



CORPORATE GOVERNANCE SURVEY

Special Report

JCR-VIS had launched its methodology for corporate governance ratings in June 2002 and subsequently announced our first such rating in January 2003. At the time we were among the first few rating agencies in the world to have developed the capability to offer such a service.

Since then we have gone on to complete eight corporate governance rating assignments, the results of six of which were made public.

However, since the number of assignments mentioned above, although representing a better trend than we expected at the time of commencement of such ratings, it no way can be considered a representative sample of corporate governance practices in the country. In order to better gauge the level of corporate governance practices in the country JCR-VIS carried out a survey based on the annual reports of the top 50 turnover companies on the Karachi Stock Exchange (exclud-

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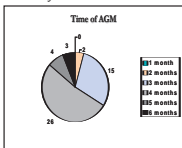
Financial Disclosure

It was observed that a significant 52% of the companies surveyed held their Annual General Meetings near to the expiry of the 4 month period permitted by the regulations, while in seven cases even this deadline was breached. Therefore, nearly two-thirds of the companies surveyed were holding their AGMs as late as possible. Such a finding can have two implications. First, the management considers the holding of the AGM more of a formality than an important service to the shareholders. The other implication could be a lack of proper financial reporting systems that are delaying the preparation of the annual accounts. Both situations, when considering the basis of our sample selection, are not in line with good governance practices. Also, although the regulators do have the discretion to relax the

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four month deadline on the request of the company, we believe that the reasons for such a delay should form part of the notice of the meeting so that the shareholders also have an understanding of the reasons behind the delay.



One area in which the survey showed a satisfactory result was the location of holding of Annual General Meetings, with only one instance where the AGM was not held in a major urban center.

External Audit

External audit is one of the areas of most attention since high profile cases like Enron, Worldcom and more recently Fannie Mae in the USA have brought the

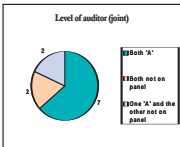
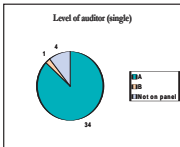
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accounting profession under significant scrutiny. In Pakistan, only the State Bank of Pakistan maintains a panel of auditors, broken up into three categories A, B & C, to determine whether an audit firm is eligible to carry out the external audit of a given bank. However, in the case of the non-bank companies the audit firm is only

required to have a satisfactory rating from the quality control panel of the Institute of Chartered Accountants of Pakistan, with no differentiation with respect to quality.

Therefore, we used the SBP panel as a guide to the quality of external auditors appointed by the sample company. The results here indicated that most management's are conscious about this aspect as it helps give credibility to the financial statements. Of the surveyed companies, 11 have had joint auditors, while only in six cases (including two joint audits) were the auditors not on the SBP panel. On the other hand, 84% of the companies had appointed auditors from the A category of the SBP panel.

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Only three of the audit reports had qualifications, while twelve included paragraphs of emphasis.

Executive Management

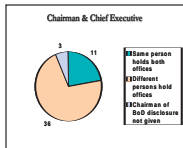
It is a common perception that most companies in Pakistan do not rely on professional management, with the sponsor families

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being the main strategic and executive decision making power in most cases, despite the public listed nature of the

company. Our survey found that a substantial 64% of the companies included in our selection did not even list the management team of the company, thus indicating the value that is placed on the professional management by the actual decision makers.

On the other hand our survey indicated a strong degree of separation of the offices of Chairman



and the Chief Executive among the sample companies (72%). Among the balance companies, we could not determine whether separation existed in three of the companies as the name of the Chairman was not disclosed. This highlights an anomaly in our regulatory framework, whereby it is

not necessary to appoint a permanent chairman of the board nor are the powers of the chairman defined.

In another area related to executive management, we endeavoured to examine the compliance with the good governance norm of separating the functions of the chief financial officer and the company secretary. Compliance in this regard was reasonable with segregation being identifiable in 30 companies, while in six the posts were stated to be held by the same person.

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However, we found that in 14 cases disclosure was not clear enough for us to determine this fact therefore distorting our results in this area.

Other Disclosures

Thirty-four of the companies surveyed had declared both their vision and mission statements separately, one had declared them on a combined basis, seven had disclosed only their mission statements, while a further eight had not disclosed either.

A disclosure that was very infrequent was that of the 'Statement of Ethics and Business Practices', which was disclosed by only seven companies. Disclosure of company websites in the annual reports, although better, was also disappointing at 48%.

Apart from financial institutions (our sample contained 10 FIs) only two companies disclosed entity credit ratings. With respect

to their dividend/bonus history, 10 of the companies surveyed did not include this data in their financial highlights.

Board of Directors

Board composition and operations are probably the most critical elements of the corporate governance culture of a company.

We give below a table tabulating the size of the boards seen in our survey:

From the above table it is obvious that most companies prefer small to medium-sized boards as these

No. of Members	
7-10	39
11-15	9
>15	2

are more manageable. However, companies should not always concentrate on the board size as the main parameter of board composition but on the type of people needed to effectively provide strategic input in company affairs.

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The above discussion on board size, however is rendered somewhat meaningless in the absence of a significant proportion of independent directors. Of our surveyed companies, 18 did not disclose the number of independent directors while a further 15 reported less than 30% of the directors as being independent. Similarly, 26 companies did not disclose the number of minority directors and

another 13 reported the complete absence of such directors on the board. We believe that in the interest of encouraging the presence of both independent and minority directors on the boards of companies they should be required to report the exact number of such directors in their annual reports.

Frequency of board meetings did not show any clear pattern although it was encouraging to note that in 39

instances more than the required minimum 4 meetings were held, while two companies did not disclose the number of meetings held.

Attendance levels at the board meetings were not as strong as we believe they should be, with 20 of the 48 companies reporting their attendance recording it at below 75%.

Audit Committee

Disclosures regarding the functioning of the audit committee were found to be so poor that it is not possible to form any opinion regarding the functioning of such committees. Only 15 companies reported the frequency of meetings of the audit committee while a mere 7 disclosed the attendance pattern of such meetings. However, we were able to collect data with respect to the presence of the chairman, chief executive or any other executive on the audit committees, in all but three cases (where as previously stated the name of the chairman was

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not disclosed). Here also the results indicated a lack of understanding of the role of the audit committee with more than half the audit committees including either the chairman or an executive director. JCR-VIS

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Faheem Ahmad

President & CEO, JCR-VIS
Founder, VIS Group

Faheem Ahmad has diverse experience with international consulting agencies in USA & Middle East. He has also held senior positions with local industrial and financial groups. In 1994, he established Vital Information Services (Pvt.) Limited, which is a leading capital market research house. VIS has the largest data bank of corporate Pakistan. His major research work includes copyrighted F&J financial strength rankings, Musharaka Variable Income Securities and stock market indices. VIS group includes JCR-VIS Credit Rating Company Limited and News-VIS Credit Information Services (Pvt.) Limited, the first private credit bureau of Pakistan. The majority of shareholders in group companies include the largest publication house in Pakistan and major financial institutions.

He obtained his B.S in Civil Engineering from NED University of Engineering and Technology, Karachi. He also has Masters degrees in Engineering and Business Administration from USA. His research work has been published in various international journals.



Saad Ahmed Madani

Group Head - Corporates & Structured Finance

Saad Ahmed Madani, a chartered accountant by profession, heads the Corporates & Structured Finance Group at JCR-VIS. In addition he also supervises corporate governance ratings. He has been associated with JCR-VIS for nearly five years, prior to which he had completed his training from a leading audit firm in Karachi.



Mansur Ali Shah

Manager

Mansur Ali Shah is in the Corporates & Structured Finance Group and is the lead analyst on corporate governance ratings. He holds a certificate in Business Accounting from the Chartered Institute of Management Accountants, UK and CA Intermediate from the Institute of Chartered Accountants of Pakistan. He has over six years working experience with two leading Chartered Accountancy firms in Karachi before joining JCR-VIS.

Jahangir Kothari Parade (Lady Lloyd Pier)
Inspired by Her Excellency, The Honorable Lady Lloyd, this promenade pier and pavillion was constructed at a cost of 3 Lakhs and donated to the public of Karachi by Jahangir Kothari to whose generosity and public spirit the gift is due. Foundation stone laid on January 5, 1920. Opened by Her Excellency, The Honorable Lady Lloyd on March 21, 1921.

Dome: A roof or vault, usually hemispherical in form. Until the 19th century, domes were constructed of masonry, of wood, or of combinations of the two, frequently reinforced with iron chains around the base to counteract the outward thrust of the structure.

Origins: The dome seems to have developed as roofing for circular mud-brick huts in ancient Mesopotamia about 6000 years ago. In the 14th century B.C. the Mycenaean Greeks built tombs roofed with steep corbeled domes in the shape of pointed beehives (tholos tombs). Otherwise, the dome was not important in ancient Greek architecture. The Romans developed the masonry dome in its purest form, culminating in a temple built by the emperor Hadrian. Set on a massive circular drum the coffered dome forms a perfect hemisphere on the interior, with a large oculus (eye) in its center to admit light.



Jahangir Kothari
Parade

National Excellence, International Reach

JCR-VIS Credit Rating Company Limited is committed to the protection of investors and offers a blend of local expertise and international experience

to serve the domestic financial markets. With its international reach, JCR-VIS is positioned to aim for an international mark. In this regard, the global experience of our principal, Japan Credit Rating Agency, Ltd. has been invaluable towards adding depth to our ongoing research endeavors, enriching us in ways, that enable us to deliver our responsibilities to the satisfaction of all investors.

The edifice of the Jahangir Kothari Parade has stood proudly through the years and is a symbol of our heritage. Its 'Dome' as the most stable of building structures, exemplifies architectural perfection. Committed to excellence, JCR-VIS continues its endeavor to remain an emblem of trust.

JCR-VIS Credit Rating Company Limited

Affiliate of Japan Credit Rating Agency, Ltd.
Founder Shareholder of Islamic International Rating Agency, Bahrain
JV Partner in CRISL, Bangladesh
Member Association of Credit Rating Agencies in Asia

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