Corporate governance disclosure compliance: a comparison between conventional and Islamic banks

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Abstract: The paper examines the extent and trend of corporate governance (CG) disclosure compliance by listed conventional and Islamic banks in Qatar, the UAE and KSA. The study found that conventional banks had more compliance compared to Islamic banks. The extent of the disclosure has increased for the sample period overall. The findings are considered interesting for many stakeholders (e.g., banks' management, shareholders, investors, relevant authorities) in the GCC countries. It helps the banks to better understand their current compliance of CG disclosure practices and identify the current challenges, hence, reduce the gap of none-compliance. Moreover, the findings are essential for the authorities to identify the strength and weakness of compliance with the CG code, thereby providing a platform to make the necessary actions to improve it. Furthermore, the findings are beneficial for the shareholders and investors to understand current CG disclosure, thus, they may better evaluate their performance and governance for decision making.

Keywords: corporate governance; code; conventional banks; Islamic banks; compliance; Qatar; Saudi Arabia; UAE.

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1 Introduction

A good economy is supported by a well-regulated financial system, which includes banks and other financial services providers. Many of the developed countries try to boost their economies with efficient financial services regulated by different authorities for their sound functioning (Sooloo, 2014). In the past few years, Islamic banks (IBs) in the Gulf Cooperation Council (GCC) countries have had stable and steady growth. Their predicted growth in the region is predicted to outperform that of conventional banks (CBs). It is also claimed that the environment in which the IBs operate in the region is very supportive (John, 2013). During the 2009 financial crisis, a major weakness was in the accounting and corporate governance (CG) standards of the banks that lent without proper tracking of the customers. Compliance with the existing standards proved to be insufficient to regulate these banks. The executive and remuneration committees of these banks were also a reason for concern during the crisis period (Kirkpatrick, 2009). "The financial crisis can be to an important extent attributed to failures and weaknesses in corporate governance arrangements" [Kirkpatrick, (2009), p.2]. In light of recent events, and considering the importance of CG, it can be said that CG is a means to control an organisation through guidelines to stabilise the benefits of different stakeholders in the organisation (Investopedia, 2014).

The banks in Qatar have been performing and are predicted to perform better than their gulf counterparts with the backing of huge investment and infrastructure projects. With the support of strong asset and loan growth of 24% and 23% respectively, the banking system in Qatar is set to increase Qatar's gross domestic product in the coming years (Gulf Times, 2014). The CG code was first issued in Qatar by the 'Qatar Financial Markets Authority' (QFMA, 2009) in January 2009 for the companies listed in the Qatari Stock Exchange and has been maintained since while in the United Arab Emirates (UAE) was issued in 2009. For the Kingdom of Saudi Arabia (KSA), the initial code was published in 2006, and a revised version was issued in 2010 (considered in this study). The Qatari CG code is considered among the good international CG standards thereby constituting a vital document for the banks and listed companies in Qatar to follow and abide by Sharar (2011). The paper aims to examine the extent and trend of compliance of the CG disclosure by the listed conventional and IB in Qatar, the UAE and KSA for the period 2010 to 2012. This study is considered to be among the pioneer studies that examine the compliance of CG disclosure and compare it between CB and IB. The findings benefit banks, stakeholders and the relevant authorities in the GCC. It helps conventional and IB better understand their current compliance of CG disclosure practices so that they could be able to identify the current challenges, hence reduce the gap of none-compliance. Also, the findings are useful for the authorities in Qatar to identify the strength and weakness of compliance with the CG code, thereby providing a platform to make the necessary actions to improve it. Moreover, the findings are considered beneficial for the other stakeholders (e.g., shareholders, investors) to understand current CG practices by conventional and IB in Qatar. Thus, they may better evaluate the performance and governance for the purpose of decision making.

2 Literature review

Sharar (2011, p.1) researched the reasons why Qatar needs a CG code stating that "…the importance of having a well-structured and mandated corporate governance framework to provide a platform for market integrity and efficiency as well as to facilitate economic growth…." The Qatari CG code adapts the OECDs basic principles to suit Qatari legislations and culture (Sharar, 2011). Spira and Bender (2005) argued that, "the establishment of board sub-committees has been strongly recommended as a suitable mechanism for improving corporate governance." They proposed the idea that the board of directors (BoD) should delegate some responsibilities to other groups in the company in order to enhance the performance of the non-executive directors (NEDs) on the board. This notion was recommended due to the increasing role and importance of NEDs on the board and for the benefit of the firm as a whole.

Even with increased discussions on the importance of CG for the financial institutions, the debate on how good the variables are in recognising the CG indicators remains limited (Abd Majid et al., 2011). Some studies developed a combination of CG standards which include the standards published by the central bank of that country with that of the AAOIFI to produce a more comprehensive list of variables for Islamic financial institutions (IFI) to form the 'best practice' in regards to the disclosure of CG for the shari'ah-based institutions (Abd Majid et al., 2011). Patel et al. (2002) discussed transparency and disclosure (T&D) in detail and deemed them to be components essential to CG. They analysed approximately 350 firms from over 15 emerging countries over three years until the year 2000. They found that the Asian markets are better in T&D in comparison to South American and Middle East markets. Hence, the better the T&D scores, the better CG the markets are expected to have. A study conducted by Habbash (2016) examined the CSR of non-financial firms in Saudi Arabia for four years from 2007. The author found a higher average disclosure for CSR at 24% than other studies while citing the application of CG code in Saudi Arabia during this period as a potential reason for this increase of around 9%. While firms with more government and family-based ownership, maturity and size were positively related to the CSR disclosure, while leveraging a negative relationship. These results can be compared with those of the financial firms CG performance in this study.

Boubakri et al. (2005, p.767) studied approximately 230 firms from semi-industrialised nations and concluded, "…that the changes in performance vary with the extent of macro-economic reforms and environment, and the effectiveness of corporate governance…." They found that due to improved CG, the company's investment, efficiency, return as profit and output significantly increased. The study also found that countries with better rights offered via CG had better efficiency compared to countries which were less developed in terms of stock exchange development. Safieddine (2009) focus on the "trade-offs between shari'ah compliance and mechanisms protecting investors' rights", found that there are some flaws in CG, internal control, and audit, in addition to the transparency of IBs. The author suggested that the IBs along with the respective authorities that govern the IBs should focus and develop their CG system. He concluded that the 'investment account holders' in the IBs are not adequately represented in the BoD, thereby hindering their right to monitor and control the activities.

Abu-Tapanjeh (2009) stated that there is increased recognition of the importance to develop the CG principles for Islamic institutions, with the basis and focal point of Islamic economy being fair, just, and honest, in addition to the safeguarding of the rights of all the parties involved in the economy. He compared the CG principles from the Islamic perspective with that of the conventional OECD model. The author concluded that the OECD is more focused on specific issues within the six criteria framework, whereas the Islamic dimensions of CG are much broader, and that not all the actions can be placed under the shari'ah jurisdiction. Lewis (2005) mentioned that the CG is concerned with the firm and its constituents, which may include the investors and shareholders. This, he argues is the conventional model of CG. In contrast, the Islamic CG model is broader and extends the responsibilities to the stakeholders of the firm, which include the investors, customers, employees, government, suppliers, and the community as a whole. Although the vision of the Islamic CG and ethical dimension is clear, the execution of such a model will encounter many challenges.

In a recent report, the former CEO of Qatar Exchange, Andre Went mentioned that "…it (CG) adds value to have a more public review… to see where the companies are in terms of implementing corporate governance" [QFC and Reuters, (2010), p.14]. The idea of CG implementation has to be taken into serious consideration, as Qatari banks and firms are becoming more globally competitive, the international norms and adherence to specific rules and regulations should be followed strictly in order to maintain a proper balance of profit and T&D (QFC and Reuters, 2010). El-Halaby and Hussainey (2016) studied the compliance of IB with AAOIFI standards. The sample from eight countries consisted of 43 IBs, were the effect on the compliance was examined three variables – bank characteristics, CG mechanisms relating to shari'ah board and BoD. They found that the compliance level with AAOIFI is mainly affected by the shari'ah supervisory board (SSB), particularly the age, size, CG and 'shari'ah-audit' of the board. The compliance of financial statements had the highest score of around 70% while CSR had a low of approximately 27%. This shows the importance of the standards in influencing the firm, in particular for IBs, as they have to be more society oriented.

Mohamed (2016) examined the differences between the two types of banks, Islamic and Conventional, in terms of CG while highlighting its importance mentioning that it is a "guarantee fairness and accountability of the global financial system." The study finds that there are certain noteworthy differences between both the systems in terms of governance concerning transparency, disclosure and audit of the supervisory board. As highlighted in the introduction, banks are a vital source for the development of an economy. However, Mohamed (2016) mentions that if the regulatory system is not efficient, then the system may become a 'distractive institution' rather than a developmental banking system that assists in the construction if the world economy. John et al. (2016) mention that both banks and regulators consider good enactment in CG an important concern. Emphasising on its importance, many listed and some non-listed firms around the world pushed for CG application and even formulated specialised codes to highlight its importance. Many countries followed the guidelines that were published by the Basel Committee that oversights the banking supervision, this further pushed the already existing governance guidelines specific to the banking sector to improve.

3 Research method

The research is based on information gathered from the annual and CG reports (if available) of the CBs and IBs in Qatar, UAE and KSA. The sample is selected from the Qatar Exchange (Qatar), Dubai Financial Markets (UAE) and Tadawul (KSA) websites under the listed securities in the banking sector. The main factor that differentiates between conventional or IB is the presence of a SSB, the offering of shari'ah viable products/services, and the company system being shari'ah-based. Even though some of the CB in 2010 and 2011 had a shari'ah banking window functioning as a part of the bank and an SSB, they will still be considered a CB due to the fact that their primary business is conventional-based and not shari'ah-based. The criteria for any bank to be included in the sample of the study should be the availability of the annual report, for the three years, 2011, 2012 and 2013, thus enabling the researcher to study disclosure trends for the particular bank. The financial institutions are divided into conventional and Islamic. In case the bank has only one annual report, it will be disqualified from the sample. This paper focuses on the CG disclosure in the Qatar banking sector, which requires an analysis of the annual reports and not financial statements. The annual/CG reports are downloaded from the Qatar Exchange website, in case the file is not available, the banks' primary website is used.

The research employs the disclosure index as a tool to study the CG compliance of the Qatari banks according to Qatari code of CG (Appendix 1), UAE banks according to UAE code of CG (Appendix 2) and KSA banks according to KSA code of CG (Appendix 3). Marston and Shrives (1991) describe the disclosure index method of analysing company annual reports as a means to provide us with the degree of disclosure rather than its quality. It may not mean that the items in the CG charters are implemented with complete respect to the charter, but their mention in the report suggests that they are aware of the articles, its application and consequences. This research uses the unweight disclosure index method, and will not give any one or set of variables an advantage over the other. This means that all the variables are equally weighted for the final score. Moreover, it is also argued that the disclosure index method for measuring CG is relevant, as mentioned, "…more importantly, the need to measure the quality of corporate governance (CG) using a disclosure index is undeniably pertinent…"

(Abd Majid et al., 2011). For every CG variable that is found and present in the annual/CG report, it will be given a score of '1', in case the CG variable is not present, it will be given a score of '0'. For each bank in every year, the score will be added and divided by the number of CG variables required in that specific code which adds up to 28 variables (i.e., items) in Qatari CG code, 14 variables in UAE CG code and 17 variables in KSA CG code. A percentage weight on the total number was calculated in order to find the amount of disclosure information provided by the banks. Currently, there are eight banks listed in the Qatar Exchange: four conventional and three Islamic, UAE: seven conventional and two Islamic, and lastly, for KSA: nine conventional and three Islamic (Appendix 4). All the banks included in the study have made available their annual reports for the three years, which means no bank will be removed.

In addition to using the disclosure index scoring method, the research also applies the descriptive statistics method of maximum, minimum, and average for the results found for each variable, bank, and bank type for both all the sample firms and also an additional test of only available data for descriptive analysis will be considered. This will assist in filtering the results for a better understanding of the data gathered from the annual/CG reports. Further analysis is performed in the form of figures and tables to provide a graphical view of the results implicated for the above mentioned measurement variables, giving an enhanced comparative analysis to the study.

4 Findings

The findings of this study are based on the information provided by the banks in their annual and CG reports. Hence, the responsibilities of the application of the variables that have been scored '1' are on the individual firm. The Qatari banks initiated the publishing of a separate CG report from the following year of CG codes in 2009. In the initial analysis of the CG compliance in the Qatari, UAE (Dubai) and KSA listed banks, only years 2010, 2011 and 2012 reports and related Qatari, UAE and KSA CG code was used to score the disclosure index. Tables 1 and 2 provide a descriptive analysis for the three countries and three years for the full sample and available sample data, respectively. Tables 1 and 2 describe the total average of both conventional and IB, in addition to the average, maximum, difference between the average of CBs and IBs and the number of banks for each category in each year and sample.

For the Qatari sample, the average DI score in the full sample version (eight CBs and three IBs) for CB is consistently more than IB for each of the three years with a high of 92.14% in 2012, while IBs had a high score of 85.71% in 2011. The maximum difference between the two categories was found in 2012 with 62.38% in favour of CBs. The UAE (Dubai) full sample (seven CBs and two IBs) on average had the lowest overall disclosure score among the three countries. The highest average score for CBs was 38.78% and 35.71% for IBs both occurring in 2011. However, it was found that the overall scoring for both the bank types was similar and the maximum difference was 14.29% in 2010. KSA full sample had nine CBs and three IBs, and had a different scoring outcome than the other two samples. It was found that the IBs in each year had significantly higher DI score than the CBs while the overall IBs percentage of the three years was around 57% while for CBs it was approximately 35%. The highest per year average score for full sample for both categories of CBs and IBs was in 2011 for Qatar with 87.05%, and the lowest was for UAE in 2010 with 25.40%.

Table 1 Descriptive analysis of full sample

Countries	*% total average*	*% max. conventional*	*% average conventional*	*% maximum Islamic*	*% average Islamic*	*% average difference (C − I)*	*Total banks*	*Conventional*	*Islamic*
Qatar (28 CG variables)									
2010	60.27	89.29	79.29	57.14	28.57	50.71	8	5	3
2011	87.05	96.43	87.86	89.29	85.71	2.14	8	5	3
2012	68.75	100.00	92.14	89.29	29.76	62.38	8	5	3
UAE (14 CG variables)									
2010	25.40	71.43	28.57	28.57	14.29	14.29	9	7	2
2011	38.10	71.43	38.78	42.86	35.71	3.06	9	7	2
2012	34.92	71.43	35.71	42.86	32.14	3.57	9	7	2
KSA (17 CG variables)									
2010	36.27	70.59	32.68	76.47	47.06	−14.38	12	9	3
2011	42.65	76.47	35.95	70.59	62.75	−26.80	12	9	3
2012	45.10	94.12	38.56	76.47	64.71	−26.14	12	9	3

Table 2 Descriptive analysis of available sample

Countries	*% total average*	*% max. conventional*	*% Average conventional*	*% maximum Islamic*	*% average Islamic*	*% average difference (C – I)*	*Total banks*	*Conventional*	*Islamic*
Qatar (28 CG variables)									
2010	68.88	89.29	79.29	57.14	42.86	36.43	7	5	2
2011	87.05	96.43	87.86	89.29	85.71	2.14	8	5	3
2012	91.67	100.00	92.14	89.29	89.29	2.86	6	5	1
UAE (14 CG variables)									
2010	58.57	71.43	66.07	28.57	28.57	37.50	5	4	1
2011	48.98	71.43	60.71	28.57	28.57	32.14	7	5	2
2012	52.38	71.43	62.50	42.86	32.14	30.36	6	4	2
KSA (17 CG variables)									
2010	62.18	70.59	58.82	76.47	70.59	–11.76	7	5	2
2011	63.97	76.47	64.71	70.59	62.75	1.96	8	5	3
2012	67.65	94.12	69.41	76.47	64.71	4.71	8	5	3

Figure 1 Average disclosure index score – Qatar (full sample)

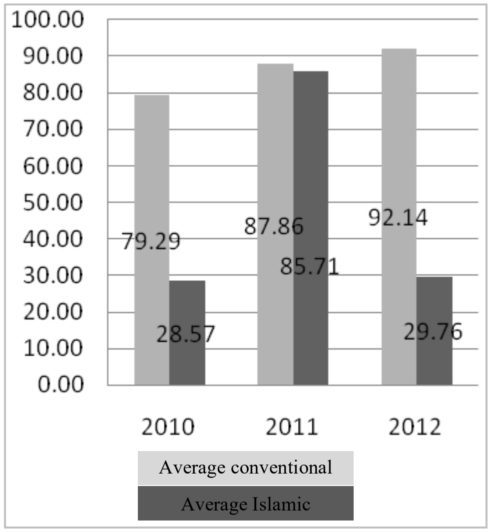
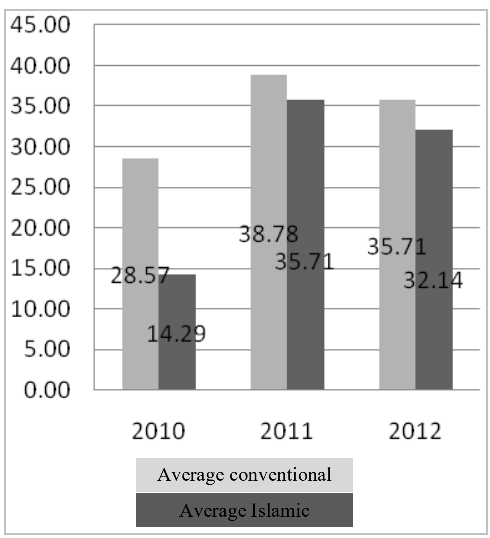
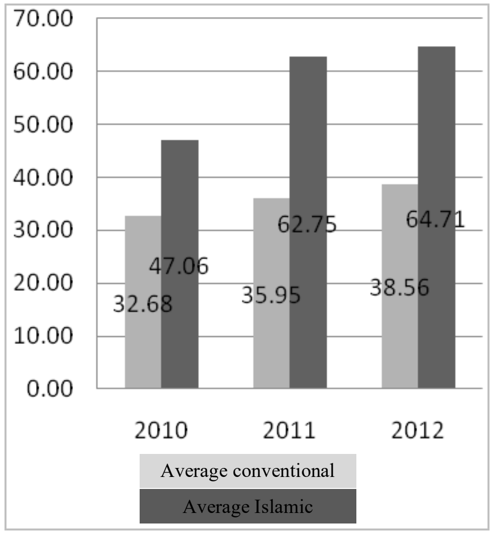


Figure 2 Average disclosure index score – UAE (full sample)



The results for the available data only category have different outcomes, as each year for each country has a different sample size than the full sample. As predicted, the average for total, CBs and IBs have risen significantly for Qatar, as the highest DI score for CBs was 92% and for IBs it was 89%, and the overall highest average was 91% in 2012, while the average difference between the two samples reduced to 36%. The UAE sample for CBs had a significant rise as well, as the average highest score rose to 66% while the IBs remained the same at 32% in 2012. However, the difference between the two categories was of around 22% on the higher side for the latter category of available data. The KSA available data category overall and CBs average results had an outcome on the higher end, with the total average increasing to 67% and highest CBs average reaching to 69%, while the DI score for IBs did not change. The difference between average CBs and IBs was the highest at 11% in 2010 for IBs.

Figure 3 Average disclosure index score – KSA (full sample)



For Qatar sample under both categories, in 2010, the article 'other board practices and duties' had '0' scores, while it was disclosed in the subsequent years. As for the UAE sample, the two articles 'administrative penalties' and 'enforcement of resolution' were not found in any of the three years for any of banks. For KSA sample, in 2010, four articles were not available in the annual reports; however, in all three years, only one article – 'shareholders right concerning dividend distribution' was not found. The overall highest average score for all the countries across all years and both the categories was found in Qatar in 2012 for the available data sample category, while the lowest overall score was found in the UAE full sample in 2010.

Figure 4 Average disclosure index score (available sample vs. full sample)

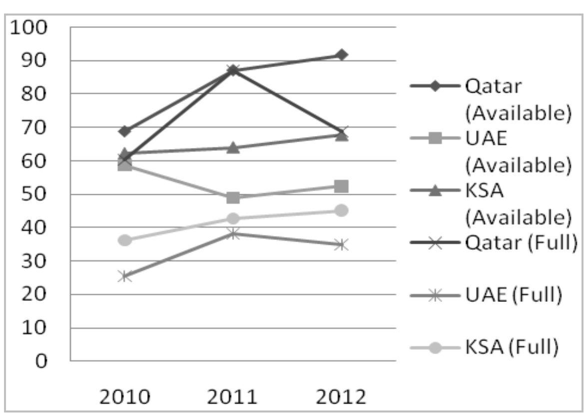


Figure 5 Average disclosure index score – conventional banks (available sample)

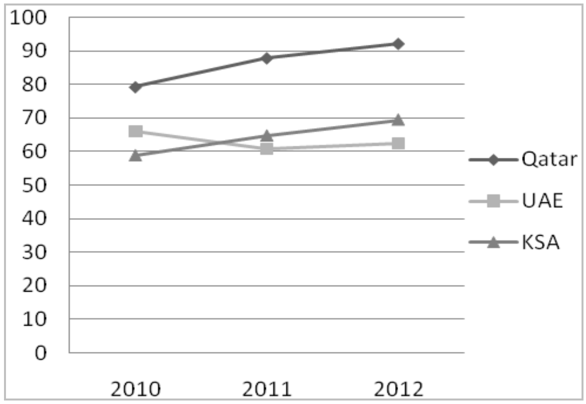
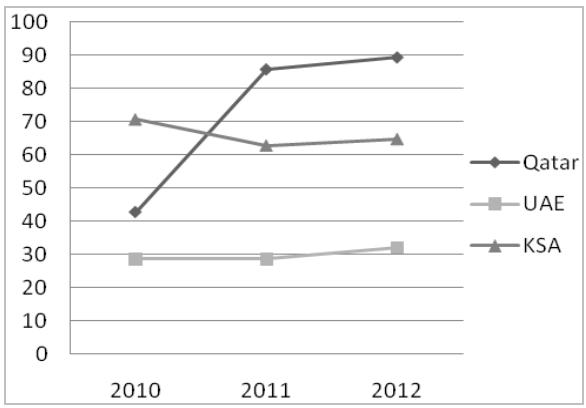


Figure 6 Average disclosure index score – Islamic banks (available sample)



5 Conclusions

It is evident from the literature review that by abiding and disclosing CG, companies provide a better view of the firm to its shareholders and stakeholders. This, in turn, increases the credibility and value of the annual report, as the increased disclosure helps with better communication with the intended parties. CG in recent times has become vital for firms, as Doha Bank CEO, Mr. R. Seetharaman, rightly said, "Governance is truly about reflecting all the stakeholders' integrated value" [QFC and Reuters, (2010), p.3]. The extent of the disclosure has also increased in the banks for the sample period overall. The CBs had a better DI score over the two categories for both Qatar and the UAE, while the KSA samples of IBs had a better overall score.

Further research can be conducted to determine the extent to which the IBs have applied the AAOIFI CG code. Although an improvement has been found in CG among the banks, knowing how it affected their performance, profitability, market price, etc., and overall perception of shareholders and stakeholders will provide valuable insights as to whether CG really has an effect on the banks' financial performance or is it just a regulation to be followed for showcasing purposes. Nevertheless, there should exist a positive relationship between the financial performance and the CG disclosure of the banks. However, it could be possible that the GCC may be an exceptional case.

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Appendix 1

Qatari corporate governance code (28 variables)

Section	*Article*	*Abb.*	*Detail*
II	3	CCGP	Company's obligation to comply with corporate governance principles
III	4	BC	Board charter
	5	BMR	Board mission and responsibility
	6	BMFD	Board members 'fiduciary duties'
	7	SCHB	Separation of positions of chairman and CEO
	8	DCHB	Duties of the chairman of the board
	9	Bcomp	Board composition
	10	NEBM	Non-executive board members
	11	BM	Board meetings
	12	BS	Board secretary
	13	CoIIT	Conflict of interests and insiders 'trading'
	14	OBPD	Other board practices and duties
	15	BMANC	Board members appointment, the nomination committee
	16	BMRRC	Board members 'remuneration', remuneration committee
	17	AC	Audit committee
IV	18	CICIA	Compliance, internal controls and the internal auditor
V	19	EA	External auditor
VI	20	CGR	The corporate governance regulations by company BoD
VII	21	GRS	General rights of shareholders and key ownership
	22	OR	Ownership records
	23	AtI	Access to information
	24	SRSM	Shareholders' rights with regard to shareholders meetings
	25	ETSVR	Equitable treatment of shareholders and exercise of voting rights
	26	SRBME	Shareholders' rights concerning board members election
	27	SRDD	Shareholders' rights concerning dividend distribution
	28	CSSRMT	Capital structures, shareholders rights, major transactions
VIII	29	STR	Stakeholders rights
IX	30	CGR2	The corporate governance report

Source: Corporate Governance Code for Companies Listed in Markets Regulated by the Qatar Financial Markets Authority issued in 2009

Appendix 2

UAE corporate governance code (14 variables)

Article	*Abb.*	*Detail*
3	CCGP	Company's obligation to comply with corporate governance principles
4	DCHB	Duties of the chairman of the board
5	BMFD	Board members 'fiduciary duties'
6	BCOM	Board committees
7	BREM	Board remuneration
8	CICIA	Compliance, internal controls and the internal auditor
9	AC	Audit committee
10	EA	External auditor
11	DMGMT	Delegation of management
12	SR	Shareholders rights
13	CoC	Code of conduct
14	CGR2	The corporate governance report
15	ADPen	Administrative penalties
16	ENRe	Enforcement of resolution

Source: Ministerial Resolution No. (518) of 2009 Concerning Governance Rules and Corporate Discipline Standards in the United Arab Emiratis

Appendix 3

KSA corporate governance code (17 variables)

Section	*Article*	*Abb.*	*Detail*
II	3	SR	Shareholders rights
	4	AtI	Access to information
	5	SRSM	Shareholders' rights with regard to shareholders' meetings
	6	ETSVR	Equitable treatment of shareholders and exercise of voting rights
	7	SRDD	Shareholders' rights concerning dividend distribution
III	8	Disc	Policies and procedures related to disclosure
	9	DiscBR	Disclosure in BoD report
IV	10	BoDF	BoD functions
	11	BMFD	Board members' fiduciary duties
	12	BoDForm	BoD formation
	13	BCOM	Board committees
	14	AC	Audit committee
	15	NRC	Board members appointment, the nomination committee and remuneration committee
	16	BM	Board meetings
	17	BREM	Board remuneration
	18	CoI	Conflict of interests
V	19	CCGP	Company's obligation to comply with corporate governance principles

Source: Corporate Governance Regulations in the Kingdom of Saudi Arabia (amended in 2010)

Appendix 4

Banks included in the study

No.	*Name of bank – Qatar*	*Type*
1	Al Ahli Bank	Conventional
2	Al Khaliji Commercial Bank	Conventional
3	Commercial Bank of Qatar	Conventional
4	Doha Bank	Conventional
5	Masraf al Rayan	Islamic
6	Qatar Islamic Bank	Islamic
7	Qatar International Islamic	Islamic
8	Qatar National Bank	Conventional

Source: Qatar Exchange website (http://www.qe.com.qa)

No.	*Name of bank – UAE*	*Type*
1	Ajman Bank	Conventional
2	Al Salam Sudan Bank	Conventional
3	Commercial Bank of Dubai	Conventional
4	Dubai Islamic Bank	Islamic
5	Emirates Islamic Bank	Islamic
6	Emirates Investment Bank	Conventional
7	Emirates NBD	Conventional
8	Mashreq Bank	Conventional
9	Al Salam Bank Bahrain	Conventional

Source: Dubai Securities Market (http://www.dfm.ae)

No.	*Name of bank – KSA*	*Type*
1	Al Rajhi Bank	Islamic
2	Arab National Bank	Conventional
3	Bank Al Bilad	Conventional
4	Bank Al Jazira	Islamic
5	Banque Saudi Fransi	Conventional
6	Inmaa Bank	Conventional
7	NCB Ahli	Islamic
8	Riyad Bank	Conventional
9	SABB HSBC	Conventional
10	SAMBA	Conventional
11	Saudi Hollandi	Conventional
12	Saudi Investment Bank	Conventional

Source: Tadawul Saudi (https://www.tadawul.com.sa)