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Impact of New Corporate Governance Code on Disclosures: Evidences from Bahraini Listed Commercial Banks

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Abstract

Corporate Governance has attracted a great deal of public interest after numerous financial irregularities occurred across the globe such as, Olympus, Satyam, Enron, WorldCom, AIG and so on. Taking cognizance of this, The Ministry of Industry and Commerce (MOIC) of Bahrain issued a Code of Corporate Governance which was made effective from January 1, 2011. Central Bank of Bahrain (CBB) has subsequently updated its Rules Book for its licensee banks based on this code. The purpose of the study is to determine the coverage of corporate disclosure's by all listed commercial banks in Bahrain Bourse and test their quality, before and after the Corporate Governance Code. For the purpose of this study, a detailed questionnaire was constructed after substantial literature review and brainstorming with various researchers, practitioners and bankers. Each bank's disclosures such as annual reports of 2010 and 2011 and other records available in their website were deeply analyzed and used to answer the questionnaire. In this study, all banks' board have been found recognizing the increasing importance of good corporate governance practices, as an important ingredient in the creation of sustainable shareholder value and protecting the interest of all shareholders. The study concluded that there occur effective and positive changes in corporate disclosures after the introduction of Corporate Governance Code.

JEL Classification Numbers: M14
Keywords: Corporate Governance, Board of Directors, Audit Committee, Disclosures, Annual Reports

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1 Introduction

Corporate Governance has attracted a great attention recently, especially after numerous financial irregularities in big and reputed companies, global financial crisis, and euro crisis in a worldwide context. In fact, the issue of governance has been much in interest and there is a believe that once the systems and procedures of governance as prescribed in the various codes are realistically adopted and implemented, transparency, fairness, board and management performance will be improved in the corporation, which turns in the reduction of fraudulent activities in corporate and improvement in public faith. Kirkpatrick (2009) once concluded, "The financial crisis can be to an important extent attributed to failures and weaknesses in corporate governance arrangements", by this we can notice that the problem of governance is faced by the whole world, and these were never implemented and practiced accurately and effectively. It is important here to distinguish between governance and management. Where management involves in the activities of directing a business, governance is more likely the oversight work for the entire company on behalf of the shareholders particularly and other stakeholders generally. Keeping in mind that the interest of various stakeholders is really important and that differs from the shareholders, in which a stakeholder can be anyone who has interest in the company and can affect or be affected by its decisions and actions. To understand the bigger picture, it is important to understand the various stakeholders' involvement in company.

Corporate governance is a system that defines the interaction among shareholders, the board, management and various other stakeholders. Where Management team, consists of CEO, CFO and so on, runs the company and the board oversees the management and makes sure that the management is running the company in the best interest of the shareholders particularly and for other stakeholders in general. Board also ensure that the management is doing their job in their best spirit, to maximize shareholders’ value, that’s why directors' duties and responsibilities are considered really important in corporate governance. Fairness, transparency, information flow, accountability, individual activities, and collective responsibility are considered the basic core values of corporate governance that are required to kick off any economy. Good governance protects shareholders, ensures equal treatment to all shareholders, requires a lot of disclosures and the board ought to be the body which oversees the all disclosures that take place and make sure that everything in the company is in the right path, to improve the confidence among shareholders.

1.1 The OECD Principles of Corporate Governance

The OECD Principles serves as one of the 12 key values for international financial stability of the Financial Stability Board and form the source for the corporate governance component of the Report on the Observance of Standards and Codes of the World Bank Group. Indeed, The OECD principles of corporate governance were certified by the ministers of OECD and initially adopted by the 30 member counties in the year 1999, and since then it has become a referential target globally for all the stakeholders, in which it includes notably the policy makers, investors and institutional and authoritarian frameworks. Abu-Tapanjeh (2007) summarized, "the core theme of the principles lies in four fundamental principles namely, 1.The mechanism of business ethics, 2. The mechanism of decision making, 3. Adequate disclosure and transparency, 4. The mechanism of book keeping and final accounts". Morck (2005) also states that the reliability and soundness of these principles have been proved by its implementation and adoption.

1.2 The Code of Corporate Governance of Kingdom of Bahrain

With the increased global challenges and competition, countries have become more interested in implementing a good corporate governance practices to be able to participate in the global economy, attract foreign investments and builds a foundation for sustainable economic growth. The Bahrain is also one of those countries that have placed a great interest in the existence of corporate governance state, and it has placed a great effort in issuing the Corporate Governance Code. Indeed, the Ministry of Industry and Commerce (MOIC) has drafted a new Commercial Companies Law, which incorporates numerous corporate governance provisions and rules. The MOIC has also issued a booklet and CD which provides guidance to directors as to the various laws which govern financial reporting requirements and other obligations to the different stakeholders. The Central Bank of Bahrain (CBB) is also very active in reviewing new corporate governance-related requirements for listed companies, and its licensees. MOIC, with the CBB, created National Steering Committee on Corporate Governance primarily to develop the new Company Law and in 2006 the Committee began its work to create Code of Corporate Governance (CCG). The committee was formed from representatives of various interested stakeholder groups. The committee developed a code of corporate governance, with the aim to support and strength Bahrain's corporate governance framework for all the companies. The draft code was presented at a public conference on 6 May, 2008 and the code was officially issued by the MOIC in 2010. All companies are required to adopt it starting from January 1, 2011, where full compliance required by end of the year 2011.

Originally, code applies to listed companies and licensees of CBB, but used as a model by all other companies to the degree that it applies to their circumstances. This code is issued on a *"Comply or Explain"* principle and has nine core principles that are in consistent with international best practices. These principles are discussed briefly in the literature review section. The code also, includes recommendations to apply the principles and gives support for the implementation of good governance. The CCG of Bahrain is considered as a dynamic document that is obviously in need of modifications from time to time to be able to response to the changing environment and circumstances. Further, the code also, goes beyond the company law requirements on a number of points e.g., duality of leadership; at least 50% of the board directors should be non-executive directors; and independent director does not own 5% or more of company's shares.

Further, a public-private partnership, the Bahrain Transparency Association, also in alliance of various market participants including, bankers, lawyers, auditors, academics, industry, and government representatives, have been working over the past ten years to improve Bahrain's corporate governance best practices.

1.3 Bahrain Bourse

Bahrain Stock Exchange (BSE) (now Bahrain Bourse) was established in 1987, however, officially began its operations in 1989 with just under 30 listed companies. In 2010, and according to Law No. 60 Bahrain Bourse (BHB), the shareholding company replaced BSE. As on 1st July 2012, there were 48 companies listed on BHB and distributed among

9 sectors, in which 2 companies are presently suspended from operating. The listed companies are classified according to their activity and the BHB operates as an autonomous institution supervised by an independent board, chaired by the Governor of the CBB.

1.4 Bahrain Economy

According to the International Monetary Fund (IMF), the growth in Gross Domestic Product (GDP) of Bahrain was 4.1% in 2010 compared to 3.1% in 2009. Owing the oil driven economy, there is an expectation that the real GDP growth accelerates to 5.104% in 2012 from 3.08% in 2011. Strong oil production and a highly favorable base effect will be the main driver of growth, however; latest political problems, with economic crisis in Europe can affect its growth. According to CBB's Economic Indicators Report of September 2011, the Consumer Price Index (CPI) was 111.4 in the 3rd quarter of 2011, 109.8 in the 2nd quarter 2011, 111.8 in the 1st quarter of 2011 and 112.3 in the 4th quarter of 2010. In fact, Bahrain competes with Malaysia as a universal center for Islamic banking and continues to search for new natural gas supplies as feedstock to carry and support its expanding petrochemical and aluminum industries.

1.5 Commercial Banks

As on 1st July 2012, there are 7 listed banks in the commercial banks sector of BHB. BHB's Annual Report (2010) reported "The commercial banks sector captured the largest share in terms of the value and volume of share traded comprising 40.70%, 54.18% respectively of the total value, followed by the investment sector 23.97%, 28.16% respectively. Ahli United Bank (AUB) came first in terms of the value of shares, while Gulf Finance House (GFH) was the most active in terms of the volume". Bahrain Banking Sector Report (2007) published by Global Investment House showed continuous impact of Bahrain's banking sector, being among the first that has a positive contribution and impact on Bahrain's domestic economy, in which it also highlights the importance of Islamic banking and its weighty contribution to the total assets of the banking system. This inspires the authors to select commercial banking sector for their study.

2 Literature Review

Cheffins (2011) described "corporate governance first came into vogue in the 1970s in the US. Within 25 years it has become the subject of debate in a global context by academics, regulators, investors and executives". This shows the roots of the term and when the phrase "Corporate Governance" became well known to everyone. According to Cadbury (1992), it is defined as “the system by which business corporations are directed and controlled”. This definition is considered traditional and focuses on how the business is being run, monitored, guided and regulated. Another definition of corporate governance is by Shleifer and Vishny (1997) where is it considered as narrow definition, more specific to the provision of finance and looks at corporate governance from an outside investor’s perspective and it does not really look at the interest of all stakeholders, instead focuses on the principle agent framework “Corporate governance deals with the ways in which suppliers of finance to corporations assure themselves of getting a return on their investment".

Zingales (1998) defines corporate governance in a more useful way and expresses the view that "allocation of ownership, capital structure, managerial incentive schemes, takeovers, board of directors, pressure from institutional investors, product market competition, labor market competition, and organizational structure, can all be thought of as institutions that affect the process through which quasi-rents are distributed.", so according to him corporate governance is "the complex set of constraints that shape the ex-post bargaining over the quasi-rents generated by a firm." Just like what Claessens (2003) commented on this definition, "It refers to both the determination of value-added by firms and the allocation of it among stakeholders that have relationships with the firm. It can be read to refer to a set of rules, as well as to institutions." This definition is even broader than the definition of corporate governance set by Adrian Cadbury (1992). In addition, highlighting what Wolfensohn (2001) defines corporate governance, "Corporate Governance is about promoting corporate fairness, transparency and accountability". This definition focuses on the core values of corporate governance; however there is one more core value, responsibility, in which it recognizes the right of stakeholders and encourages active cooperation between corporation and stakeholders. The business is also responsible for actions that it can take over and above compliance with minimum legal requirements. Dyck (2000) also express in adding this argument that corporate governance is generally the complex set of socially defined constraints that influence the willingness to make investments in corporations in substitute and exchange for promises.

The OECD defines Corporate Governance as, "Corporate governance involves a set of relationships between a company's management, its board, its shareholders and other stakeholders. Corporate governance also provides the structure through which the objectives of the company are set, and the means of attaining those objectives and monitoring performance are determined." This definition of the OECD is consistent with the one presented by Cadbury. From all of the above, we can reach to the following:

Corporate governance is a system; controls, rules, processes and procedures, which defines the interaction between shareholders, the board, management and other stakeholders, in which to ensure that the interests of all of these are met in full. The company is being managed in the interest of the shareholders and other stakeholders, where the main external stakeholder groups in contemporary business corporations are shareholders, debt holders, trade creditors, suppliers, customers and communities affected by the corporation's activities. Internal stakeholders are the board of directors, executives, and other employees. Corporate governance is all about balancing individual and societal goals, as well as, economic and social goals, so it has a broad scope including social and institutional aspects. It deals with the manner and way the providers of finance guarantee themselves of getting a fair return on their investment and since companies are owned by the shareholders, but run by the board of directors, corporate governance clearly helps in distinguishing between the owners and the managers and ensures that the company is run in the interests of those shareholders, while keeping in mind the interest of other stakeholders to be able to look at it from the right, effective way.

2.1 Corporate Governance Mechanisms

Where corporate governance mechanisms are used by organizations in order to manage their businesses whether they are large, privately or publicly held corporations, the mechanisms varies between societies and countries depending on a number of factors that affects how the country is shaped.

2.2 Board of Directors

The board as a body of a number of nominated members by shareholders for overseeing the company's actions and activities serves as one of the most important corporate governance mechanisms that are projected and intended just like what Barnhart, Marr and Rosenstein (1994) said; "to ensure that the interests of shareholders and managers are closely aligned and to discipline or remove ineffective management teams". There are different responsibilities of the board members, where the legal responsibilities differ depending on the nature of the organization and vary with the jurisdiction in which it operates. However, there are a number of responsibilities in common between with them, as Park and Shin (2003) stated, "Directors must act in good faith in the interests of the company, rather than those of the shareholders alone", this role is considered really vital for the board to pursue, where effectiveness of the board is considered a vital factor in determining the ability of the business in successfully achieving its objectives and is noted in the Commercial Companies Law in the Kingdom of Bahrain (2001);"A crucial element in determining whether a business can achieve the requisite flexibility is the quality and effectiveness of its board of directors, and the system of corporate governance in which the organization operates.". Indeed, regulators describe them as the ultimate corporate governance mechanism for monitoring the financial reporting process. The Cadbury report (1992) stated, "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 committee".
Hussain's and Mallin's (2002) claimed as “Bahraini companies have placed a number of corporate governance best practice's features, where boards are dominated by non-executive directors, and there is the separation of the roles of Chair and CEO". Further in 2003 they find "the key factors influencing the appointment of the non executive directors are relevant skill, business experience and reputation. The majority of companies also, have an audit committee, around a third have a remuneration committee. However, none has a nominations committee and in terms of the workings of the board, meetings are held on average 4.4 times a year. Succession plans are in place in a third of respondent companies.". This shows that the companies of Bahrain have realized the need of good governance even 10-15 years back which resulted in recent CCG.

2.3 Audit Committee

Deloittee (2012) explained the role of audit committee as "The audit committee is established with the aim of enhancing confidence in the integrity of an organization's processes and procedures relating to internal control and corporate reporting including financial reporting. Audit Committee provides an ‘independent’ reassurance to the board through its oversight and monitoring role".

3 Research Methodology

3.1 Objectives of the study

The study aims to test the quantity and quality of corporate governance disclosures by all listed commercial banks in BHB, before and after the introduction of CCG. The study will further try to examine the changes in governance related reporting after the introduction of CCG. Each bank disclosures will be deeply analyzed through their annual reports and their websites.

3.2 Sample Selection

The purpose of the study is descriptive and explanatory, as it utilizes descriptions related to corporate governance, as well as that it establishes casual relationships between variables, as a questionnaire has been formed to examine the disclosures by Commercial Bank Sector of Bahrain. The deductive approach is applied, where using the literature is important in helping the researchers in identifying theories and ideas those will be tested using the information available. To gather the information, first of all, we did our start search from Bahrain Bourse's website. The list of all the listed companies was available there. From these 48 companies, which are divided into 9 different sectors, it can be seen that there are 7 companies in the Commercial Banks Sector, 12 in the Investment Sector, 5 in the Insurance Sector, 9 in the Services Sector, 3 in the Industrial Sector, 5 in the Hotels and Tourisms Sector, 4 in the Non Bahraini Companies, 1 in the Preferred Shares and finally 2 in the Closed Companies Sector. We decided to focus on the Commercial Banking Sector, as according to Global Investment House KSCC (2007) report, "this sector is a mature and well regulated sector in Bahrain" and contributed significantly in GDP of this country. It is believed to be a promising sector and has remained to be a keystone for expansion of the domestic economy being one of the highest contributor's to the country's GDP after the Oil and Gas Sector. When we started our research before one year, there were 50 companies listed on BHB, instead of 48, in which eight commercial banks were listed. Bahraini Saudi Bank (BSB) merged with Al Salam Bank (ASBB) in April 25, 2012 which reduced listed banking sector companies to 7.

3.3 Questionnaire

We designed a questionnaire after reading numerous articles, books, various codes of countries (including Bahrain) and discussion with industry people, academics, policy makers, researchers and others. Never the less, the literature review has been used as a guide for the researchers in constructing the questionnaire and reinforcing the concepts. After writing the final draft of the questions, the researchers showed the questionnaire to some senior management and directors in some of the Bahraini's well known commercial and investment banks to receive their comments. The researchers finally, took their advices into account, tried to benefit from them and made the required possible changes. Then, we used documentation analysis from annual reports and minutes of the meetings of the entire currently Listed Commercial Banks Sector; to test and examine their disclosure practices.

The final questionnaire as shown in the next section is divided into 8 parts. Part 1 covers corporate governance practices in general and included whether the company has a website, whistleblower policy, corporate secretary, stock options and performance incentives for directors and so on. Part 2 mainly contains Board of Directors' (BODs) questions such as; whether the company has a board charter, the number of executives and non executive directors and their meetings. Part 3 included questions about the Audit Committee and its members, where part 4, 5, 6 checks whether the company has a nominating, remuneration and corporate governance committee respectively or not and related questions. The 7 part is for the risk policy/management Committee and the last part 8 is concerning with the ninth principle of the CCG which is for the responsibility of the Islamic Banks only to form a Sharia Supervisory Board (SSB).

4 Findings and Analysis

In this section, we are showing findings for each question in our questionnaire given in Table 1, by focusing mainly on the years 2010 and 2011, which is relevant period before and after the introduction of Corporate Governance Code in the Kingdom of Bahrain.

Table 1: Disclosures of commercial banks, answered by using documentation analysis

Questions	**Year**	**AUB**		**ASBB**		**BisB**		**BBK**		**ITHMAAR**		**KHCB**		**NBB**		**BSB**	
Part 1: General corporate Governance Questions:		**yes**	**no**	**yes**	**no**	**yes**	**no**	**yes**	**no**	**yes**	**no**	**yes**	**no**	**yes**	**no**	**yes**	**no**
1.1) Company has a website	2010	✓		✓		✓		✓		✓		✓		✓		✓	
	2011	✓		✓		✓		✓		✓		✓		✓		✓	
1.2) The annual reports are available in company's website.	2010	✓		✓		✓		✓		✓		✓		✓		✓	
	2011	✓		✓		✓		✓		✓		✓		✓			✓
1.3) Company provides any other information for shareholders on website (Such as; dividend information, credit rating, financial highlights).	2010	✓		✓		✓		✓		✓		✓		✓		✓	
	2011	✓		✓		✓		✓		✓		✓		✓		✓	
1.4) Company has a formal code of corporate governance.	2010	✓		✓		✓		✓		✓		✓		✓		✓	
	2011	✓		✓		✓		✓		✓		✓		✓		✓	
1.5) Company disclosed corporate governance information in annual report.	2010	✓		✓		✓		✓		✓		✓		✓		✓	
	2011	✓		✓		✓		✓		✓		✓		✓			
1.6) Company has whistleblower policy in place.	2010							✓		✓							
	2011	✓		✓				✓		✓				✓			
1.7) CEO and CFO are signatory to the financial statement.	2010	✓		✓		✓		✓		✓		✓		✓		✓	
	2011	✓		✓		✓		✓		✓		✓		✓		✓	
1.8) Company	2010	✓		✓		✓		✓		✓		✓		✓		✓	

has corporate secretary and/or compliance officer.	2011	✓		✓		✓		✓		✓		✓		✓			
1.9) Company has succession plan for management.	2010					✓		✓									
	2011	✓				✓		✓				✓		✓			
1.10) Company has delegation of decision making authority through special committee.	2010	✓		✓		✓		✓		✓		✓		✓		✓	
	2011	✓		✓		✓		✓		✓		✓		✓			
1.11) The annual report discloses related party transactions and approval process for related party transactions.	2010	✓		✓		✓		✓		✓		✓		✓		✓	
	2011	✓		✓		✓		✓		✓		✓		✓		✓	
1.12) The annual report discloses the company director's position with other organizations.	2010	✓		✓		✓		✓		✓		✓		✓		✓	
	2011	✓		✓		✓		✓		✓		✓		✓			
1.13) The annual report discloses start and end date of term of each board member.	2010	✓		✓		✓		✓		✓		✓		✓		✓	
	2011	✓		✓		✓		✓		✓		✓		✓			
1.14) The annual report discloses the number of shares held by each director.	2010		✓		✓		✓	✓		✓			✓		✓	✓	
	2011	✓		✓		✓		✓		✓		✓		✓			
1.15) Company has stock options and performance linked incentives for top executives.	2010	✓		✓		✓		✓		✓		✓		✓		✓	
	2011	✓		✓		✓		✓		✓		✓		✓			
Part 2: Board of Directors Questions		**Yes**	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**
2.1) Company has a board charter.	2010	✓		✓		✓		✓		✓		✓		✓		✓	
	2011	✓		✓		✓		✓		✓		✓		✓			
2.2) Company has written roles and responsibilities for the board members.	2010	✓		✓		✓		✓		✓		✓		✓		✓	
	2011	✓		✓		✓		✓		✓		✓		✓			
2.3) Board has no more than 15 members.	2010	✓		✓		✓		✓		✓		✓		✓		✓	
	2011	✓		✓		✓		✓		✓		✓		✓			
2.4) Board meets not less than four times	2010			✓		✓		✓		✓		✓				✓	
	2011	✓		✓		✓		✓		✓		✓		✓			

a year.																	
2.5) At least half of the company's directors are non executives.	2010	✓		✓		✓		✓		✓		✓		✓		✓	
	2011	✓		✓		✓		✓		✓		✓		✓			
2.6) At least three of the non executive directors are independent.	2010	✓		✓		✓		✓		✓		✓		✓			✓
	2011	✓		✓		✓		✓		✓		✓		✓			
2.7) The chairman is an independent director.	2010		✓	✓		✓		✓			✓	✓			✓		✓
	2011		✓	✓		✓		✓			✓	✓			✓		
2.8) The chairman of the board is same as the CEO	2010		✓		✓		✓		✓		✓		✓		✓		✓
	2011		✓		✓		✓		✓		✓		✓		✓		
2.9) The chairman of the board is a company executive.	2010		✓		✓		✓		✓		✓		✓		✓		✓
	2011		✓		✓		✓		✓		✓		✓		✓		
2.10) Board regularly reviews its size and composition.	2010	✓		✓		✓		✓		✓		✓		✓		✓	
	2011	✓		✓		✓		✓		✓		✓		✓			
2.11) Directors require formal approval of the board to accept appointment with board of another company.	2010			✓				✓		✓		✓		✓		✓	
	2011	✓		✓		✓		✓		✓		✓		✓			
2.12) Company has a ceiling policy for the maximum directorships with other companies.	2010							✓									
	2011					✓		✓				✓		✓			
2.13) Company has a written procedure for the appointment of new directors.	2010		✓		✓	✓		✓		✓		✓		✓			✓
	2011	✓		✓		✓		✓		✓		✓		✓			
2.14) Company has a policy to give formal orientation to new directors.	2010		✓		✓	✓		✓		✓		✓		✓			✓
	2011	✓		✓		✓		✓		✓		✓		✓			
2.15) Board meetings are followed with independent directors' session.	2010							✓									
	2011			✓		✓		✓				✓		✓			
2.16) Company has a formal written performance appraisal policy.	2010			✓		✓				✓		✓					
	2011	✓		✓		✓		✓		✓		✓		✓			
2.17) Company has a succession plan for directors.	2010					✓		✓									
	2011	✓				✓		✓				✓		✓			
2.18) Company has a formal written policy	2010	✓		✓		✓		✓		✓		✓		✓		✓	
	2011	✓		✓		✓		✓		✓		✓		✓			

specifying the types of non audit services which are permissible to statutory auditors.																	
2.19) Board reviews the independence of each director at least annually.	2010	✓		✓		✓		✓		✓		✓		✓		✓	
	2011	✓		✓		✓		✓		✓		✓		✓			
2.20) Company has formal written conflicts of interest policy.	2010					✓		✓		✓		✓					
	2011	✓		✓		✓		✓		✓		✓		✓			
2.21) Company has policy to seek conflicts of interest information from the directors.	2010					✓		✓		✓		✓					
	2011	✓		✓		✓		✓		✓		✓		✓			
2.22) Board has a policy to take decision in the absence of a director, if he has interest.	2010					✓		✓		✓		✓					
	2011	✓		✓		✓		✓		✓		✓		✓			
Part 3: Audit Committee Questions		**Yes**	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**
3.1) Company has an Audit Committee. (If No, skip part 3).	2010	✓		✓		✓		✓		✓		✓		✓		✓	
	2011	✓		✓		✓		✓		✓		✓		✓			
3.2) Company has a formal Audit Committee Charter.	2010	✓		✓		✓		✓		✓		✓		✓		✓	
	2011	✓		✓		✓		✓		✓		✓		✓			
3.3) Audit Charter defines the roles and responsibilities, rights and obligations of the members.	2010	✓		✓		✓		✓		✓		✓		✓		✓	
	2011	✓		✓		✓		✓		✓		✓		✓			
3.4) Committee has three members or more.	2010	✓		✓		✓		✓		✓		✓				✓	
	2011	✓		✓		✓		✓		✓		✓		✓			
3.5) Majority of the committee's members is independent.	2010	✓		✓			✓	✓		✓		✓					✓
	2011	✓		✓		✓		✓		✓			✓	✓			
3.6) Audit Committee's chairman is the chairman of the board.	2010		✓		✓		✓		✓		✓		✓		✓		✓
	2011		✓		✓		✓		✓		✓		✓		✓		
3.7) Committee reviews and discusses the scope and results of auditors without the presence of executive	2010		✓	✓		✓		✓		✓		✓		✓		✓	
	2011	✓		✓		✓		✓		✓		✓		✓			

management if needed.																	
3.8) Committee met at least four times a year.	2010			✓		✓		✓			✓	✓					
	2011	✓		✓		✓		✓		✓		✓		✓			
3.9) Company has internal audit system.	2010	✓		✓		✓		✓		✓		✓		✓		✓	
	2011	✓		✓		✓		✓		✓		✓		✓		✓	
3.10) Audit Committee approves the appointment and remuneration of head of internal audit.	2010	✓		✓		✓		✓		✓		✓		✓		✓	
	2011	✓		✓		✓		✓		✓		✓		✓		✓	
3.11) Head of internal audit department reports functionally to the audit committee's chairman.	2010	✓		✓		✓		✓		✓		✓		✓		✓	
	2011	✓		✓		✓		✓		✓		✓		✓		✓	
3.12) Head of internal audit department reports administratively to the CEO.	2010	✓		✓		✓		✓		✓		✓		✓		✓	
	2011	✓		✓		✓		✓		✓		✓		✓		✓	
3.13) Committee evaluates the performance of internal audit department annually.	2010	✓		✓		✓		✓				✓		✓		✓	
	2011	✓		✓		✓		✓		✓		✓		✓		✓	
3.14) Company has a formal performance appraisal policy of Audit Committee.	2010			✓		✓								✓		✓	
	2011	✓		✓		✓		✓		✓		✓		✓			
Part 4: Nominating Committee Question		**Yes**	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**
4.1) Company has a Nomination Committee. (If No, Skip part 4)	2010		✓		✓	✓		✓		✓		✓		✓			✓
	2011	✓		✓		✓		✓		✓		✓		✓			
4.2) Committee includes only non executive directors.	2010					✓		✓				✓					
	2011	✓		✓		✓		✓		✓		✓		✓			
4.3) The majority of the members are independent.	2010					✓			✓			✓					
	2011	✓		✓		✓		✓		✓		✓		✓			
4.4) Committee met at least twice.	2010					✓		✓		✓		✓					
	2011	✓		✓		✓		✓		✓		✓			✓		
4.5) Company has a formal performance appraisal policy for nomination.	2010					✓											
	2011	✓				✓		✓		✓		✓		✓			
Part 5: Remuneration Committee		**Yes**	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**

Questions																	
5.1) Company has Remuneration Committee. (If No, skip part 5)	2010	✓		✓		✓		✓		✓		✓		✓			✓
	2011	✓		✓		✓		✓		✓		✓		✓			
5.2) Committee includes only non executive directors.	2010		✓	✓		✓		✓				✓					
	2011		✓	✓		✓		✓		✓		✓		✓			
5.3) The majority of the members are independent.	2010		✓	✓		✓			✓			✓					
	2011		✓	✓		✓		✓		✓		✓		✓			
5.4) Committee met at least twice.	2010				✓	✓		✓		✓		✓					
	2011		✓	✓		✓		✓		✓		✓			✓		
5.5) Company has a formal performance appraisal policy of remuneration committee.	2010			✓		✓											
	2011	✓		✓		✓		✓		✓		✓		✓			
Part 6: Corporate Governance Committee Questions		**Yes**	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**
6.1) Company has a Corporate Governance Committee. (If No, skip part 6)	2010		✓		✓		✓	✓			✓	✓			✓		✓
	2011		✓		✓		✓	✓		✓		✓			✓		
6.2) At least three members from the board are presenting this committee.	2010							✓				✓					
	2011							✓			✓	✓					
6.3) The majority of the members are independent.	2010							✓				✓					
	2011							✓		✓		✓					
6.4) Company has a formal performance appraisal policy of corporate governance committee.	2010																
	2011							✓		✓		✓					
Part 7: Risk Policy/ Management Committee Questions		**Yes**	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**
7.1) Company has a Risk Policy/Management Committee. (If No, skip part 7)	2010		✓		✓	✓			✓	✓		✓			✓		✓
	2011		✓		✓	✓			✓	✓		✓			✓		
7.2) Majority of the members is independent.	2010					✓				✓		✓					
	2011					✓				✓		✓					
7.3) Committee met at least four times during the year.	2010					✓				✓		✓					
	2011					✓				✓		✓					
7.4) Risk management and compliance department reports	2010					✓				✓		✓					
	2011					✓				✓		✓					

functionally to the risk policy/management committee.																	
7.5) Risk management and compliance department reports administratively to the CEO.	2010					✓				✓		✓					
	2011					✓				✓		✓					
7.6) Company has a formal performance appraisal policy of risk policy/management committee.	2010					✓											
	2011					✓						✓					
Part 8: Shari'a Supervisory Board (SSB) Questions		**Yes**	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**	**Yes**	**No**
8.1) Company has a Shari'a Supervisory Board. (If No, skip part 8)	2010		✓	✓		✓			✓	✓		✓			✓	✓	
	2011		✓	✓		✓			✓	✓		✓			✓	✓	
8.2) The group of Shari'a consists of at least three Islamic Scholars.	2010			✓		✓				✓		✓				✓	
	2011			✓		✓				✓		✓				✓	
8.3) An annual audit report is issued by the SSB confirming the Bank's compliance with sharia's rules and principles.	2010			✓		✓				✓		✓				✓	
	2011			✓		✓				✓		✓				✓	
8.4) Company has performance related remuneration to Shari'a Supervisory Board's members.	2010					✓					✓	✓					
	2011			✓		✓					✓	✓					

4.1 General - Corporate Governance

We found that every bank maintains its website and disclosed the annual reports of both years their website, except for Bahraini Saudi Bank (BSB), which was merged with AL Salam Bank (ASBB) on the 25th of April 2012, although financial statements of BSB for the year 2011 was released. In BSB case, we ignored to extract much information except clearly given information on its website and financial statements as it is merged with ASBB and we assumed that ASBB will disclose such information in future. All the banks provided other useful information for shareholders on their website, whereas in 2011 most of the banks have a shareholder's communications page and banks provide information like financial highlights, dividends information and market watch for investors on their website. All commercial banks have a formal code of corporate governance and they all disclosed corporate governance information in separate section of their 2010 and 2011 annual reports. Having a whistle blowing policy is really important as it provides adequate protection to the employees, investors and other stakeholders and the audit committee is the one who normally oversees such a policy. Generally, the listed commercial banks have this policy in place; however Bahrain Islamic Bank (BisB) and Khaleeji Commercial Bank (KHCB) didn’t disclose such information about the policy in their annual reports, nor in their website during 2010 and 2011. Ahli United (AUB) and National Bank of Bahrain (NBB) disclosed this policy in their 2011annual reports only and it seems they start to disclose this policy because of Code requirements. Ithmaar bank developed a new whistle blower policy in 2011 and disclosed in their 2011 annual report but they didn’t disclose their old policy in their 2010 annual report. The Chief Executive Officers (CEOs) and Chief Financial Officers (CFOs) of all the banks are signatory to the financial statements which is in line with Sarbanes-Oxley Act of USA and Code of Bahrain. All the banks do have a corporate secretary or compliance officer or similar officer. Regarding question number 1.9, which is related to succession plan of management, there is no clear disclosure about whether the banks have succession plan for management or not, however BisB and Bank of Bahrain and Kuwait (BBK) disclosed such information in their website, but not in their annual reports. AUB, KHCB, and NBB provided this information in 2011. All the banks have delegation of decision making authority through special committees and they disclosed related party transactions and the approval process for related party transactions. The 2010 & 2011 annual reports of the entire banks disclosed the bank director's position with other organizations and the start and end date of term of each director. In reference to question number 1.14, the 2011 annual reports of all banks disclosed the number of shares held by each director, however the 2010 annual reports of AUB, ASBB, BisB, KHCB, and NBB disclosed the number of shares, percentage of shareholding of directors and senior management but not each director separately. All the banks have employee's long term incentive plans such as employee stock options and/or employee performance share plan.

4.2 Board of Directors

We found that every bank has a board charter and written roles and responsibilities for board members from their annual reports. During 2010 and 2011, the board of any banks had no more than 11 members.

Table 2: Board size, composition, the number of Executive, Non Executive, Independent and Non Executive directors

Banks	Year	Board Composition	Executive Directors	Non Executive Directors	Independent and Non Executive Directors
AUB	2010	10	3	3	4
	2011	10	2	4	4
ASBB	2010	11	1	-	10
	2011	11	1	-	10
BisB	2010	7	-	4	3

	2011	8	-	3	5
BBK	2010	11	-	7	4
	2011	11	-	7	4
ITHMAAR	2010	9	1	4	4
	2011	9	1	3	5
KHCB	2010	9	1	4	4
	2011	10	1	5	4
NBB	2010	10	1	5	4
	2011	10	1	5	4
BSB	2010	5	2	3	-
	2011	*	*	*	*
Average	2010	9	1	4	4
	2011	9	1	3	5

(Source: Annual Reports of respective banks).
*The Annual Report of BSB for 2011 was unavailable.

From Table 2, we can notice that the average number of board size is 9 during 2010 and 2011 and banks have increased the number of independent and non executive directors in their board in 2011 as compared to the year 2010.
The number of board members increased from 7 to 8 and 9 to 10 in BisB and KHCB respectively. The board of all banks met not less than four times a year during 2010 and 2011, however AUB and NBB didn’t mention in their 2010 annual report the number of meetings held by each committee of the board.

Table 3:Number of meetings held by the board of each bank

Banks	Board Meetings During 2010 and 2011 Note: Standard No. of Meetings required each year is 4	
	2010	2011
AUB	*	4
ASBB	4	4
BisB	4	7
BBK	8	8
ITHMAAR	9	4
KHCB	7	6
NBB	*	6
BSB	4	*
Average	5	5

(Source: Annual Reports of respective banks).
* Unavailable

From Table 3, we can notice that each bank had minimum 4 meeting (mandatory limit) and maximum 9 meeting during year 2010 and 2011. However, average number of meeting was 5 in both years. BisB has 7 meetings as compared to 4 in year 2011.
Further, Comparing NBB's annual report 2010 with 2011, there is a huge difference in how the company disclosed its corporate governance and other information in the report. In fact, there is a lack of governance disclosures in NBB's 2010 annual report, as the company didn’t disclose the names of directors representing each board committee, who

is independent and who is non executive, and it didn’t even disclose the number of meetings held by each committees. At least half of all banks' directors are non executive and three of those are independent, except for BSB which reflects the independence of the board. In reference to question number 2.7, the chairman of ASBB, BisB, BBK, and KHCB is independent, in contrast to AUB, ITHMAAR, NBB, and BSB. However, all banks' have separated the role of the chairman from the CEO and all chairmen are non executive directors which are required by most of the codes in the world.

We noticed from annual reports that all the banks' board regularly reviews its size and composition, and directors require formal approval of the board to accept appointment with board of another company. There is no clear disclosure for whether banks have a ceiling policy for the maximum directorships with other companies, except for BisB, BBK, KHCB, and NBB, as these companies mentioned such a policy in their Corporate Governance Code and guidelines. Although NBB mentioned in their 2011 annual report this policy and showed it as an exception for its compliance with the requirement of the High Level Control Module, as their two board members hold more than three directorships in public companies and they are also being proposed for re-election. Regarding question 2.13 and 2.14, all the banks have written procedure for the appointment of new directors and a policy to give formal orientation to new directors, except for AUB, ASBB and BSB, as in year 2010 these three banks didn’t have a nomination committee. However, AUB and ASBB formed their nomination committee in 2011. There is no clear disclosure for whether the board meetings are followed with independent directors' session or not in their annual reports, however in 2011 annual report, most of banks' corporate governance guidelines mentioned this point. From annual report 2011, we noted that all the banks have written performance appraisal policy, contrary to 2010. All the banks have a formal written policy specifying the types of non audit services which are permissible to statutory auditors and board's of banks reviews the independence of each director, at least annually. All the banks have formal written conflicts of interest policy; however, there is no clear disclosure for all banks in 2010 annual report.

4.3 Audit Committee

We find that every bank has audit committee with formal audit charter that defines the roles and responsibilities, rights and obligations. The audit committee of all the banks has three members or more and the majority of them are independent, except in 2010, BisB and BSB had 1 independent member out of total 3 members. KHCB had the majority of independent members in 2010; however in 2011 one independent member out of total three was member of the audit committee. As mentioned earlier, NBB didn’t disclose in its 2010 annual report the names of directors in each committee and the number of meetings held. The chairman of audit committee is not the same as the chairman of the board in all the banks and they all have a formal system that approves the appointment and remuneration of head of internal audit department. The head of internal audit reports functionally to the audit committee's chairman and administratively to the CEO. The audit committee of all the banks met at least four times during 2010 and 2011, except ITHMAAR, as the committee met only 3 times during 2010.

4.4 Nomination Committee

The researchers find that every bank has a nomination and remuneration committee in 2011. However, during 2010 AUB, ASBB didn't have a nominating committee and neither BSB has a nominating, or a remuneration committee. The nomination committee of all the banks included only non executive directors, in which the majority is independent in 2010 and 2011, except in 2010, BBK had only one independent director representing the nomination and remuneration committee out of total four members. The nomination committee of all the banks met at least twice during 2010 and 2011, except for NBB, as the nomination and remuneration committee met only once during 2011.

4.5 Remuneration Committee

The Remuneration Committee of all the banks includes only non executive directors in 2010 and 2011, except AUB as there is one executive member representing the committee out of total three in both years. The majority of the members were independent, except AUB as one independent member represented the committee in 2010 and 2011 and in 2010 as mentioned earlier BBK had one independent member only. The committee of all banks met at least twice in 2010, except ASBB as the committee met only once in 2010 and in 2011, AUB and NBB's remuneration committee met only once, instead of twice as compared to year 2010.

4.6 Corporate Governance Committee

Only two banks BBK and KHCB, out of total eight, had a Corporate Governance Committee in year 2010 and 2011; however, ITHMAAR also formed Corporate Governance Committee in 2011. In BBK and KHCB at least three members from the board represented this committee in 2010 and 2011. However, at the end of 2011 and as ITHMAAR established it's (CG) Committee on the 4th December 2011 it had two independent directors and a member of Shari'a Supervisory Board, so only two board members out of total three representing this committee. The majority of KHCB, BBK and ITHMAAR's members in this committee were independent and the banks had a formal performance appraisal policy for this committee.

It is noticed that AUB didn't have this committee, however, it has an Audit and Compliance Committee and one of its responsibilities is to develop and review the effectiveness of the Corporate Governance framework and liaison with the bank's external auditors and regulators.

4.7 Risk Policy/Management Committee

Regarding the Risk Policy/Management Committee's questions, only three banks had such a committee in 2010 and 2011 which are BisB, ITHMAAR, and KHCB. We can notice that all the three banks are Islamic Banks, the majority of the members are independent and the committee met at least four times during 2010 and 2011. The risk management and compliance department reports functionally to this committee and administratively to the CEO.

4.8 Sharia Supervisory Board (SSB)

Forming a SSB is the responsibility of Islamic Banks only, as the most noticeable purpose behind that is to legitimately state for participating Muslim customers that the financially offered product or service is acceptable from an Islamic Lawful perspective. All the Islamic banks in Bahrain such as ASBB, BisB, ITHMAAR, KHCB and BSB have a SBB Committee that consists of at least there Islamic Scholars in 2010 and 2011. An annual audit report has been issued by the SSB Committee confirming the Bank's compliance with Sharia rules and principles. In 2010 and 2011, the Islamic Banks had performance related remuneration to all Sharia Supervisory Board's members, however ITHMAAR didn't pay performance related remuneration to SSB members.

5 Conclusion

The research paper aimed at determining the coverage of Corporate Governance practices and testing the quality of corporate governance disclosures by all listed commercial banks in BHB. Banks are required to comply with the High Level Controls Module of CBB Rulebook which became effective from the 1st of Jan 2011 with full compliance mandated by the financial year end 2011. The HC Module contains both rules and guidance; where rules must be complied with, but guidance may either be or not be explained by way of an annual report to the shareholders and to the CBB.

It can be concluded that all the listed commercial banks discloseed fairly good coverage of corporate governance practices. Examining the 2011 banks' annual reports and comparing it with 2010's, there are lots of effective and positive changes in Corporate Governance reporting in response of the introduction of code. The introduction of code increased the level of disclosures and transparency without any exception. After the code became effective, all the banks disclosed the number of shares held by each director, AUB disclosed the number of meetings held by each committee, in addition to other useful information, which promote the transparency and fairness. NBB's annual report became very revealing; AUB and ASBB established their nomination committee and ITHMAAR formed their Corporate Governance Committee.

It is the fact that AUB, ITHMAAR, NBB, and SBS's chairmen of the board are still non independent director, however, since the code is issued on a *Comply or Explain principle,* the banks with non independent chairman like AUB and NBB are of the opinion that this does not impact the effectiveness and efficiency of the board of directors, as the directors concerned provide adequate attention to their responsibilities as directors of the bank, and there are no conflicts of interest between their other directorships and that of the bank. Finally, the introduction of code brings more disclosures and reporting on governance issues in listed banks and licensees of CBB.

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