

Critical Analysis of the Code of Corporate Governance in the Light of Islamic Principles of Corporate Governance

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Abstract

Corporate governance is intended to create accountability in companies in order to avoid corporate disasters, as it believes on prevention rather than cure. This paper examines the code of corporate governance in the ambit of Islamic principles of corporate governance. It intends to identify weaknesses in the prevalent ideologies of corporate governance in Pakistan and propose reforms in them getting the insight from Islamic ideologies of corporate governance as well. To conduct research for this paper, qualitative research methodology has been used by employing doctrinal approach along with interpretative philosophy to comprehend the underlying meaning of corporate laws and the code of corporate governance of Pakistan. This paper would have a significant impact on the existing knowledge and the on-going debate regarding the significance of corporate governance principles for the advancement of business sector for accountability, transparency and disclosure requirements.

Keywords: Code of Corporate Governance, Company Law, Islamic concept of corporate governance, Independent non-executive directors (INEDs), Board of directors (BODs),

I Introduction:

Allah sent us to this world tested by Him for a purpose to develop our expertise and capabilities through the responsibilities. He says:

*"I have created only jinns and men that they may serve me"*¹

The status of a man's responsibilities is towards him and toward the Ummah as a whole. It is the responsibility of all Muslims to justify the usage of resources in all their deeds which Allah has bestowed.

*"Behold, thy Lord said to the angels: "I will create a vicegerent on earth." They said: "Wilt Thou place therein one who will make mischief therein and shed blood?- whilst we do celebrate Thy praises and glorify Thy holy (name)?" He said: "I know what ye know not."*²

In the governance of companies, man is the vital point for the system to be working meritoriously in the factual direction. In other words, he is the actual stakeholder. It shows that the man is a dominant pillar in the management and direction in order to attain the sole purpose of the company and to achieve company's vision and mission.

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¹ Al-Quran, Adh-Dhariat:56

² Al-Quran, Al-Baqarah:30

The Malaysian Finance Committee on Corporate Governance in its Report on Corporate Governance 1999 defines Corporate Governance as:

*“Corporate governance is the process and structure used to direct and manage the business and affairs of the company towards enhancing business prosperity and corporate accountability with the ultimate objective of realising long-term shareholder value, whilst taking into account the interest of other stakeholders”.*³

Good governance is not just relative to attain corporate brilliance. Though, it is the basic requirement for economic and social advancement. Present corporations are not just business objects instead the devices of economic and social revolution.⁴

*“Corporate Governance is the system by which companies are directed and controlled. Board of directors is responsible for the governance of their companies. The shareholders’ role in governance is to appoint the directors and the auditors and to satisfy themselves that an appropriate structure is in place.”*⁵

In terms of corporate governance, the company directors, management and auditors should act with the aim of satiating the optimal requirements of the shareholders and Allah as well. The key objective of corporate governance is to advance transparency, trustworthiness and accountability; the standards which are dominant in ISLAM.

While talking about accountability, it is the faith of Muslims that they will have to face *karma*; in other words, a person will be accounted for what-ever he does in this world and in the hereafter (life after death). One has to follow Allah’s path in order to look for His pleasure which means, each act should be according to the Islamic teachings. There should not be any existence of deception and substantial misstatement in their dealings and conduct. The Holy Prophet (peace be upon him) said:

“Each one of you is a guardian and each guardian is accountable to everything under his care”

The notion of transparency has been revealed by Allah in the following ayat:

*“O ye who believe! When ye deal with each other, in transactions involving future obligations in a fixed period of time, reduce them to writing. Let a scribe write down faithfully as between the parties”*⁶

The companies are answerable to stakeholders. Therefore, their aims should not be just to get financial benefits instead they also have the social responsibility towards Ummah. Companies should disclose and unveil information regarding their policy making, taking decisions and activities undertaken such as their Corporate Social Responsibility, as the Islamic system desires truthfulness, veracity, honesty and integrity in the governance mechanisms. As stated in Bukhari:

*“if he does not strive diligently to promote their welfare, he will not enter Paradise with them.”*⁷

³ Dato Shahraili Haji Abdul Munid, “Corporate Governance in Islamic Perspectives”, *MICG Malaysian Institute of Corporate Governance*, 2007

⁴ Dr Madhav Mehra, President of World Council for Corporate Governance

⁵ Cadbury Sir Adrian, *Report of the Committee on the Financial Aspects of Corporate Governance* (London: Gee and Co. Ltd. 1992).

⁶ Al-Quran, Al-Baqarah:282

In terms of transparency, it is the responsibility of companies to disclose information regarding their policies and contribution towards community regarding the usage of means and fortification of environment.⁸

The Quran depicts the notion of trustworthiness as:

“O ye who believe! betray not the trust of Allah and the Messenger, nor misappropriate knowingly things entrusted to you.”⁹

Islam preaches to follow highest ethical conduct in the dealings of business and commercial activities. This wisdom of stewardship takes everyone to develop the properties delegated to them according to their paramount capabilities as a submission to Allah. The chief executive officer must be judged by how the financial matters are being coped according to the Islamic principles instead of considering that how much the wealth has grown.

The Holy Prophet (peace be upon him) said:

“Righteous businessmen will be raised on the Day of Judgment”

“A truthful merchant will be raised on the Day of Judgment together with the truthful and the martyrs”¹⁰

While talking about fairness, Islam advocates combined decision making, patience, civil and political independence.

“It is part of the Mercy of Allah that thou dost deal gently with them. Were thou severe or harsh-hearted, they would have broken away from about thee: so pass over (their faults), and ask for (Allah’s) forgiveness for them; and consult them in affairs (of moment). Then, when thou hast taken a decision put thy trust in Allah. For Allah loves those who put their trust (in Him)”¹¹

Islam is obdurate regarding independent justice:

“Allah doth command you to render back your trusts to those to whom they are due; and when ye judge between man and man, that ye judge with justice: Verily how excellent is the teaching which He giveth you! For Allah is He Who heareth and seeth all things”¹²

II Corporate Governance Framework and Pattern of Shareholding in Pakistan:

The corporate sector of Pakistan like USA, UK and rest of the world had also experienced several corporate scandals; PTCL, NICL, NPP and PR are few examples of worse corporate governance.¹³ The Securities and Exchange Commission of Pakistan

⁷ Al-Buraey 2007, p.5

⁸ Rozaini Haniffa and Terry Cooke, “Culture, Corporate Governance and Disclosure in Malaysian”, Abacus 38, no. 3, 2002, pp.317-349

⁹ Al-Quran, Al-Anfal:2

¹⁰ Narrated by Al-Tirmidhi (1210), Al-Daarimi (2/247), Ibn Maajah (2146), Ibn Hibaan (11/276)

¹¹ Al-Quran, Al-Imran:159

¹² Al-Quran, An-Nisah:58

¹³ Waqar Ghani and Junaid Ashraf, “Corporate Governance, Business Group Affiliation, and Firm Performance: Descriptive Evidence from Pakistan”, *Centre of Management and Economic Research Working Paper Series 05-35*, 2005, 19

(SECP) established in 1997, is the primary watchdog and retains the authority to enforce and implement the codes of best practice in the corporate sector of Pakistan.¹⁴

The SECP implements the code by making them the part of listing rules, as it assures the implementation and adoption of the Code.¹⁵ The Code comprises the principles of best practices envisioned to provide a contrivance for the governance of companies listed on stock exchanges of Pakistan. The basic aim of the Code is to safeguard the benefits of stakeholders' and stimulate market buoyancy which eventually have an affirmative influence on the companies' outcome. To achieve this aim, the Code formulated by getting the insight from other countries having different models of corporate governance, predominantly from the UK, the USA and South Africa.

The corporate sector of Pakistan consists mainly upon family and State Owned Enterprises. Families are the key stakeholders in both public and private companies.¹⁶ Among privately owned businesses, more than fifty per cents of shareholding are owned by spouses (two persons) just to fulfil the criteria of privately owned business according to Company Law.¹⁷ Moreover, more than 75% of shareholding in the public companies is also held by families unlike UK and many other countries where dispensing 25% of shares to general public is mandatory requirement for the establishment of an active and dynamic market.¹⁸

Nevertheless, neither the code nor listing rules contain any such requirement in the corporate market of Pakistan and consequently, certain groups and families grasp the controlling authority by owning large shareholdings which bereaved the individual investors and smaller shareholders to have their active participation in the board meetings. Even the combined voting could not curb this issue due to the concentration of major shareholding in selected hands. Moreover, the concentration of shareholding in few hands creates liquidity issue in the business market. The interlocking management and pyramiding are composite phenomenon difficult to be apprehended by a common investor.

Furthermore, the executive and non-executive directors are usually appointed among relatives or on the basis of personal relations on the demise of skilled, experienced

¹⁴ Faryal Salman, and Kamran Siddiqui, "Corporate Governance in Pakistan: From the Perspective of Securities and Exchange Commission of Pakistan", *The IUP Journal of Corporate Governance*, 12, no. 4, 2013, 13-15; Faryal Salman and Kamran Siddiqui, "Corporate Governance in Pakistan: From the Perspectives of Pakistan Institute of Corporate Governance", *The IUP Journal of Corporate Governance* 12, no. 4, 2013, pp.17-20

¹⁵ Haroon Hamid, and Valeria Kozhich, "Corporate Governance in an Emerging Market: A Perspective on Pakistan", *Journal of Legal Technology Risk Management* 1, no. 1, 2006, pp.1-3

¹⁶ Awais Gulzar and Zongjun Wang, "Corporate Governance and Non-Listed Family Owned Businesses: An Evidence from Pakistan", *International Journal of Innovation, Management and Technology* 1, no. 2, 2010, pp.124-125

¹⁷ Adnan Ibrahim, "Corporate Governance in Pakistan: Analysis of Current Challenges and Recommendations for Future Reform", *Washington University Global Studies Law Review* 5, no.2, 2006, p.323

¹⁸ Moin Fuda, CIPE 1, Corporate Governance in Family-Owned Companies in Pakistan, (2014), <www.cipe.org/publications/detail/corporate-governance-family-owned-companies> (accessed 10 March 2018)

and capable persons. The board of directors has to take significant policy decisions which they generally take without formally calling the proper meeting fulfilling its all requirements. The idea of retaining this concentration of control is to achieve enigmatic benefits and to have their hold on the complete stream of trade.¹⁹

After families, the state is the second largest stakeholder in both listed and non-listed companies. The state-owned enterprises signify 52.8% of the cumulative capitalisation among the key forty companies listed on Karachi Stock Exchange. The state-owned companies are usually politically governed. Therefore, the governance of these companies depends on the enchantment of state, as every government changes the key positions of administration and the conditions for the selections on these positions is political affiliation leaving aside the appropriate experience and qualification.²⁰

The authors submit that family-owned and state-owned companies are crucial for the growth of corporate market in Pakistan though; the control maximisation is a great interruption in this development. These large shareholders (family and state) generally oppose modifications and growth of best principles of corporate governance as these principles creates the system of check and balance and frightens to delist their companies. In fact, there was a substantial delisting after the declaration of the first code of corporate governance in 2002.

Moreover, several small and private companies including family-owned are ignorant from the optimal advantages of developed corporate governance.²¹ In order to overcome this issue, SECP constituted Pakistan Institute of Corporate Governance (PICG) in order to disseminate the cognizance regarding the benefits of complying with the codes of best practice in corporations. The PICG has trained several individuals to execute this assignment.

Moreover, dispersed ownership has been introduced recently in Pakistan. The state divested its shareholdings to the public in the early twenty first century.²² This act of state enticed family-owned and multinational companies²³ which generated the trend of public shareholding in the corporate market. Though, the proportion of this shareholding is quite lesser while comparing with the shareholdings of large stakeholders such as, families, state and multinational companies. The government, in the recent past, planned to dissociate 26% of its shareholding in 80 state-owned enterprises and 12% to be

¹⁹ Attiya Javid and Robina Iqbal, "Corporate Governance in Pakistan: Corporate Valuation, Ownership and Financing", *PIDE Working Papers 2010*, Vol. 57, 2010, p.12

<<http://pide.org.pk/pdf/Working%20Paper/WorkingPaper-57.pdf>> accessed 20 December 2017

²⁰ Robert McGee, "Corporate Governance in Transition and Developing Economies: A Case Study of Pakistan", *Working Paper. Florida International University*, 2010,

<<http://ssrn.com/abstract=1665112>> (accessed 10-01-2018)

²¹ IMF Report on the Observance of Standards and Codes (ROSC); Corporate Governance Country Assessment (Pakistan), June 2005, by World Bank, Report on the Observance of Standards and Codes (ROSC) Corporate Governance

²² John Cubbin and Dennis Leech, "The Effect of Shareholding Dispersion on the Degree of Control in British Companies: Theory and Management", *The Economic Journal* 93, 1983, p.355

²³ The multinational companies are those companies who are registered as domestic company as subsidiary companies of overseas holding companies according to the companies ordinance 1984.

distributed among employees, which will promote the notion of dispersed ownership in the corporate structure of Pakistan.

After state, multinational companies are the third substantial stakeholder in the commercial sector of Pakistan. Among the leading forty listed companies at Karachi Stock Exchange, five are multinationals which institute 17% capitalisation.²⁴ The multinational companies bring foreign direct investment (FDI) in country which is inevitable for the economic development. In addition to this, the multinationals are more strict and anxious about the adoption of best principles of corporate governance due to which they are renowned for being transparent in their dealings fulfilling the disclosure requirements and likewise demonstrate high standards of governance. The governance strategies of multinationals working in Pakistan can be a motivational force for local business community for improving their governance standards and taking the implementation of the Code earnestly. Moreover, the existence of multinationals and growth of their performance can also instigate government to play its role for the development of a strong corporate governance mechanism in the country.

The authors submit that the foreign direct investment can further be increased if the governance standards of Pakistan's corporate sector are upgraded. Multinational companies may act as role model for indigenous companies in terms of disclosure, transparency, accountability and other governance standards. The authors additionally assert that the banks and institutional investors are also large shareholders in Pakistan's business market but their role corporate governance of the country is very minute. Banks give appropriate representation to institutional investors in their respective board of directors however; their role is limited in other corporations and organisations which should be addressed seriously as they can be an impetus of change and development of corporate governance in Pakistan being experts of investment and influential due to their large shareholdings.

III Critical Analysis of the Code of Corporate Governance of Pakistan and Recommendations for its Improvement:

Good governance is the key to attain the confidence of investors which influence the investment decisions and attract foreign direct investment which is inevitable for economy of a country. Moreover, the adoption and implementation of good governance standards is also required to compete globally.²⁵ Corporate governance is required for both business opulence and accountability. Hence, the SECP strived to raise the standards of corporate governance standards.²⁶ The issuance of the first code of corporate governance (the Code) in 2002 was the first major step in this regard. The Code set out a mechanism accustomed to handle the densities of the Pakistan's business market and besides accumulated the corporate governance principles as epitomised in several substantial intercontinental models of corporate governance.²⁷

²⁴ Ali Cheema et al., *A Comparative Analysis of Corporate Governance in South Asia: Charting a Road Map for Bangladesh*, Corporate Governance in Pakistan: Issues of Ownership, Control and the Law, 2003

²⁵ Steven Bainbridge, *The New Corporate Governance in Theory and Practice*, (New York: Oxford University Press, 2008), p.6

²⁶ Mr Muhammad Ali, The former Chairman of the SECP.

²⁷ Qaiser Yasser, "Corporate Governance and Performance: A Case Study for Pakistani Communication Sector", *International Journal of Trade, Economics and Finance* 2, no. 3, (2011), 1

The implementation of the Code was professed obligatory by SECP as it was made the part of listing rules for the listed companies. However, the adoption of two provisions of the Code was left voluntary. The authors submit that the voluntary provision of the Code relating to the representation of independent non-executive directors (INEDs) ought to be obligatory in place of voluntary. The argument is that the office of INEDs has a considerable significance and impact on the company matters in order to look after the process of decision-making among corporate boards. Though, in Pakistan the office of INED is measured as an honorary position and the individual from family or friends is usually appointed on this significant position leaving aside the suitable person. Although the Code clearly states that:

*"the expression "independent director" means a director who is not connected with the listed company or its promoters or directors on the basis of family relationship and who does not have any other relationship, whether pecuniary or otherwise, with the listed company, its associated companies, directors, executives or related parties. The test of independence principally emanates from the fact whether such person can be reasonably perceived as being able to exercise independent business judgment without being subservient to any apparent form of interference."*²⁸

Furthermore, while the compliance with the code was made a condition precedent for the listing of listed companies, even then the compliance was not satisfactory, mainly due to the lack of interest on behalf of government, the consigned benefit of families and several other causes. Therefore, the authors argue that the strong compliance mechanism is inevitable to achieve the real impact of the Code. Publishing the code was a bold step, but this code is not used if cannot be applied in letter and spirit.

Moreover, it appears that at the time of drafting the Code, other corporate laws were not corroborated or verified, since these laws and the Code overlap with each other. For example, the 2002 Code requires that the chairman of the publicly traded company ensure that the minutes of the board meetings have been correctly drafted.²⁹ However, article 173 (1) of the Ordinance³⁰ confers on the company itself the responsibility of keeping a correct record of the minutes of the proceedings of the Annual General Meeting, without specifying, however, what is 'Company' means that the company is a legal person administered by several offices, and the disposition of the order does not specify which office of the company is answerable for performing this task.

Though, the 2012 Code uses the word 'Chairman' to fulfil this purpose.³¹ These contradictory and overlapping provisions create an obstacle to carrying out the most significant job of recording the minutes of the Board meetings. In addition, compliance with the provisions of the ordinance is obligatory and, in case of violation, the offender (s) must pay a fine; conversely, defiance with the code is compulsory also. In such a situation, the executive directors of the boards of directors believe that they can use these provisions for their benefit. The authorities should cogitate seriously on these issues, since it is the meetings of the boards of directors that decide the fortune of a company;

²⁸ Clause (i) (b) of the code of corporate governance 2002

²⁹ Clause (xii) of the CCG 2002

³⁰ Section 173(1) of the Companies Ordinance 1984

³¹ Clause (viii) of the CCG 2012

they also determine the fate of the shareholders. Therefore, a consistent and formal procedure should have been defined in all company laws to record board meetings.

In addition, the ordinance provides that,³² a person cannot be a director of a publicly traded company and, in it or in its partner participates in the brokerage business as an associate of a stock exchange. However, the Code does not prohibit that person from being a director of a publicly traded company if he obtains exemption from the SECP. In such a situation, the Code itself offers the opportunity to persons with vested interests may be exempt from the SECP and may be attached with the business of the company. In this situation, where does the ordinance stand for, whose violation initiates a procedure before the courts? The authors argue that the law and rules should be free of such uncertainties and that authorities should take them seriously if they wish to improve corporate governance practices in letter and spirit.

Furthermore, the Ordinance states that:³³

any stakeholder (director, CEO or executive) of a company³⁴ retaining equity securities more than ten per-cent as favourable holder of a listed company is under obligation to prepare a report of any profit s/he gets from the trade of these securities within six months. Moreover, such person is additionally under obligation to declare that gain to the company and indicate this to the Registrar³⁵ and the Commission.³⁶

However, the Code³⁷ provides that:

such person making any gain shall immediately notify the Company Secretary in writing and will furthermore provide the documented record of the cost and amount of shares within four days of such transaction. Then it is the responsibility of the Company Secretary to document and present it before the BODs in its next meeting.

In this case, the code establishes unblemished and sterner provisions that must be applied; though, the ordinance relaxes the rules by providing an extended period of six months to reveal any gain obtained by the interested party in a business. Six months are sufficient for a person to earn profits from the actions of a corporation and then delete their file.

This ambiguity between two laws and regulations generates confusion as compliance with the Ordinance is compulsory for all companies and violation of this implicates application of penalty nevertheless, the SECP further demands comprehensive implementation of the Code. Resultantly, corporations chose and comply with the provision according to their choice which stops the growth of virtuous corporate governance practices. These contradictory and ambiguous laws make their application even more difficult. As the degree of enforcement of laws comes later, the laws must first be strong and effective enough to be followed them. Decision makers must apply

³² Section 187(j) of The Companies Ordinance 1984

³³ Section 224 of the Companies Ordinance 1984

³⁴ Including directors, officers, major shareholders etc.

³⁵ Registrar means the Registrar performing the function of registering companies under the Companies Ordinance 1984.

³⁶ Here Commission means the Securities and Exchange Commission of Pakistan.

³⁷ Both CCG; clause (xxvi) of the CCG 2002 and clause (xxiii) of the CCG 2012

regulatory impact assessment (RIA) more rigorously in order to promote accountability and transparency among corporations.³⁸

Moving further, the Code 2002 was substituted with the Code 2012, which has also been incorporated in the appropriate Listing Regulations. The revised Code accentuated the significance of independent directors on the board of directors and declares the appointment of at least one independent director obligatory though, 1/3rd independent directors of the total members of the BODs is desired.³⁹ Additionally, the new Code of 2017 acknowledged the significance of NEDs, and declared two NEDs compulsory for each corporate board of listed companies or 1/3rd whichever is higher.⁴⁰

However, the authors argue that this number of independent directors must be enlarged by at least 50% in the board of directors to guarantee a tighter control of the board of directors to increase accountability and transparency. Secondly, PICG must also strive to make the business community aware that NEDs appointment on the Board is not just honouring friends and family members instead NEDs should be autonomous persons who could supervise strategies and decision-making of board of directors in order to make corporate boards more accountable and making their proceedings more transparent. In addition, the total number of director positions that a person can have at one time is abridged from seven to ten in the 2012 Code, which has been reduced to five in the new code proposal of 2017. Though there is no limit of holding director positions in a listed holding company.⁴¹ The authors argue that the primary aim to lessen the number of director positions might be to reduce a director's workload so that he can do justice to his duties to corporations. To achieve this purpose, this number could be further condensed, since the position of the director in seven companies is still too heavy. A person is unable to do justice while having too many liabilities towards several businesses.

This interlocking directorate is a fairly ancient and widespread phenomenon in companies.⁴² Yet, legal efforts have been made to minimize this phenomenon. Companies can obtain the paybacks that lessen environmental improbability via an interlocking horizontal organization that unites its competitors; vertical harmonization that associates an organization with input subcontractors or output receivers; Competition and greater reputation.⁴³ However, antitrust legislation assumes that the establishment and maintenance of market uncertainty through competition is a social good. Though, reducing this insecurity through interrelation could be a strategy to increase profits for companies and their shareholders.

³⁸ Rasul Raees and Asif Saeed, "Regulatory Impact Assessment (RIA) of SECP's Corporate Governance Code in Pakistan", *CMER Working Paper No. 05-39*, (2004), <http://saber.eaber.org/sites/default/files/documents/LUMS_Rais_2005.pdf> (accessed 20 June 2018)

³⁹ Clause (i) (b) of the CCG 2012

⁴⁰ The latest criteria of independence are provided u/s 166(2) of the Companies Act, 2017.

⁴¹ ⁴¹ Clause (ii) of the CCG 2012

⁴² Michael Jacobs, *Combatting Anti-Competitive Interlocking: Section 8 of the Clayton Act as a Template for Chile and Similar Emerging Economies*, *Fiscalia Nacional Economica Working Paper*, (2013), www.fne.gob.cl/wp-content/uploads/2013/11/Clayton-Act-Section-8.pdf (accessed 10th January 2018)

⁴³ David Schoorman *et al.*, "Interlocking Directorates: A Strategy for Reducing Environmental Uncertainty", *The Academy of Management Review* 6, no. 2, 1981, p.243

In Pakistan, antitrust legislation is known as ‘the Competition Act 2010’. Section 3 of the law prohibits the abuse of any dominant position by acts that limit or distort competition in the concerned market. Nevertheless, the applicability of this law does not appear to have been effective until now, since interlocking management overcomes and is little used in Pakistani companies, especially in family businesses.

The authors argue that a person being director of numerous companies cannot be impartial regarding the matters of a particular company. Resultantly, the assets of the general public and investors are on higher risk in that company. This practice can be reduced in two ways; First, introduce legislation or modify the code and reduce the number of managerial positions that a person can occupy; secondly, by strengthening the influence of institutional investors by strengthening their role in corporate governance, by granting them the appropriate involvement and representation of the boards so that they can control the strategies and actions of those directors.

In addition, the new code announced the assessment criteria of the board of directors to guarantee the responsibility of the board of directors for their strategies and activities. However, it is up to the board of directors of each company to define an evaluation mechanism within two years after the publication of this code. The authors advocate that, instead of leaving this on the board of directors of each company, the SECP should develop a general evaluation mechanism for the board of directors and publish it on its website to guide each company. Companies must evaluate the performance of their meetings according to these criteria and indicate it in their annual reports. Though, companies can amend the general criteria defined by the SECP based on the different and modified requirements of their business by formally obtaining SECP approval on a ‘one size fits all’ basis.

The Code⁴⁴ further provides that:

there should be a defined and fair mechanism regarding directors’ remuneration and its disclosure in the annual report of listed companies. The chairman of the audit committee will now be an INED, who will not be the chairman of BODs. Audit Committee will consist upon NEDs.⁴⁵ The secretary of Audit Committee will either be the Company Secretary or Head of Internal Audit and the CFO will not be elected as the secretary to the Audit Committee.⁴⁶ The task of Internal Audit might be commissioned by a listed company to a specialised services company or be executed by the Internal Audit staff of the holding company.⁴⁷

Some provisions of the code have been revised based on the lessons learned from the day-to-day problems and concerns of listed companies. The basic purpose is to guarantee that it mimics changes in fears of governance, financial situations, international practices and standards.

On the other hand, the authors argue that this Code still has few issues. One, some of its provisions instead of solving the governance problems escalates them, again for being mystifying and overlapping with the Ordinance like the previous Code.

⁴⁴ Clause (xvii) of the CCG 2012

⁴⁵ Clause (xxiv) of the CCG 2012

⁴⁶ Clause (xxx) of the CCG 2012

⁴⁷ Clause (xxxi) of the CCG 2012

Moreover, the implementation issue of the Code in its true sense also remains the same as was with the previous Code. However, the positive impact of the Code has started to be seen as the corporations have started to acknowledge corporate governance best practices and their significance.

For example, irrespective of the voluntary requirement to designate INEDs, many companies, whether they are listed or not, have chosen INEDs. However, it is difficult to find people who are ready to take on the role of INEDs, since the remuneration is not equivalent to their roles and responsibilities. An adequate compensation plan is vital for hiring competent persons who will fulfil the duties of this office.

In addition, the 2012 Code requires listed companies to dispense a statement in their annual reports to elucidate their position concerning the compliance with the code. The statement must be true and in advance and must be based on the essential evidence provided by the company making the statement. Each issuer must ensure that the declaration of Code Compliance is reviewed and confirmed by the auditors when this statement can be confirmed fairly, before publication. Legal auditors must ensure that their non-compliance with the requirements established in the code is recognised in their annual report. However, in a certain situation in which defiance with the Code is a practical procedure, SECP is authorized to award immunity from compliance with this situation to appropriately record the details for non-compliance.⁴⁸

These provisions of the Code reveal that SECP is taking the compliance with the Code seriously. The authors submit that the Code encloses several resilient provisions too and as a result the business community has started to give importance to good governance standards. However, there are some basic lacunas in the Code which needs to be addressed and rectified in order to achieve the international standard of best principles of corporate governance.

In summary the authors conclude that, the provisions of the Code should not be contradictory with other corporate laws as the compliance with Code has been declared mandatory by SECP and when two mandatory laws/rules come into conflict, their application becomes difficult.

Another substantial task is to create cognizance regarding the advantages of adopting the principles of corporate governance, the PICG should announce more effective methods to raise awareness in the business world, since it has been observed that new entrepreneurs with little or no knowledge. They consider principles of corporate governance heavy. This can be attained by organizing regular seminars and workshops on the significance of corporate governance principles, their influence on make the most of shareholder wealth and corporate performance.

Rating agencies can also play their part in this by publishing an annual rating list of companies that comply with the Code. Institutional investors can be proved fruitful in this regard. In addition, the subject of corporate governance can be included in the curriculum of business schools and LLB students can also be taught with the subject of corporate law. Third, misconceptions about the INED office should also be eliminated (as

⁴⁸ Clauses (xI), (xLi) and (xLii) of the CCG 2012

indicated above); people perceive this function as an honour that CEOs can appoint a director outside the NED position to pay homage.

Moreover, an appropriate and firmer procedure for the appointment, roles and responsibilities of INEDs should be introduced. Consciousness is required on both sides; the companies and INED with respect to the responsibilities of this office, the purpose of designating INEDs for board of directors is to supervise the policies and strategic decision making of board of directors to defend the interests of the shareholders. The authors believe that corporate governance has to do only with protecting the interests of the shareholders and improving the performance of the business.

Lastly, the regulators should review the Code regularly keeping in mind the environment of corporate sector of Pakistan. The authors believe that by regularly modifying and revising the code, taking into account the needs and changes in the business environment, it will help to improve Pakistan's business sector to a large extent, as it is being done now gradually.

IV Conclusion:

This paper established that the basic pillars of good corporate governance are transparency, accountability, responsibility, fairness, competency, integrity, loyalty/truthfulness, tolerance, trust, sincerity and not being a hypocrite which are the teachings of Islam. The authors submit that the analysis of code of corporate governance reveals that the underlying idea of introducing and formulating code of corporate governance is actually to achieve these attributes in corporations, as these are the principles of good corporate governance.

The principles of good corporate governance have their impact on corporations, society and on the economy as whole. For instance, the companies who adopt the principles of good governance, the value of their shares increases, their capital cost reduces, their capital efficiency enhanced and shareholder's rights are protected. Moreover, it creates a transparent society by preventing corruption, by establishing rule of law and by promoting ethical wealth creation. Additionally, it increase competitiveness among corporations through fair competition nationally and internationally, helps in making positive developments in capital market, helps in achieving more sustainable economic growth and revitalise market economy.

This paper conducted a comprehensive examination of the code of corporate governance of Pakistan by employing a doctrinal methodological approach and tested it in the light of Islamic principles. It identified the strong and weak provisions of the Code and formulate recommendations whose incorporation can make the Code more effective in terms of achieving the goal of good corporate governance with that of Islamic principles i.e., transparency, accountability, responsibility, fairness.