomination and Remuneration Committee. Unless delegated pieces of work are determined in terms of length and specific power, they are null and void. The CGC also introduces a beneficial clause regarding the duty not to exceed their powers, which seeks to prevent corporations from providing cash mortgages to board members or certifying cash mortgages to board members via a third party. This is designed to protect the capital of both shareholders and corporation.

On the other hand, the duty of loyalty has been put in question by conflicts of interests within the board and insider trading. A conflict of interests is defined as a position that would strain the impartiality of members owing to personal benefits, both material and moral, or those pertaining to their relatives. Non-executive board members are observed to have a conflict of interests within the board when they hold positions on various corporations' boards and have options and shares in those corporations. As regards the Saudi situation, the law cases which have been introduced in this section prove that conflicts of interests were experienced by both executive and non-executive board members. The CGC has sought to manage conflicts of interests within the board by proposing three significant objectives. It advises that the board should create a written policy that controls the related groups and resolves any conflict of interests when it arises. It also excludes board members from either competing or trading in the corporation's commercial transactions. On the other hand, the CGC has needlessly provided the following points of exception:

1. When the board member has established prior approval from the corporation's general meeting to do so, subject to annual renewal.
2. When the board member notifies the board and the shareholders about any secret activities and commercial contracts that are concluded for the corporation.
3. When the board member is the best bidder through public bidding.

Critics of the CGC's exceptions argue that it is wrong to allow board members with conflicts of interests to compete and trade in the corporation's affairs where they can submit the optimal offer through public bidding, as detailed insider knowledge of the corporation and its activities makes their offer the most likely to win a general bidding contest. The futility of this exception signifies the need for this clause of the CGC to be amended by the Capital Market Authority Board in order to inspire good corporate governance practices.

The second matter open to challenge is insider trading which contravenes the meaning of duty of loyalty by the board members. Insider trading is defined as information obtained by the insider that is not available to the general public, has not been disclosed, and whose release and availability would have a material effect on the price or value of a security related to such information; furthermore, that the insider knows that such information is not generally available and that, if it were available, it would have a material effect on the price or value of such security. It is thought that insider trading is very difficult to prove and investigate, although a number of bodies are in a position to both prove and prevent it. These include the Capital Market Authority Board, the General Department of Corporate Governance, the CRSD, a corporation's board Nomination and Remuneration Sub-Committee and the Saudi National Anti-Corruption Commission. Law cases relating to insider trading were particularly described and evaluated in this section. The CRSD imposed fines and prevented the violating board members from working with listed corporations for 3 years. The CRSD also forced these board members to pay back to the Capital Market Authority the venture that was gained in accordance with their insider dealings. It is worth observing that the CRSD issued a penalty of imprisonment against the chairman of the *Bishah Agriculture Development Company*'s board because he was litigated against for breach of duty and insider trading. This case has been debated by Saudi corporate governance observers. They argue that the CRSD should not have the right to pass prison sentences since this constitutes a criminal sanction, which should not be imposed by a quasi-judicial committee such as the CRSD. Instead, penalties should be imposed by the Saudi Criminal Prosecution, which is responsible for determining criminal sanctions. Similarly, UK law has assigned insider dealing to the Criminal Prosecution Service.

The board's responsibilities were discussed in Sect. 16.3. It was argued that these responsibilities should be included in the corporation's articles of association and that board members had a duty to fulfill their responsibilities effectively. Moreover, board members should not distinguish between major and minor shareholders when gathering information, making decisions and producing the board's annual report. In addition, the board is responsible for all the corporation's policies including the financial plan, the budget, the performance strategy, the internal audit plan and the financial annual statements. In particular, the board should develop the relevant policies to regulate relationships with the different stakeholder groups, namely the suppliers, consumers, lenders, shareholders and the whole of society.

The creation for boards was considered in Sect. 16.4. It was noted that the CGC insists that the minimum number of board seats should be 3 and the maximum 11. The dual and unitary board forms were covered. Although neither the CGC nor the CL advise any board restriction, as a consequence of the adoption of the Anglo-American corporate governance model by the Saudi regulator some listed corporations have unitary boards comparable to US corporations.

Section 16.5 focused on the separation of the powers held by board members. Saudi Arabia adopted this method following the Cadbury report, which suggested a separation of the board members' powers. The CGC naturally favors the separation of the board's chairman and chief executive positions. Since the separation of the board members' powers is affected by the Saudi ownership structure, this was thought to merit discussion and a presentation of the definitions of dispersed and concentrated ownership. Dispersed ownership implies that the corporation's shareholdings are owned by a large number of shareholders. The reasons for the spread of this ownership structure in developed markets are based on competent general legal orders, effective corporate governance systems, capable securities' markets and stringent disclosure and transparency requests. By contrast, in the concentrated ownership structure the corporation's shareholdings are held by a major or a small number of shareholders. This type of ownership has flourished in emerging markets because of their problematical general legal structures, inexperienced corporate governance systems, weak securities markets and inadequacies in the settings for disclosure and transparency. Concentrated ownership structures are to be expected where the government is undemocratic and unfair. However, it may also be found in situations of economic improvement, technological advancement, cultural variations and legal modifications.

In the Saudi case, the ownership structure has been influenced by the Saudi rich families and the Saudi government. The government holds 45 % of the shares listed on the Saudi exchange. The shares total 8.8 billion and the capitalization amounts to $155.92 billion. The government has formed many institutional funds that invest in several Saudi listed corporations and owns these shares through its institutional funds. There are many governmental funds and the main institutional investors in Saudi Arabia comprise the Public Investment Fund, the Public Pension Agency and the General Organizations for Social Insurance. It has been argued that the rich families used to own small ventures which were transferred to listed corporations, and were then able to keep a significant number of shareholdings inside those corporations. These listed family corporations are active in different stock exchange sectors, including energy and communication.

The argument against the Saudi ownership structure is that the CGC provides the listed corporations' articles of association that should state clearly the appointment and removal of the board members and their length in office. The board member should not join the board for more than 3 years although this is subject to renewal. Board members should not occupy board seats in more than five listed corporations at the same time. The practice of these lawful clauses is undermined by the influence held by rich families and the government. Rich families usually nominate board members for an unlimited period of time, and they often represent more than five listed corporations simultaneously. In contrast, the government usually influences the appointment and removal of board members in the listed corporations where it holds a significant number of its shareholdings. The supporters of government ownership argue that the government has more than enough votes to replace its representatives in those listed corporations' boards. In the case of the *Saudi Arabian Mining Company* the government was able to elect five out of nine of its board members on the basis of its ownership of 50 % of the company's shares. Opponents of the government and rich families' impact on the ownership structure argue that permitting the board members to work for an indeterminate mandate and time weakens the board members' contribution to the corporation. In particular, the shareholders' representatives on the board would not be able to challenge those sent by the government and the rich families when making decisions given the power imbalance.

The categories of board membership were examined in Sect. 16.6. The CGC recognizes the implications surrounding the presence of executive, non-executive and independent members on the listed corporations' boards. It was demonstrated that a corporation board's Nomination and Remuneration Committee plays a major role in selecting non-executive and independent members to join the corporation's general meeting. The Capital Market Authority's General Department of Corporate Governance also carries out an important task when evaluating listed corporations' boards' annual reports in order to check for non-executive and independent members.

The board sub-committees were the focus of Sect. 16.8. The CGC is flexible in terms of encouraging the board to decide what kinds of co-operative committees should be created. However, it advises that the board should at least establish an Audit Committee and a Nomination and Remuneration Committee. These co-operative committees need to be stated clearly in the board annual report. Although the board can delegate some of its jurisdictions to be managed by the co-operative committees, it still has ultimate responsibility for any delegated work undertaken by them. The Capital Market Authority Board has mandated Articles 13, 14 and 15 of the CGC, which are related to board sub-committees, good auditing and accounting measures and which are expected to be feasible in listed corporations. However, the Audit Committee should contain at least three members, both non-executive and independent, who are experts in finance, auditing and accounting, to be part of this committee. Specifically, the audit committee is accountable for checking the usefulness of the internal audit system, charging and discharging the external auditors, examining jointly with the external auditors the corporation's audit plan and the board's annual report. The Capital Market Authority Board has recently begun to list companies in breach of Audit Committee requirements as stated in the CGC. However, it does not indicate whether the external auditors encounter difficulties from board members or corporation employees when carrying out their duties. The Nomination and Remuneration Committee's remit was also outlined, including recommending new board members, updating the required certificates for board membership, discussing the board's strengths and weaknesses, checking the independence of non-executive and independent members, ensuring the absence of conflicts of interest and proposing board members' compensations.

Board members' compensation was debated in Sect. 16.9. Saudi board members' compensation arrangements are in a very poor state. The Consultative Council recently evaluated remuneration as not more than $133,333 per member, including, surprisingly, executive members. The CGC indicates that the board members' compensation policy should be stated in the corporation's articles of association. Compensations can be awarded as salaries, bonuses and attendance payments. The CGC does not define the maximum amount for remunerations, but states as a condition that they should be approved by the general meeting and included in the board's annual report.

16.10.2 Recommendations for the Reform and Improvement of Saudi Board of Directors

Board members should be highly and appropriately qualified in finance, law, management and economics. Accordingly, the CGC should make this a mandatory condition for all board members and top executives. Board members and top executives should be trained in a designated institute of directors as found in the UK but which has yet to be established in Saudi Arabia. The institute of directors would take on a range of useful roles and responsibilities, including raising awareness of the advantages of corporate governance among directors and top executives and enhancing their management skills.

Moreover, even though the CGC supported the separation of the roles of board chairman and chief executive, this step has not been fully translated into practice, largely due to the presence of the rich families and the government ownership pattern throughout the vast majority of listed corporations. Hence the Capital Market Authority Board should make greater efforts to ensure this regulation is implemented, in order to minimize the negative influence exerted by the rich families and the government on the nomination of board members for an indeterminate period of time and board mandate. On the other hand, a clear classification of the board members' duties including the duty of care, the duty of loyalty and the duty to act within their powers would inspire the board members to control the corporation responsibly and to behave truthfully and accountably to all the groups beneficial to the corporation. Therefore, the CGC should comprise requirements to clearly profile these duties.

Further, the CGC exceptions regarding conflicts of interest within the board under Article 18 of the CGC should be cancelled by the Capital Market Authority Board as these concessions allow board members to compete and trade in their corporations' submissions. In contrast, the Committees for the Resolution of Securities Disputes should not have the right to imprison individuals in breach of the regulations on conflict of interests and insider trading. Good practice regarding this fundamental principle is exemplified in the UK Companies Act, which transmits these deeds to be a matter for the Criminal Prosecution Service.

The CGC should enact specific points to define executive members: they should not hold positions for more than 3 years without the shareholders' agreement and there should be full transparency and disclosure of the board executive members' revenue. These significant points can be regulated based on the Cadbury report.

The Saudi board meeting aims to be an open discussion, yet the CGC does not frame noteworthy criteria for board meetings. Questions to be addressed include how often board members should meet, how many members should be present at a meeting for it to be legally acceptable, and how many votes should be combined to shape the board's final decision The CL specifies that the meeting of the board of directors shall be valid only if attended by at least one half of the directors, provided that the number of those present shall not be less than three, unless the corporation's articles of association provide for a higher number. In addition, the resolutions of the board shall be adopted by a majority vote of the directors present or represented. In the event of a tie, the chairman's vote shall carry, unless the corporation's articles of association provide otherwise. None of these requisites appear in the CGC. In view of their significance in civil and criminal liabilities when shareholders litigate against board members they should be transmitted under the CGC.

In order to give the board of directors more power to fulfill its duties and responsibilities effectively, the CGC should suggest several board sub-committees such as a risk committee, a finance and investment committee, a quality committee and a workforce committee to operate alongside the aforesaid Audit and the Nomination and Remuneration committees.

The CGC does not comment on inviting experienced non-members to join the audit committee meeting as required. This good practice, suggested in the Cadbury report, should be promulgated by the CGC. It is one of a number of noteworthy items from the Cadbury report that the CGC would be well advised to consider. Others include the stipulation that the audit committee should meet at least twice a year, that the external auditor and finance manager as well as other board members should frequently join the audit committee meetings, and that the audit committee and the external auditor should have at least one special meeting without the above-mentioned groups in order to eliminate any confusion over members' concerns.

The CGC should also highlight difficulties, which should not be presented when the external auditors review the corporation's information and annual report. The CL takes a valuable step towards the active operational role of the external auditors. It also validates that any board member, executive or employee attempting to hinder the external auditors will be sued. It is thought that this clause should also be adopted by the CGC.

In addition, the CGC omits to mention how many members the Nomination and Remuneration Committee should consist of. This is not in line with the recommendations for good practice found in the Greenbury report, which calls for three non-executive members. In addition, it is of concern that the CGC does not discuss how the Nomination and Remuneration Committee members should be rewarded. Again, guidance on good practice may be gleaned from the Greenbury report's recommendations that committee members be compensated with fixed lump sum payments determined by the board within the limits agreed in the corporation's articles of association and which should reflect the amount of time they commit to corporation business.

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