

Al-Faryan, Mamdouh Abdulaziz Saleh

Article — Published Version

Corporate governance in Saudi Arabia: An overview of its evolution and recent trends

Risk Governance & Control: Financial Markets & Institutions

Suggested Citation: Al-Faryan, Mamdouh Abdulaziz Saleh (2020) : Corporate governance in Saudi Arabia: An overview of its evolution and recent trends, Risk Governance & Control: Financial Markets & Institutions, ISSN 2077-429X, Virtus Interpress, Sumy, Vol. 10, Iss. 1, pp. 23-36, <https://doi.org/10.22495/rgcv10i1p2>

This Version is available at:

<https://hdl.handle.net/10419/225997>

Standard-Nutzungsbedingungen:

Die Dokumente auf EconStor dürfen zu eigenen wissenschaftlichen Zwecken und zum Privatgebrauch gespeichert und kopiert werden.

Sie dürfen die Dokumente nicht für öffentliche oder kommerzielle Zwecke vervielfältigen, öffentlich ausstellen, öffentlich zugänglich machen, vertreiben oder anderweitig nutzen.

Sofern die Verfasser die Dokumente unter Open-Content-Lizenzen (insbesondere CC-Lizenzen) zur Verfügung gestellt haben sollten, gelten abweichend von diesen Nutzungsbedingungen die in der dort genannten Lizenz gewährten Nutzungsrechte.

Terms of use:

Documents in EconStor may be saved and copied for your personal and scholarly purposes.

You are not to copy documents for public or commercial purposes, to exhibit the documents publicly, to make them publicly available on the internet, or to distribute or otherwise use the documents in public.

If the documents have been made available under an Open Content Licence (especially Creative Commons Licences), you may exercise further usage rights as specified in the indicated licence.



<https://creativecommons.org/licenses/by/4.0/>

CORPORATE GOVERNANCE IN SAUDI ARABIA: AN OVERVIEW OF ITS EVOLUTION AND RECENT TRENDS

Mamdouh Abdulaziz Saleh Al-Faryan *

* Department of Economics and Finance, Faculty of Business and Law, University of Portsmouth, the UK
Contact details: Department of Economics and Finance, Faculty of Business and Law, University of Portsmouth, Richmond Building
Portland Street Portsmouth PO1 3DE, the UK



Abstract

How to cite this paper:

Al-Faryan, M. A. S. (2020). Corporate governance in Saudi Arabia: An overview of its evolution and recent trends. *Risk Governance and Control: Financial Markets & Institutions*, 10(1), 23-36. <http://doi.org/10.22495/rgcv10i1p2>

Copyright © 2020 The Author

This work is licensed under a Creative Commons Attribution 4.0 International License (CC BY 4.0).
<https://creativecommons.org/licenses/by/4.0/>

ISSN Online: 2077-4303

ISSN Print: 2077-429X

Received: 20.01.2019

Accepted: 17.02.2020

JEL Classification: G18, G34, G38, K22

DOI: 10.22495/rgcv10i1p2

In spite of growing interest in Saudi corporate governance systems, there is little literature on the evolution of Saudi corporate governance. This study helps close this gap by investigating and compiling corporate governance development in Saudi Arabia. After providing background information for Saudi Arabia and its corporate governance model, we touch on the Saudi legal system and key external institutions that helped shape its corporate governance. We examine the specific contributions of the accounting and auditing professions, and the roles of the National Anti-Corruption Commission and the Saudi Stock Exchange. We describe key reforms implemented to develop the Saudi economy and evaluate their importance in facilitating change in corporate governance practices. This study contributes as an initial point of reference for future studies on Saudi Arabia, and serves as a one-stop resource for both academics and practitioners, while specifically benefitting foreign and domestic investors considering investments in Saudi Arabia.

Keywords: Capital Markets, Corporate Governance, Ownership, Foreign Direct Investment, Saudi Arabia, Saudi Legal System, Stock Market Crash

Authors' individual contribution: The author is responsible for all the contributions to the paper according to CRediT (Contributor Roles Taxonomy) standards.

1. INTRODUCTION

There are many reasons for the push to create a corporate governance framework in Saudi Arabia, such as the desire of policymakers to present the country as modern and equipped to welcome foreign direct investors and investments in various ownership forms and improve the accountability of listed firms. However, one of the main reasons has been the need to diversify and develop the Saudi economy away from its oil dependency and develop the capital market as an important capital source. In 1999, the Supreme Economic Council (SEC) was created because of an urgent notification from the Saudi executive authority to improve Saudi Arabia's economic performance. As the supervisor of all Saudi Arabian economic and financial policies, the

SEC has wide-ranging responsibilities.¹ In 2000, policymakers passed a number of legal and economic measures designed to enhance Saudi Arabia's global position. In April 2000, the Saudi Arabian General Investment Authority (SAGIA) was established to promote a pro-business environment and explore investment opportunities within the energy, transportation, and knowledge-based industries in Saudi Arabia.² One of SAGIA's main objectives is to eradicate problems faced by domestic and foreign investors in starting and running businesses (KSA-CM, 2000b). In these areas, it works closely with the SEC, serving as a mediator between investors and the government (SAMIRAD, n.d.).

¹ The SEC is headed by the King and ministers (Supreme Economic Council Law, 1999, Art. 4). In January 2015, King Salman replaced the SEC with the Saudi Council of Economic and Development Affairs, a subcommittee of the Saudi government, headed by Crown Prince Mohammed bin Salman.

² SAGIA also serves the business community as the 'one-stop shop' for licences, permits, and other business administrative procedures.

A further reason for the development of Saudi corporate governance was the 2006 stock market crash, which led the Saudi Capital Market Authority (CMA) to establish measures designed to protect the market and investors from future failures. On July 3, 2006, the CMA Board initiated a corporate governance project and, on November 12, 2006, issued a final form of corporate governance in resolution and Corporate Governance Code No. 1-212-2006. This was due to the CMA's concern about the lack of mechanisms for improving market efficiency over time, which could also maintain and increase the attractiveness of trading Saudi securities. To facilitate the process, the CMA created corporate governance principles by adapting those of international organisations such as the Organisation for Economic Co-operation and Development (OECD) and the United Kingdom (UK) corporate governance codes in the Cadbury and Greenbury reports (Riyadh Chamber of Commerce and Industry, 2007, p. 40). The academic contributions by many public and private institutions also helped determine the evolution and development of corporate governance in Saudi Arabia and increase the importance of corporate governance in corporate life.³ Additionally, various factors and events have led to key developments in and the evolution of Saudi corporate governance, which can be seen in laws, regulations, and the external framework of corporate governance, as well as the reforms the country experienced, which are the focus of the subsequent sections.

These contributions to corporate governance development range from legal to institutional, as reflected by the Saudi Arabia legal system, including the authority vested in the CMA to regulate and supervise the day-to-day operations of the Saudi Stock Exchange (SSE).

Section 2 presents a review of the literature on corporate governance in Saudi Arabia. Section 3 discusses corporate governance developments in Saudi Arabia, and Section 4 examines the legal system and key external institutions that helped shape the development of corporate governance up to 2017. Section 5 explores the accounting and auditing profession's influence on the development of corporate governance, while Section 6 discusses the National Anti-Corruption Commission (NAC). Section 7 examines the Saudi government's key reforms and assesses their importance in facilitating corporate governance change. Section 8 briefly assesses the roles of the SSE and the insurance sector in developing the existing corporate governance framework. Section 9 concludes this study.

³ For example, the tenth conference for developing accounting and auditing practices at the King Saud University in 2003 recommended adopting and implementing corporate governance principles. In 2007, various conferences discussed corporate governance and its importance for Saudi Arabia. Conferences were also held regarding the corporate governance of financial and exchange companies. Furthermore, conferences on the role of banks in encouraging corporate governance were held by the Institute of Saudi Banking and the International Finance Corporation (IFC). During 2008 and 2009, many seminars and conferences were held and viewed as effective in pushing for the need to apply corporate governance principles. The CMA and US Securities and Exchange Commission held the first workshops on corporate governance. The second workshop was held at the King Saud University, by the King Abdullah Centre for Research and Studies. A further international conference on corporate governance was held at the King Khalid University, by the Centre of Corporate Governance.

2. LITERATURE REVIEW

Corporate governance is an organisational variable that is often difficult to detect or manage. Typically, it reflects the relationship between various agents who determine a corporation's future direction and performance. The configuration of corporate governance includes a formal mechanism, legal rules, and informal mechanisms such as conventions and organisational norms, which are as much relational as legal. The corporate governance literature reveals a wide range of corporate governance regimes in both developed countries and emerging markets. Over time, these economies have developed different market mechanisms, legal structures, factor markets, and private and public institutions and, in turn, corporate governance arrangements. These arrangements may even vary between industry sectors within the same country or may be widely influenced by a country's institutional, political, and social norms. This suggests there is no single model of corporate governance in any country, as governance practices are known to vary not only across countries but also across firms and industry sectors.

One of the most apparent differences between the governance systems of industrialised countries lies in firm ownership and control. Corporate governance systems can thus be distinguished by the degree of ownership and control and by identification of the shareholders who control a firm. Some systems are defined by dispersed ownership (insider systems), while others are characterised by concentrated ownership (outsider systems). With insider corporate governance systems, such as those in the United Kingdom (UK) and the United States (US), the conflict of interest is mainly between strong managers and weak widely dispersed shareholders. In outsider corporate governance systems, which prevail in continental Europe and Japan, the fundamental conflict is between controlling shareholders, also known as block-holders, and weak minority shareholders. These differences primarily result from the diverse legal, regulatory, and institutional environments in countries, as well as cultural norms and historical factors (Aguilera & Jackson, 2003; Shleifer & Vishny, 1997).

The relative success of corporate governance in industrialised countries may be considered against the backdrop of globalisation and industrial reforms instigated by governments worldwide to attract inward foreign direct investments. In turn, this approach has focussed attention on either establishing a corporate governance framework where none previously existed or implementing corporate governance changes. This is particularly the case in countries that previously only paid lip service to corporate issues but now actively seek to implement policies that promote adopting specific corporate governance forms and especially governance change. In this context, the search for the most suitable corporate governance practices is founded on adopting what works best in other countries, inferring the lessons that can be derived from country-level experiences and transferring these practices to countries without a long history of corporate governance practices. As such, research in this area is crucial to countries such as Saudi Arabia

that have taken great leaps towards implementing corporate governance practices as a first step in bringing their corporate governance levels in line with the practices of OECD countries (Al-Janadi, Abdul Rahman, & Omar, 2013; Al-Matari, Al-Swidi, Bt Fadzil, & Al-Matari, 2012; Falgi, 2009).

Corporate governance, a crucial element in developed, emerging, and developing countries, involves multi-dimensional factors such as the business environment, economy, legal structures, and social and cultural backgrounds. As such, its focus has naturally become much wider, including prevention of fraudulent activities, improved transparency and disclosure, and increased economic stability, growth, and development, as well as market efficiency. It has thus become important in signalling the need to create clearer rules of conduct and operations. This holds particularly true in light of the impact of the Saudi and other Gulf countries' stock market crashes in the global financial market, with most retail investors losing substantial amounts of invested funds due to the Gulf markets' poor governance and corporate practices. Kim (2010) and Heenetigala and Armstrong (2011) note that the benefits of good corporate governance can be far-reaching because it can influence neighbouring regions as well as the country itself. Therefore, it is important to analyse the financial aspects of corporate governance in Saudi Arabia to reveal its current state and the success of the measures implemented to improve and enhance corporate governance quality, as well as to provide useful insights into future corporate governance reforms in Saudi Arabia.

Al-Dubai, Ismail, and Amran (2015) use data for 75 Saudi listed firms for 2007–2011 to study the non-linear relationship between family ownership and firm value. Specifically, the study investigates the relationship between expropriation and monitoring in family firms and finds that family ownership of 28% is a turning point for confirming the expropriating-monitoring trait of family firms. The authors note that investors should not undervalue Saudi stocks based on ownership as, at a certain point, the benefits of family firm monitoring will exceed costs. Further, Habbash and Bajaher (2015) study the moderating effect of family-owned firms and argue that family ownership and corporate governance can be monitoring substitutes, while Amin and Hamdan (2018) use a sample of 171 Saudi firms for 2013–2014 and, employing a fixed effects regression model, investigate the relationship between ownership structure and firm performance. Ownership concentration and structure for family, foreign, managerial, and institutional firms is studied using the return on assets (ROA) as the only performance measure. The study finds institutional ownership has a positive effect on performance, while foreign ownership has a negative effect. Notably, family and managerial ownership show no significant relationships with performance.

In another literature strand, Alhumoudi (2016) examines Saudi ownership structures, focussing on managerial and shareholder ownership concentrations above 5%, and report that managerial ownership has a positive effect on firm performance. Buallay, Hamdan, and Zureigat (2017) examine the impact of corporate governance on firm

performance and show a significantly negative effect on firm value of the three largest shareholder groups. Al-Ghamdi and Rhodes (2015) examine shareholders holding above 10% equity stakes in family- and non-family-owned Saudi firms (excluding the banking and financial service sectors) for 2006–2013, and find that ownership concentration in family firms has no impact on ROA but affects Tobin's Q.

There are many studies on the ownership structures of listed firms across various sectors, with most ignoring firms in the financial sector, while a small number of studies investigate only financial sector firms. A criticism of this approach is that the sample becomes very small, which affects the empirical findings. Furthermore, such studies claim there are regulatory differences between financial and non-financial firms; however, they do not clearly identify these differences. The literature review above shows that most studies employ similar models and methodologies, including variables and performance measures. Therefore, it is unclear how past studies have adjusted their methods to incorporate the regulation differences between industries.

The vast literature on corporate governance focusses on developed countries, which have specific characteristics in terms of legal structure, market structure, institutional environment, and social and economic cultures built over several centuries. Consequently, studying the Saudi Arabian market contributes to the corporate governance literature in terms of providing an analysis of a large developing economy. The characteristics of the Saudi economic environment make this study even more interesting. Examples are the high ownership concentration of family-owned firms, relatively few listed firms, and a large number of privately owned family firms (Bolbol & Omran, 2005). Furthermore, the privatisation and market reforms over the last few decades not only in Saudi Arabia but other Gulf states as well, make this study important, as it has been argued that privatisation has been slower compared to developing nations in other regions (Belkhir, Maghyereh, & Awartani, 2016).

2.1. Model of corporate governance in Saudi Arabia

The transition from the no specific model of corporate governance tailored to the Saudi Arabian context to the adoption of an Anglo-American model of corporate governance that is in tune with Saudi Arabia's business environment was an attempt to introduce corporate governance mechanisms and principles to align managers' interests with those of Saudi firms. However, it may be argued that agency theory has overlooked the cultural aspects of Saudi Arabia, namely the extent to which owners of Saudi firms are able to create a corporate governance framework to match their needs. Further, it is likely that different types of investors may pursue different interests, with some investors placing more emphasis on social welfare or community ideals, while others may favour maximising personal wealth. Arguably, some shareholders may prefer corporations to be run by independent managers with minimal crossholdings, while others may prefer government-owned companies. Considering these cultural characteristics may thus hinder

development and prevent real changes from taking place. However, based on well-publicised announcements by Saudi policymakers, the intention has been for corporate governance in Saudi Arabia to converge towards international best practices.

Saudi Arabia has strong historical relationships with the UK and the US, from which it has borrowed many business practice regulations and standards, such as accounting practices and standards, auditing standards, and auditor independence (Al-Angari, 2004), and adapted them to the Islamic context (Alghamdi, 2012). Banks and financial institutions are also subject to international accounting standards and companies listed on the SSE are required to follow national accounting standards (NAS) (IFRS, 2017).

3. DEVELOPMENT OF CORPORATE GOVERNANCE IN SAUDI ARABIA

It was not until 2005 that serious discussions regarding corporate reforms began when the Saudi Arabian CMA (also abbreviated as SACMA) drew attention to the problems with Saudi companies' performance. These were further highlighted by the stock market crash of 2006, the implications of which became a major concern for investors. Following the crash, a series of measures were implemented as an attempt by policymakers to address structural problems such as weak legal and investor protection, economic uncertainty, government-owned firms, family-dominated companies, poor company performance, and high ownership concentration, which underline the need for an effective corporate governance framework. Domestic and foreign investors viewed this step as a positive policy move towards developing and enhancing corporate governance in Saudi Arabia. Its benefits include adopting, following, and adhering to international best practices and the corporate governance principles issued by the OECD which, over time, would enhance the international competitiveness of the diversified economy. It is perhaps worth noting that the OECD has recommended adopting rule-based corporate governance (as set by industrialised countries' capital markets) owing to the Saudi stock market's position and its poor corporate discipline and lack of corporate experience. As such, the emphasis has been placed on legal and regulatory control in shaping the development of the corporate governance framework; the legal system has been pivotal by specifying practices and regulations, as has the Saudi constitution, which is based on the Quran and Sunnah and adheres to Islamic Shariah Law (Al-Harkan, 2005).⁴ In fact, all aspects of Saudi life are deeply influenced by Islam, which affects business operations, especially through the focus on ethics and belief in human equality (Moustafa, 1985). When Saudi Arabia adopts accounting and auditing standards or corporate governance practices, it alters them to be consistent with Saudi Islamic law (Al-Harkan, 2005).

3.1. Company Law and company structure

Company Law (1965) in Saudi Arabia is viewed as one of the most important regulations, as it is one of the first laws to regulate Saudi Arabian firms and was issued by royal decree, which means it applies to all companies. Originally derived from British Company Law, it has been updated to the current situation. However, Al-Ghamdi and Al-Angari (2005) argue that it is still outdated and does not accommodate modern requirements. In addition to Company Law, corporate structure, which must be consistent with this law, plays a key role in determining the legal and organisational systems of Saudi Arabian corporations. Specifically, companies are required to set out a number of regulations in their foundation stage, such as the appointment of the board of directors, termination, and shareholder rights.

3.2. Shareholder rights

In Saudi Arabia, Company Law provides for and protects shareholders' rights to their shares. Particularly, the law gives shareholders that own 20 or more shares the right to attend the corporation's annual general meeting (AGM), where company issues are discussed. Shareholders also have the right to discuss and vote on company decisions, look at company archives, and dispose of shares as they will. Article 109 of Saudi Arabia Company Law states that shareholders who own 5% or more of a company's shares have the right to request the companies' settlement authority to inspect the company if they have doubts concerning the board of directors or conduct of external auditors. Since the law protects shareholders' interests, it confers upon them the right to receive profits on their shareholdings, as well as the residual profits upon company dissolution.

3.3. Company internal control

In 2000, the SEC approved the recommendations made by the Ministerial Committee created by Royal Decree No. 3151 to study the situation of listed Saudi companies. The Committee focussed on two key issues to improve the Saudi stock market's integrity. First, it highlighted and supported the role of company internal controls and advised and encouraged shareholders to monitor their company's performance. Second, it ensures sufficient information is available in firm financial statements to allow investors and shareholders to appraise a company's performance and value, thereby enabling market participants to protect their investments.

3.4. Accounting and auditing standards

To enhance corporate governance in Saudi Arabia, the National Accounting and Auditing Standards (NAAS) were issued by policymakers in 1986. These were derived from the US standards and had to be followed by listed Saudi firms, except for those in the banking and financial sectors, which follow international accounting standards (IFRS, 2017).

⁴ The teachings of prophet Muhammad (peace be upon him).

The question to be addressed is whether policymakers in Saudi Arabia 1986 had other reasons (besides corporate governance) to issue the NAAS. The first main reasons are zakat and tax. The accounting reports in the standards calculate tax profit and zakat or produce information that helps the national planner prepare national data. This data aids in planning and decision-making at the national level, despite the adoption of economic reform programs, which include liberalization of family firms and opening them up to the public by initial public offerings (IPO) and increasing the number of companies. Second, investors and other users of financial statements are satisfied with national standards and financial statements, while it is difficult for users to switch to reading financial statements prepared with accounting methods other than those they are accustomed to, such as international accounting and auditing standards. This is especially the case because the accounting knowledge of financial statement users in Saudi Arabia is considered too weak to understand financial reporting produced using different accounting standards. Third, one set of standards for all firms makes it easy to understand financial reporting. Finally, applying Saudi Accounting and Auditing Standards lies within the framework of unifying the accounting terms and concepts used in preparing financial statements. This helps prevent fraud and manipulation that may occur from the use of different terminologies and helps control the work of companies and prevent them from evading payment of zakat or tax.

Since 1992, the Saudi Organisation for Certified Public Accountants (SOCPA) has been responsible for developing and reviewing accounting and auditing standards. More recently, SOCPA attempted to merge the Saudi national standards with IFRS; as a result, banks and financial institutions have started to apply IFRS. This was considered the beginning of Saudi stock market reform and making disclosure more uniform, which enabled investors to more easily compare and evaluate published financial statements and other information. To date, the NAS have played a key role in developing disclosure and financial transaction treatment. They consist of 21 standards relating to issues such as disclosure requirements, inventory standards, and revenue standards. The NAS also played a key role in increasing the external auditor competence and

enhancing audit quality through 16 standards often associated with auditor competence, audit plans, independence, and audit reports. These standards represent the early development of corporate governance in Saudi Arabia through their impact on listed firms.

3.5. Capital Market Law

Capital Market Law, which regulates the conduct of market participants while also protecting investors' interests, was issued in 2003 by Royal Decree No. M/30 dated 2/6/1424H (July 31, 2003) to help sustain growth and attract new investors by protecting the stock market. For example, the law requires strict disclosure and has made any market abuse by way of manipulation and insider trading illegal, thereby ensuring fair stock market dealings, efficiency, and investor confidence in the Saudi stock market. Saudi Arabia's Capital Market Law consists of 10 chapters and 67 articles and led to the creation of the SACMA, which has full authority and power over all capital market activity, including the Saudi stock market and all listed firms, and the right to issue new rules to regulate the stock market activity. Capital Market Law also led to the improvement in and development of corporate governance to create the stock exchange as we know it today. Furthermore, this law led to the creation of a securities deposit centre, a securities settlement committee, and an appeals committee to ensure the Saudi stock market's efficient functioning.

3.6. Corporate Governance Code

Despite past rules and regulations, corporate governance mechanisms in Saudi Arabia were minor and largely ignored until 2005. In 2005, the SACMA drew attention to problems in company performance as a result of the 2006 stock market crash, thereby highlighting significant weaknesses in financial reporting, transparency, and disclosure and a lack of accountability (SOCPA, 2007). On February 25, 2006, the market closed at a historic high of 20,634.86; the collapse began the next day. By the end of 2006, the main stock market index, the SSE, had lost about 65% of its value and market capitalization had fallen by half to \$ 326.9 billion (Figure 1).

Figure 1. SSE weekly index from 2000 to 2006

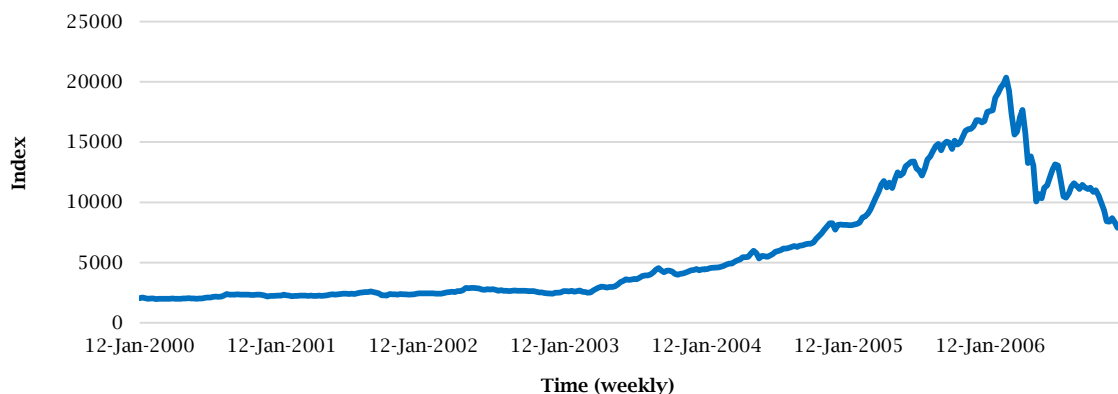
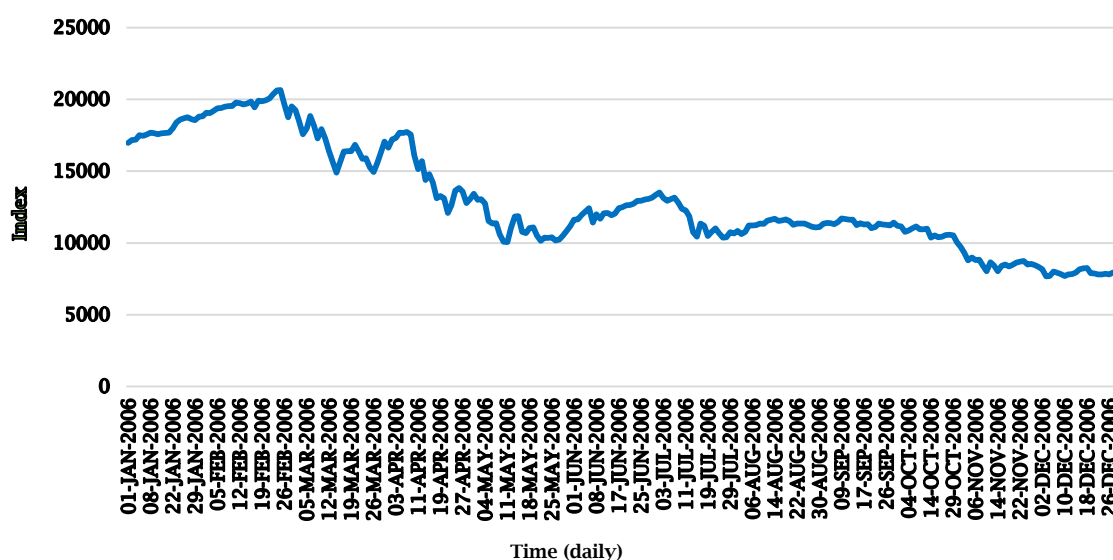


Figure 2 shows that the SSE index decreased from 20,634.86 on February 25, 2006, to 7933.29 by the end of 2006. Prior to 2006, corporate governance mechanisms in Saudi Arabia included key rules, regulations, and standards for shareholder rights, board composition, disclosure, and transparency for listed companies, all originating from various sources. The key laws underlying corporate governance and its legal framework can be divided

into three groups — Company Law, SOCPA, and CMA — all aiming to tackle and develop corporate governance by ensuring best practices, compliance, and protection of shareholder and stakeholder rights while maintaining market integrity and confidence. One criticism directed at these arrangements was that they lacked an overall or central corporate governance framework for listed firms.

Figure 2. SSE daily index from January 1, 2006 to December 27, 2006



It was only after the 2006 stock market crash that corporate governance began to receive wide support from the Saudi government, with SACMA issuing a Corporate Governance Code titled 'Corporate Governance Regulations in the Kingdom of Saudi Arabia' in 2006, which was amended in 2009, and applies to all companies listed on the SSE on a comply and explain basis. The code stipulates that corporate governance information should be disclosed by all traded companies. Initially, the code mostly served to provide guidelines to listed companies but, since 2010, it has become mandatory. It consists of 19 articles and is divided into five sections that cover the five main OECD principles. Part 1 (Articles 1-2) presents preliminary provisions and defines the terms and expressions that relate to the regulation. Part 2 (Articles 3-7) is about shareholder rights and the general assembly, specifically allowing shareholders to exercise their rights, including rights to general meetings, voting rights, and rights to dividends, and have access to information. Part 3 (Articles 8-9) relates to policies and procedures regarding disclosure and transparency and, in particular, board of director reports. Part 4 (Articles 10-18) refers to the role and functions of the board of directors.⁵ Part 5 (Article 19) includes closing provisions and effective enforcement dates upon their publication (CMA, 2006; Hussainey & Al-Nodel, 2008). In 2009, the CMA stated that 96% of all firms listed on the Saudi stock market had complied with

the Corporate Governance Code ("Market Authority", 2011). Although the World Bank's analysis differed from the CMA's statistics, it agreed that Saudi Arabia was attempting to replicate international best practices and that the CMA was still in its infancy stage (Berg & Di Benedetto, 2009). In 2012, the Saudi Arabian Monetary Agency (SAMA) issued the 'Principles of Corporate Governance for Banks Operating in Saudi Arabia'. This code relates more specifically to listed banks and financial institutions and consists of six key principles: board member qualifications, board composition and appointment, board responsibilities, board committees, shareholder rights, and disclosure and transparency.

3.7. Duplication between Company Law and the Corporate Governance Code

There are some similarities between Saudi Arabia's Corporate Governance Code and the Saudi Arabia Company Law, the latter being based on French law (Koraytem, 2000, p. 65). Company Law was initiated by the Ministry of Commerce and Industry, whereas the code of corporate governance was issued by the CMA. Company Law consists of 12 chapters with 227 compulsory articles and affects all companies in Saudi Arabia, including limited liability companies, joint liability companies, limited partnerships, professional companies, and joint stock companies (Company Law, 1965, Art. 2 and 5-10). As previously noted, the CMA is responsible for the SSE and its listed firms. The CMA is a semi-governmental body in charge of Saudi corporate governance regulations,

⁵ This includes its formation, meetings, board committees, audit committees, nomination and remunerations committee, indemnification of board members, and conflicts of interest within the board.

although a dual system of corporate governance exists for listed firms, stemming from the CMA and the Ministry of Commerce and Industry, which implemented the Company Law. However, it is worth noting that, according to policymakers, the CMA is the more advanced body, being well placed to encourage and implement corporate governance mechanisms. This is because Company Law is being reviewed by the Consultative Council, that is, the Saudi legislative body. Additionally, Company Law is viewed as a point of reference for the Ministry of Commerce and Industry, with some corporate governance provisions included within Company Law but without specific articles relating to corporate governance. Currently, the legislative body is looking to reform and update Saudi Company Law to align it with recent developments.

4. EXTERNAL INSTITUTIONS SHAPING SAUDI ARABIA'S CORPORATE GOVERNANCE FRAMEWORK

The main external framework for corporate governance in Saudi Arabia includes the SAMA and Ministry for Commerce and Industry. SAMA is Saudi Arabia's central bank, established in 1952 to create the Saudi currency and develop and reform the financial market. Currently, the main function of SAMA includes banking for the government, management of monetary policy, maintaining stable prices and exchange rates, promoting financial system growth and soundness, and supervising commercial banks and financial institutions, including insurance companies. SAMA was first responsible for operating and regulating the Saudi stock market.⁶ In 1984, SAMA, along with the Ministry of Finance and National Economy and the Ministry of Commerce, formed a Ministerial Committee to regulate and develop the Saudi stock market.⁷ As a result, the Saudi Share Registration Company (SSRC) was established by royal decree; it is run by local banks and supervised by SAMA. Part of SAMA's role is to support settlement operations, and transfers and registration of property are automatically implemented. Overall, this was the beginning of an era moving towards automated electronic stock market trading processes.

4.1. Ministry of Commerce and Industry

The Ministry of Commerce and the Ministry of Industry merged to form the Ministry of Commerce and Industry with the authority to monitor Saudi companies, including limited liability companies, joint liability companies, limited partnerships, professional companies, and joint stock companies.⁸ Although the main functions of the Ministry of Commerce and Industry are to regulate, supervise, and register Saudi companies and ensure their compliance with regulations, it also plays a key role in corporate governance as it certifies the companies to be listed and ensures their company policies are in line with Company Law and good corporate

governance practices with respect to shareholder rights (Company Law, 1965, Art. 83). Once firms are listed on the SSE, they are further regulated by the CMA.⁹

4.2. Role of the Capital Market Authority

The CMA began as an unofficial organization, which means it operated under its own rules and an informal broker-based system from the 1950s; it was not until the 1980s that the Saudi government began its basic regulation. The Capital Market Law was first enacted in 2003 to regulate the CMA regarding its responsibilities towards the stock exchange and investors and in 2004, it officially became the independent main regulatory body of the Saudi capital market for the SSE and all listed firms. The CMA has direct links to the Prime Minister and reports directly to the King; it also has executive legislative powers to adopt and pass regulations to maintain market confidence.¹⁰ The main role of the CMA is to regulate and help develop the Saudi stock market and thus, listed firms. As such, the CMA establishes rules and regulations to increase investment and enhance transparency and disclosure, and also to protect investors and stock market participants from illegal market activities (CMA, n.d.a). Therefore, the CMA is considered the most important external institution shaping corporate governance in Saudi Arabia. Despite being a semi-governmental organisation with administrative autonomy, its role and responsibilities have far-reaching legal and financial implications.

The CMA is governed by a board of five highly qualified permanent members appointed by the Prime Minister, each serving a 5-year term that is subject to only one renewal.¹¹ Recently, it has become easier and quicker for the CMA board to enact statutory regulations, provided it is within the remit of the Capital Market Law, which allows it to pass new articles without review by the Kingdom of Saudi Arabia's Council of Ministers (KSA-CM) or the Consultative Council as legislative bodies (Capital Market Law, 2003, Art. 5 B). One of the most important regulations issued by the CMA is the Corporate Governance Code of 2006, for which it was mandated all powers over the Saudi capital market. As such, the key CMA objectives, apart from regulating and developing the Saudi stock market, are to improve disclosure, increase transparency, ensure fair trading activity, and make changes to the stock exchange and listed Saudi firms' requirements as and when necessary.¹² For this purpose, the CMA has an internal department (the General Department of Corporate Governance) responsible for improving

⁹ The Ministry of Commerce and Industry has an indirect supervisory role for various other bodies such as the CMA, Tadawul, and SOCPA. A key department of the Ministry is the Department of General Companies, which is responsible for examining and amending the articles of association for newly established firms (Company Law, 1965, Art. 49).

¹⁰ The CMA has full authority to accomplish its role and responsibilities (Capital Market Law, 2003, Art. 4 A). The King is the head of the Council of Ministers.

¹¹ The CMA board Chairman and Deputy Chairman are nominated, with salaries predetermined by royal order (Capital Market Law, 2003, Art. 7 A and 7 B).

¹² At the same time, it is also responsible for and in charge of issuing regulations, instructions, and ensuring these are implemented and followed (Capital Market Law, 2003, Art. 5 A).

⁶ www.sama.gov.sa

⁷ www.tadawul.com

⁸ In May 2016, the name of the Ministry of Commerce and Industry was changed to the Ministry of Commerce and Investment.

and implementing corporate governance systems (CMA, n.d.b) and for liaising with the various local and international institutions regarding corporate governance issues that can benefit listed Saudi firms and the stock market. Within its available means, the CMA has worked with struggling brokerage firms to achieve a more effective stock market. Following the stock market crash of 2006 and the subsequent recovery, one of the key corporate governance changes implemented by the CMA was regulation of financial statements and the work of mediators in the stock market in terms of market transparency, which resulted in increased stock trading volume and investor confidence owing to guarantees related to shareholder rights.

Since its inception, the CMA has contributed significantly to shaping corporate governance practices in Saudi Arabia. Before 2000, firms were not required to publish financial statements; as a result, trading was largely conducted without technical analysis of firms, where the majority of retail investors were first-time traders who were easily manipulated into investing in stocks that incurred large losses in the stock market crash of 2006. To prevent this type of conduct, the CMA introduced the Corporate Governance Code and regulations to prevent fraud and deception, as well as increase transparency and disclosure. Another important CMA reform was the opening of the stock market to foreign investors in June 2015, with the scope of creating a globally recognised and valued stock exchange on par with the US, the UK, and other leading stock exchanges.

4.3. Committees for the resolution of securities disputes

The judicial system in Saudi Arabia is divided into: 1) the Sharia court system; 2) the board of grievance, and 3) quasi-judicial committees. The latter have a loose structure because they comprise a wide range of governmental and semi-governmental bodies. For instance, the Committees for the Resolution of Securities Disputes (CRSD) is a quasi-judicial financial commission, whose fundamental role is to protect shareholders, investors of listed firms, and the stock market; maintain market confidence; implement regulations; and resolve any disputes that may arise based on Capital Market Law. The CRSD considers various corporate sector law cases, such as insider trading and conflicts of interest and also contributes to advancing corporate governance practice, since this cannot occur without judicial system support.

4.4. Appeal Committee for the Resolution of Securities Conflict

The Appeal Committee for the Resolution of Securities Conflicts has three members, nominated by the KSA-CM by royal decree. They have three-year terms, which are subject to renewal. Members are often representatives of the Ministry of Finance, Ministry of Commerce and Industry, and the Bureau of Experts at the Council of Ministers (Capital Market Law, 2003, Art. 25 G). Defendants have the right to appeal to this body within 30 days of the

final CRSD verdict. The Appeal Committee for the Resolution of Securities Conflicts has the final verdict since it has the power to uphold or overturn CRSD judgements (CMA, 2011, Art. 39). By allowing listed firms and stock market participants to appeal decisions made by the CRSD, this committee represents an additional layer of corporate governance that benefits the functioning of the stock market.

5. ROLE OF THE ACCOUNTING AND AUDITING PROFESSION AND THE SAUDI ORGANISATION FOR CERTIFIED PUBLIC ACCOUNTANTS

The Saudi Ministry of Finance founded the first accounting and auditing company in 1957 and granted seven licenses for accounting and auditing firms, of which six were foreign and one Saudi. Al-Angari (2004) notes that the accounting and auditing profession in Saudi Arabia lacked specialised knowledge, education, and training, with very few highly skilled and qualified accountants and auditors, which explains the strong presence of foreign accountancy firms. This is because the accounting and auditing profession plays a key role in developing the corporate governance framework in Saudi Arabia as a mechanism for the development and growth of the stock market and economy.

The issues in Saudi accounting and auditing practices arise due to Company Law, which does not include adequate accounting and auditing standards, thus failing to uphold legal clauses for the accounting and auditing profession (Al-Amari, 1989). Therefore, it has been argued that Company Law is a determinant of the weak status of the accounting and auditing profession in Saudi Arabia; this has led to poor corporate governance in terms of weak disclosure and transparency and had a negative effect on the SSE. However, in support of Saudi Company Law, it does require licensed accounting and auditing firms to disclose information such as reputation and members' experience, nationality, and residence. Additionally, Company Law requires firms to submit a financial report to a public chartered accountant and audit firm.¹³ To develop the Saudi audit and accounting systems, in 2003, SOCPA created a committee to evaluate the internal audit committees of listed firms.

The 2006 Saudi stock market crash was partly blamed on the accounting and auditing profession, as professionals were widely considered as failing in their auditing of Saudi firms (Al-Muneef, 2006). The attempts to improve standards in this profession go back to 1992, when SOCPA was created. SOCPA is supervised by the Ministry of Commerce and Industry and is responsible for the development, promotion, and enhancement of auditing and accounting standards and principles. It has thus made recommendations to the boards of listed Saudi firms regarding the non-transparent functions of audit committees and the shortage of satisfactory control functions. It has also suggested that development committees, such as nomination and remuneration committees or risk and audit committees, should be implemented on all firm

¹³ The chartered company has the right to access firm records, demand further information and explanations, and access firm assets and liabilities (Company Law, 1965, Art. 130).

boards. SOCPA notes that many audit committee members of listed firms do not possess the correct accounting or auditing qualifications; coupled with a lack of professionalism, this could have a negative impact on stock market stakeholders and shareholders, as evidenced by the stock market crash of 2006 (SOCPA, 2007).

Recent SOCPA standards draw on both UK and the US experiences and are in line with the best international standards and practice. This has given investors not only the confidence to invest in the Saudi stock market, but also played an important role in the stock market recovery following the 2006 crash. Additionally, SOCPA had a positive impact on firms, particularly in their efforts to achieve growth and, in turn, on the performance of their stocks. This is because, through SOCPA administrative controls and regulations, shareholder equity enabled many firms to avoid bankruptcy caused by losses originating from the stock market crash. In 2015, SOCPA clarified its role in enhancing the financial strength of the Saudi economy, serving its institutions, and providing adequate information. This helps managers and their clients make informed decisions, which ensures continuous good performance and helps achieve their objectives. However, to maintain confidence in the stock market, it ultimately protects the stock market, the rights of shareholders, and the rights of clients. Further, SOCPA helps both the SAMA and CMA in their development and review of accounting standards for listed companies and assists them in decision making on dealings of listed firms. That is, SOCPA acts as an additional tool for the CMA and SAMA while also providing professional services to ensure shareholder rights and the continuing development of the Saudi stock market in line with international accounting standards.

NAAS are based on the US standards and were first issued in 1986. The subsequent developments in these standards laid the foundation for the development of corporate governance in Saudi Arabia. Most listed Saudi firms are required to comply with these standards; although the banking and financial sectors are exempt from these but required to follow IFRS (2017), the standards have a decided impact on listed firms. SOCPA has been responsible for developing and reviewing accounting and auditing standards since 1992. The importance afforded to the NAAS resulted in their playing a crucial role in the development of financial information and the treatment of financial transactions. They include 21 standards for accounting firms and 16 for auditing firms. The 21 accounting standards, as outlined by SOCPA (2017), cover: 1) presentation and public disclosure; 2) foreign currency; 3) commodity inventory; 4) disclosure of transactions with related parties; 5) revenue; 6) administrative and marketing expenses; 7) research and development costs; 8) consolidation of financial statements; 9) investment in securities; 10) initial financial reporting; 11) zakat and income tax; 12) fixed assets; 13) accounting standards for leasing; 14) sectoral reports; 15) accounting standards for investments; 16) intangible assets; 17) accounting standards on government grants; 18) impairment accounting for non-current assets; 19) earnings per share criterion; 20) construction contracts and service; and 21) accounting standards for enterprise assembly operations.

The 16 standards applied to the auditing profession, as stipulated by SOCPA (2015), are: 1) adequate professional qualification; 2) impartiality, objectivity, and independence; 3) professional care; 4) planning; 5) control and documentation; 6) audit evidence; 7) reports; 8) auditing in computer facilities; 9) special reports; 10) audit risk and relative importance; 11) internal audit for the purpose of reviewing financial statements; 12) examination of initial financial reports; 13) samples for review purposes; 14) future financial statements; 15) auditor responsibility for fraud when reviewing financial statements; and 16) confirmation of auditor competence.

6. NATIONAL ANTI-CORRUPTION COMMISSION

In Saudi Arabia, stock market corruption is considered to occur when firms or individuals do not adhere to or follow Capital Market Law or other regulations, such as corporate governance codes, or when they do not explain why they have breached or have not conformed to a specific regulation. Since the development of corporate governance in Saudi Arabia, there have been substantial improvements in reducing the corruption level in the stock market. Saudi regulators have only recently paid attention to getting a firm grasp on corruption as a result of the various corrupt activities by corporations and individuals and in light of the policymakers' focus on attracting international investors for Saudi stocks.¹⁴ Consequently, the NAC was created in 2011 by royal decree to encourage good corporate governance, with the explicit roles of eradicating corruption, protecting integrity in business dealings, and assisting other semi-governmental organisations.¹⁵ NAC reports to Tadawul, CMA, and SAMA and is also empowered to access the bank accounts of suspected managers through SAMA. It has the right to full disclosure, to collate data on the stock market, analyse and monitor companies, and proactively protect shareholder rights and the stock market's integrity. It also investigates weak areas in the Capital Market Law that may lead to corruption and works with agencies such as the SOCPA and CMA to monitor stock market manipulations and those firms and participants that do not uphold the fairness and integrity of the market. It is widely considered that the presence of NAC is a deterrent to those that do not follow the Saudi stock market regulations and thus gives investors confidence.

7. KEY REFORMS IN SAUDI ARABIA

The boom in oil prices in the 1970s and the subsequent increase in oil revenue led to the Saudi government's more central role in the economy. Oil revenue, along with government fiscal expenditure, were key determinants of the Saudi economy's economic development and growth, although the subsequent fall in oil prices in the 1980s prompted the government to promote economic liberalisation and become a member of the World Trade Organisation (WTO). At the same time, the government reduced its involvement in the economy

¹⁴ Corruption can include anything from fraud and bribery to favouritism (Al-Bushra, 2007). Moreover, conflicts of interest and insider trading can be viewed as corrupt activities.

¹⁵ The NAC is associated directly with the King, and even state-owned firms are subject to the corruption commission according to Royal Decree, No. 165, dated May 2, 2011, and NAC Law 2011, Art. 1 and 2.

by reducing subsidies and the privatisation of state-owned enterprises. However, Saudi reforms were very slow, with piecemeal implementation (KSA-CM, 1997; IMF, 2001; Malik, 1999). Most of them took place after 2000; particularly those after 2003 occurred when increased oil prices substantially increased oil revenue. Real gross domestic product (GDP) growth in 2003 was 7.2% and was projected to be even higher in 2004 (IMF, 2005); it was within this period that reforms were most rapid. WTO membership also contributed to the pace of the reform, since it involved greater transparency in trade, the economic environment, and non-resident businesses, all of which were facilitated at the time. Further, WTO membership required reforms that led to the formation of various bodies and administrative structures. For example, the SEC was created in August 1999 to evaluate economic, industrial, agricultural, and labour policies and their effectiveness. Other organisations were created to cover economic policy and the rapid reform agenda; the Supreme Council for Petroleum and Minerals Affairs (SCPM) was created in January 2000 to develop policies on the exploitation of hydrocarbon resources.¹⁶ Its main objective was to attract international investments, starting with natural gas. The Supreme Commission for Tourism (SCT) was established in April 2000 to foster tourism and encourage international investments in tourism, they aim to attract tourism other than that of Muslim pilgrims to holy sites. SAGIA was established in April 2000 to promote a pro-business environment and explore investment opportunities in the energy, transportation, and knowledge-based industries. It also promoted foreign investment and served the business community as a 'one-stop shop' for licences, permits, and other business administrative procedures.¹⁷ As a requirement of its WTO membership, Saudi Arabia reduced import tariffs on agricultural and industrial products for its main trading partner, the European Union (EU) in August 2003 (ICTSD, 2003); the service sector was opened to the EU in areas such as banking, insurance, telecommunications, and construction. At the same time, the US imposed more demands than the EU regarding fuel discounts, intellectual property rights, and financial sector reforms. However, once the US and Saudi Arabia finalised a trade agreement, most of the obstacles that prevented Saudi Arabia from joining the WTO were resolved. Although some critical issues remain, such as giving certain merchants exclusive rights to act as agents of foreign firms, which only serves to restrict competition, the WTO membership allowed Saudi Arabia to expand its markets and improve production efficiency.

7.1. Privatisation

As previously mentioned, the Saudi government commenced its programme of privatisation for state-owned companies in 2000. In 2001, the SEC was made responsible for supervising the privatisation programme, including which firms to

be privatised, and developed strategic plans, a timetable, and monitored and implemented these initiatives. In August 2001, the SEC created the privatisation committee to take control of the process, with members from relevant ministries and economic bodies (KSA-SEC, 2001). In June 2002, the SEC accepted the privatisation strategy of the privatisation committee and, in November 2002, the KSA-CM approved the list of public utilities and activities targeted for privatisation (KSA-MC, 2002). The privatisation process focussed on strategy, a regulatory framework for the privatised sectors, regulatory agencies, systematic methods for setting tariffs for services that were previously subsidised, and procedures for restructuring public enterprises before privatisation. It also brought in strategic partners, particularly for large privatisation projects; helped foster the right business environment for privatisation; and ensured that capital markets functioned properly.

7.2. Foreign investment

Prior to April 2000, foreign investment in Saudi Arabia was only allowed if it satisfied specific conditions: 1) it targeted development projects; 2) it included a transfer of technology; and 3) projects included a Saudi partner with a minimum 25% share.¹⁸ Many licence applications took considerable time to process unless, of course, the partner was the government. SAGIA was required to process investment decisions within 30 days. Before April 2000, foreign firms and investors, except for Gulf Cooperation Council (GCC) citizens, were not permitted to own land or participate in internal trade and distribution activities. However, this changed in June 2000, when the KSA-CM endorsed a new law that would allow SAGIA to facilitate foreign investment by speeding up the decision process, which also reduced the bureaucracy level (SAGIA, 2000). As a result, foreign owners were allowed 100% ownership, except in certain sectors, and domestic and foreign-owned firms faced the same treatment. This means that foreign firms could access cheaper loans from the Saudi Industrial Development Fund (SIDF) on the same terms as Saudi firms: that is, as much as 50% of the investment. Foreign firms could also own land for licensed activities, to house employees, and sponsor and employ non-Saudis.¹⁹ Further, the KSA-CM established the Real Estate Law or 'The System of Real Estate Ownership and Investment of Non-Saudis' as a corollary to the Foreign Direct Investment Law, which allows non-Saudis to own property for their private residences (KSA-CM, 2000a). The reform also targeted Saudi nationals holding funds outside of Saudi Arabia by inviting them to invest in Saudi Arabia instead.²⁰

7.3. Tax reform

The measures designed to reform Saudi Arabia's tax system were intended to make Saudi Arabia attractive for both domestic and foreign investors. This was a necessary policy response because, prior to 2000, the level of corporation tax applied to

¹⁶ In May 2015, King Salman established The Supreme Council of the Saudi Arabian Oil Company (Saudi Aramco) to replace the SCPM, which is led by the Crown Prince Mohammad bin Salman.

¹⁷ SAGIA works closely with the SEC, and SCT is a mediator between investors and the government (SAMIRAD, n.d.; Saudi Arabian General Investment Authority Law, 2000, Art. 3).

¹⁸ The Foreign Capital Investment Committee demanded a 51% equity stake for Saudis.

¹⁹ Previously, the Saudi partner was required to hold the land.

²⁰ It is estimated that at least United States Dollars (USD) 650 billion are held outside Saudi Arabia.

foreign firms — as high as 45% — was a hindrance to foreign investments, while it was considerably lower in other GCC countries. At the same time, the corporation tax for Saudi firms was a mere 2.5% in zakat. To reduce this imbalance, with the introduction of the new Corporate Tax Law (KSA-CM, 2004a) in 2000, policymakers reduced the corporation tax applied to foreign firms to 30% and further to 20% in July 2004. However, taxation was higher in the hydrocarbon sector. For instance, both the oil and hydrocarbon production tax rates were set at 85%, while the rate was 30% for the natural gas sector. However, it is still considered too high in comparison to other GCC states, such as Bahrain and the United Arab Emirates (UAE), where no corporate tax exists. Therefore, it is unlikely foreign firms will shift their operations to Saudi Arabia from other GCC states under the current tax regime.

In any case, the tax law and regulations in Saudi Arabia are now much clearer, which may enhance the confidence of both domestic and foreign investors.²¹ In 2017, further tax reforms were adopted for oil and hydrocarbon sector investments, reducing tax rates by investment level as follows. On investments below Saudi Arabian Riyal (SAR) 225 billion, the 85% tax rate continues to apply, while the rate for investments between SAR 225 and 300 billion was 75%, the rate for investments between SAR 300 and 375 billion was 65%, and the rate for investments above SAR 375 billion was 50%. Furthermore, in 2018, tax reforms in the gas sector ensured taxation levels reached 20%.

7.4. Intellectual property rights

In June 2003, the KSA-CM approved a new Copyright Law, which went into effect six months after it was proposed and is designed to protect intellectual property rights for literature, computer programmes, arts and sciences, audio recordings, and visual displays (KSA-CM, 2003). In July 2004, the KSA-CM passed a new Patent Law, which covers integrated circuits, plant varieties, and industrial design (KSA-CM, 2004b), changes that are consistent with the requirement of WTO's Agreement on Trade Related Aspects of Intellectual Property Rights (TRIPS).

8. CAPITAL MARKETS

The SSE has a short history and initially functioned without any formal regulatory framework. In fact, it was possible to trade shares via national security depository centres without any investor protection. The Capital Market Law, which went into effect in July 2003, formally established the SSE as regulated by the Saudi Arabian Securities and Exchange Commission. This has been known since July 2004 as SACMA or CMA and oversees the operation of the SSE, including its organisation (i.e., ensuring efficient and transparent transactions and monitoring all aspects of trade securities), and protects investors from unfair practices.²² Until recently, trading on the SSE was limited to GCC citizens, while non-GCC investors could only trade in the mutual funds offered by Saudi Banks.

In 2007, developments in corporate governance regulation led to the reform of the SSE to enhance the growth of the Saudi economy, and it was

renamed Tadawul. Tadawul is self-regulated and governed by board members nominated by the CMA from key sectors and governmental bodies (Capital Market Law, 2003, Art. 22 B). The privatisation programme of the Saudi government led to the listing of many public, private, and family companies on the stock market, which led to the growth of the SSE. More recently, stock market regulations have been relaxed to allow foreign investments. This means that Tadawul is open to foreign ownership, although some restrictions still exist.²³

The stock exchange's main contribution to the development of corporate governance in Saudi Arabia relates to: 1) its contribution towards imposing general meetings; 2) ensuring shareholders' voting rights are enforced fairly; and 3) ensuring the rights of minority shareholders. The stock exchange is also responsible for various other targets linked to corporate governance practices, such as guaranteeing listing requirements, ensuring transaction impartiality, undertaking transparency requirements, certifying technical mechanisms and information for listed firms, resolving disputes, and approving regulations (Capital Market Law, 2003, Art. 20 C). On November 12, 2006, the CMA Board issued the Corporate Governance Code, which primarily targets good corporate governance principles that are broadly consistent with those of international organisations and their members, such as the OECD or the UK (Riyadh Chamber of Commerce and Industry, 2007, p. 40).

At the micro-level of the SSE, Tadawul and NASDAQ undertook a joint project in 2014 to replace the SAXESS trading platform with NASDAQ's X-Stream INET Trading. The new platform was launched in September 2015 as the latest in trading solutions and the fastest recorded trading platform. It reduces the chance of errors and fraud, thereby guaranteeing a more secure trading environment. The changes implemented by Tadawul have thus far contributed to the SSE's development and increased investor confidence in the regulatory framework.

In June 2015, Saudi Arabia opened its stock market to foreign investors, who were previously only allowed to invest through exchange-traded funds (ETFs) and participatory notes. This change can be explained by the country's desire to diversify its economy away from oil, giving companies the opportunity to improve corporate governance and thereby attract experience into the stock market. However, despite these changes, some restrictions still applied; for example, only institutional investors with at least USD 5 billion in assets under management and at least five years of experience were allowed to participate in the Saudi market. This threshold was reduced to USD 500 million in 2018. All foreign investors combined can own as much as 49% of a single stock, while ownership of any single foreign investor in one company is capped at 5%. There is a 20% ceiling for all qualified foreign investors in any stock holding. Moreover, all qualified foreign investor holdings must not exceed 10% of the entire market. According to the CEO of the SSE, Adel Al-Ghamdi, 'nothing is set in stone' and 'will evolve as we go forward'. It has been argued that the rationale for such restrictions is the need to reduce market volatility by attracting institutional investors with long-term aspirations. Qualified foreign investors and their clients can vote in

²¹ In 2018, Saudi Arabia established a 5% value added tax (VAT).

²² www.cma.org.sa

²³ However, the SSE is perhaps more stable and secure than it has ever been.

meetings and elect board members that is expected to improve corporate governance in Saudi Arabia (Hankir, & El Baltaji, 2015).

8.1. Insurance sector

Although the Saudi insurance sector is perhaps the largest in the GCC, its regulation by SAMA only begun in July 2003. The insurance sector was opened to foreign investors in 2007 (SAMA, 2007). However, in 2004, a legal framework for insurance companies to operate was created. There was only one Saudi insurance company at that time, but by the end of 2008, there were 21 insurance firms operating in the country (SAMA, 2008). Currently, there are 33 insurance companies listed on the SSE.

9. CONCLUSION

This study has provided an overview of the evolution and development of corporate governance in Saudi Arabia by highlighting the key reforms that have taken place from the discovery and export of oil to the formation of new bodies such as the SAMA, SEC, SAGIA, SCT, and CMA, which helped develop and establish sound policies and practices with a resounding effect on Saudi corporate life. Additionally, the country's WTO membership was a necessary impetus for corporate governance changes through the adoption of internationally accepted principles for good corporate governance; these helped provide standards related to disclosure, transparency, and accountability in the development of corporate governance in Saudi Arabia. The role of Saudi Arabian law in shaping good corporate governance was also important, as it adapted elements of the UK and the US good corporate governance practices such as those related to adapting international accounting standards to

the Islamic framework. The key developments were the Company Law (1965), shareholder rights, company internal control, NAAS, Capital Market Law, and the corporate governance codes. The study also provided a brief overview of the legal system and key institutions responsible for shaping the corporate governance framework, such as the central bank (SAMA), the Ministry of Commerce and Industry, CMA, CRSD, and the Appeal Committee for the Resolution of Securities Conflicts. SOCPA and the accounting and auditing profession were then considered, followed by a short discussion of the NAC. This study also identified the key reforms in Saudi Arabia, with a focus on privatisation, foreign investment, tax, intellectual property rights, and capital market. Finally, the study examined the role of the SSE and insurance sector in the development of Saudi corporate governance.

This research was carried out in Saudi Arabia, an emerging market, for several compelling reasons. First, most of the previous research studies on corporate governance and firm performance issues have been limited to those of developed or large emerging economies. Second, small economies, such as those of Middle East countries and more specifically Saudi Arabia, suffer from a significant lack of study. Third, non-listed firms are not obligated to disclose corporate governance information, so the period before they are listed is shrouded in mystery, and it is not possible to know whether the firm applied the corporate governance code. To date, there is a lack of studies investigating the following: authorities and responsibilities, subcommittees, the legal system in Saudi Arabia, and its impact on corporate practices. Therefore, this study was an attempt to bridge this gap by considering development, external governance, and key reforms.

REFERENCES

1. Aguilera, R. V., & Jackson, G. (2003). The cross-national diversity of corporate governance: Dimensions and determinants. *The Academy of Management Review*, 28(3), 447-465. <https://doi.org/10.2307/30040732>
2. Al-Amari, S. R. (1989). *The development of accounting standards and practices in the Kingdom of Saudi Arabia* (Doctoral thesis, University of Glasgow). Retrieved from <http://theses.gla.ac.uk/77956/1/10999274.pdf>
3. Al-Angari, H. A. (2004). *Auditing in the Kingdom of Saudi Arabia*. Jeddah, Saudi Arabia: Sarawat.
4. Al-Bushra, M. A. (2007). *Corruption and organised crime*. Retrieved from <https://repository.nauss.edu.sa/bitstream/handle/123456789/54307/978-9962-8-8.pdf?sequence=1>
5. Al-Dubai, S. A. A., Ismail, K. N. I. K., & Amran, N. A. (2015). Are family members expropriated-monitoring shareholders? Non-linear evidence from the Saudi Arabia. *Jurnal Pengurusan*, 44, 57-65. <https://doi.org/10.17576/pengurusan-2015-44-06>
6. Al-Ghamdi, M., & Rhodes, M. (2015). Family ownership, corporate governance and performance: Evidence from Saudi Arabia. *International Journal of Economics and Finance*, 7(2), 78-89. <https://doi.org/10.5539/ijef.v7n2p78>
7. Alghamdi, S. A. L. (2012). *Investigation into earnings management practices and the role of corporate governance and external audit in emerging markets: Empirical evidence from Saudi listed companies* (Doctoral thesis, Durham University). Retrieved from [http://etheses.dur.ac.uk/3438/1/SALIM_ALGHAMDIL\(2012\)PDF.pdf?DDD2+](http://etheses.dur.ac.uk/3438/1/SALIM_ALGHAMDIL(2012)PDF.pdf?DDD2+)
8. Al-Ghamdi, S. A., & Al-Angari, H. A. (2005). The impacts of implementing quality review program on audit firms in the Kingdom of Saudi Arabia: An empirical study. *Journal of King Abdulaziz University: Economics and Administration*, 19(2), 187-224. Retrieved from https://www.kau.edu.sa/Show_Res.aspx?Site_ID=320&LNG=EN&RN=51721
9. Al-Harkan, A. A. M. (2005). *An investigation into the emerging corporate governance framework in Saudi Arabia* (Doctoral thesis, Cardiff University). Retrieved from <https://ethos.bl.uk/OrderDetails.do?uin=uk.bl.ethos.434006>
10. Alhumoudi, H. Y. (2016). Corporate governance mechanisms and firms' performance: An empirical analysis of firms listed on the Saudi Stock Exchange. *International Journal of Accounting and Financial Reporting*, 6(2), 101-145. <https://doi.org/10.5296/ijaf.v6i2.9192>
11. Al-Janadi, Y., Abdul Rahman, R., & Omar, N. H. (2013). Corporate governance mechanisms and voluntary disclosure in Saudi Arabia. *Research Journal of Finance and Accounting*, 4(4), 25-35. Retrieved from <https://pdfs.semanticscholar.org/78a9/b2f1c40016eb14c19f092c52e919c18f5065.pdf>

12. Al-Matari, Y. A., Al-Swidi, A. K., Bt Fadzil, F. H., & Al-Matari, E. M. (2012). Board of directors, audit committee characteristics and performance of Saudi Arabia listed companies. *International Review of Management and Marketing*, 2(4), 241–251. Retrieved from <http://www.econjournals.com/index.php/irmm/article/view/303>
13. Al-Muneef, I. A. (2006). *Corporate governance functions, duties and responsibilities of the board of directors*. Retrieved from https://library.nauss.edu.sa/cgi-bin/koha/opac-detail.pl?biblionumber=18590&query_desc=Provider%3A%D8%A7%D9%84%D9%85%D8%AF%D9%8A%D8%B1%D8%8C
14. Amin, A. A., & Hamdan, A. M. (2018). Evaluating the effect of ownership structure on firm performance: Evidence from Saudi Arabian listed companies. *Journal of Economic Cooperation and Development*, 39(3), 65–92. Retrieved from <https://www.sesric.org/pdf.php?file=ART16072601-2.pdf>
15. Belkhir, M., Maghyreh, A., & Awartani, B. (2016). Institutions and corporate capital structure in the MENA region. *Emerging Markets Review*, 26, 99–129. <https://doi.org/10.1016/j.ememar.2016.01.001>
16. Berg, A. S., & Di Benedetto, P. (2009). *Corporate governance country assessment: Kingdom of Saudi Arabia* (World Bank Report on the Observance of Standards and Codes (ROSC) No. 62577). Retrieved from <http://documents.worldbank.org/curated/en/838731468106752813/pdf/625770WPOROSC000Box0361486B0PUBLICO.pdf>
17. Bolbol, A. A., & Omran, M. M. (2005). Investment and the stock market: Evidence from Arab firm-level panel data. *Emerging Markets Review*, 6(1), 85–106. <https://doi.org/10.1016/j.ememar.2004.09.005>
18. Buallay, A., Hamdan, A., & Zureigat, Q. (2017). Corporate governance and firm performance: Evidence from Saudi Arabia. *Australasian Accounting, Business and Finance Journal*, 11(1), 78–98. <https://doi.org/10.14453/aabfj.v11i1.6>
19. Capital Market Authority (CMA). (2003). *Capital Market Law*. Retrieved from CMA website: <https://cma.org.sa/en/RulesRegulations/CMALaw/Pages/default.aspx>
20. Capital Market Authority (CMA). (2006). Corporate governance regulations in the Kingdom of Saudi Arabia. Retrieved from European Corporate Governance Institute (ECGI) website: https://ecgi.global/sites/default/files/codes/documents/cg_regulations_saudi_arabia_nov2006_en.pdf
21. Capital Market Authority (CMA). (2011). *The resolution of securities disputes proceedings regulations*. Retrieved from CMA website: https://cma.org.sa/en/RulesRegulations/Regulations/Documents/RSDPR_en.pdf
22. Capital Market Authority (CMA). (n.d.a). *Capital market authority*. Retrieved from CMA website: <https://cma.org.sa/en/AboutCMA/Pages/AboutCMA.aspx>
23. Capital Market Authority (CMA). (n.d.b). *Organization structure*. Retrieved from CMA website: https://cma.org.sa/en/AboutCMA/CMA_Department/Pages/default.aspx
24. Falgi, K. I. (2009). *Corporate governance in Saudi Arabia: A stakeholder perspective* (Doctoral thesis, University of Dundee). Retrieved from https://discovery.dundee.ac.uk/ws/portalfiles/portal/1253522/Falgi_phd_2009.pdf
25. General Secretariat of the Committees for Resolution of Insurance Disputes and Violations. (1965). *Company Law* Retrieved from <https://www.idc.gov.sa/en-us/RulesandRegulations1/The%20saudi%20Companies%27%20Law.pdf>
26. Habbash, M. S., & Bajaher, M. S. (2015). An empirical analysis of the impact of board structure on the performance of large Saudi firms. *Arab Journal of Administrative Sciences*, 22(1), 91–105. <https://doi.org/10.34120/0430-022-001-005>
27. Hankir, Z., & El Baltaji, D. (2015, June 15). What investors need to know as Saudi stocks open up to the world. *Bloomberg*. Retrieved from <http://www.bloomberg.com/news/articles/2015-06-14/why-mideast-stock-markets-will-never-be-the-same-after-monday>
28. Heenetigala, K., & Armstrong, A. F. (2011). The impact of corporate governance on firm performance in an unstable economic and political environment: Evidence from Sri Lanka. In *Proceedings from 2012 Financial Markets & Corporate Governance Conference*. <https://doi.org/10.2139/ssrn.1971927>
29. Hussainey, K., & Al-Nodel, A. (2008). Corporate governance online reporting by Saudi listed companies. In *Research in Accounting in Emerging Economies: Vol. 8. Corporate Governance in Less Developed and Emerging Economies* (pp. 39-64). [https://doi.org/10.1016/S1479-3563\(08\)08002-X](https://doi.org/10.1016/S1479-3563(08)08002-X)
30. International Centre for Trade and Sustainable Development (ICTSD). (2003, September 25). EU trade deal brings Saudi Arabia closer to WTO membership. *BRIDGES*, 7(31), pp. 5-6. Retrieved from ICTSD website: <http://www.ictsd.org/sites/default/files/review/bridgesweekly/bridgesweekly7-31.pdf>
31. International Financial Reporting Standards (IFRS). (2017). *Who uses IFRS standards? Saudi Arabia*. Retrieved from <https://www.ifrs.org/use-around-the-world/use-of-ifrs-standards-by-jurisdiction/saudi-arabia/#application>
32. International Monetary Fund (IMF). (2001). IMF concludes 2001 article IV consultation with Saudi Arabia (Public information notice No. 01/119). Retrieved from IMF website: https://www.imf.org/en/News/Articles/2015/09/28/04/53/pn01119#P29_350
33. International Monetary Fund (IMF). (2005). *IMF concludes 2004 article IV consultation with Saudi Arabia* (Public information notice No. 05/3). Retrieved from IMF website: <https://www.imf.org/en/News/Articles/2015/09/28/04/53/pn0503>
34. Kim, H. (2010). Does corporate governance or transparency affect foreign direct investment? *International Journal of Economics and Management Engineering*, 4(7), 1694-1701. Retrieved from <https://publications.waset.org/11894/does-corporate-governance-or-transparency-affect-foreign-direct-investment>
35. Kingdom of Saudi Arabia, Council of Ministers (KSA-CM). (2000a) *Law of real estate ownership and investment by non-Saudis*. Retrieved from <https://old.boe.gov.sa/ViewSystemDetails.aspx?lang=en&SystemID=92&VersionID=109#search1>
36. Kingdom of Saudi Arabia, Council of Ministers (KSA-CM). (2000b). *Statute of the General Investment Authority*. Retrieved from <https://old.boe.gov.sa/ViewSystemDetails.aspx?lang=en&SystemID=51&VersionID=61&languageid=2>
37. Kingdom of Saudi Arabia, Council of Ministers (KSA-CM). (2003). *Copyright law 2003*. Retrieved from <https://old.boe.gov.sa/ShowPDF.aspx?filename=4a615e64-b651-4b8c-a2e0-4241d27cef1&SystemID=16&VersionID=24>
38. Kingdom of Saudi Arabia, Council of Ministers (KSA-CM). (2004a). *Income tax law 2004*. Retrieved from <https://old.boe.gov.sa/ViewSystemDetails.aspx?lang=en&SystemID=198&VersionID=215#search1>
39. Kingdom of Saudi Arabia, Council of Ministers (KSA-CM). (2011). *Statute of The National Anti-Corruption Commission*. Retrieved from <https://old.boe.gov.sa/ViewSystemDetails.aspx?lang=en&SystemID=285&VersionID=265#search1>

40. Kingdom of Saudi Arabia, Council of Ministers (KSA-MC). (2002). *The list of public utilities and activities targeted for privatisation*. Retrieved from <http://www.ncar.gov.sa/Documents/Details?Id=bH2BCPWaWabCwX2a8zO5aQ%3D%3D>
41. Kingdom of Saudi Arabia, Council of Ministers. (KSA-CM). (1997). *Privatisation and policies. Decision No. 60*. Retrieved from <http://www.ncar.gov.sa/Documents/Details?Id=%2BMhx3cE4Z4UrsLEOZo1dg%3D%3D>
42. Kingdom of Saudi Arabia, Council of Ministers. (KSA-CM). (2004b). *The patent law 2004. Decision No. M/28*. Retrieved from <http://www.ncar.gov.sa/Documents/Details?Id=9PtZU%2Be5VX3bD3Je6VN7yA%3D%3D>
43. Kingdom of Saudi Arabia, Supreme Economic Council (KSA-SEC). (2001). *Privatisation objectives and policies*. Retrieved from <https://www.mafhoum.com/press3/112E15.htm>
44. Koraytem, T. (2000). The Islamic nature of the Saudi regulations for companies. *Arab Law Quarterly*, 15(1), 63-69. <https://doi.org/10.1163/A:1006744924328>
45. Malik, M. (1999). *The private sector and the state in Saudi Arabia* (Doctoral thesis, Durham University). Retrieved from <http://etheses.dur.ac.uk/1651/1/1651.pdf?ETHOS>
46. Market authority: 96% application of mandatory rules of governance in listed companies. (2011, February 1). *Aleqt Newspaper*, No. 6322. Retrieved from http://www.aleqt.com/2011/02/01/article_498736.html
47. Moustafa, M. E. (1985). Framework for the role of accounting in the economic development in Saudi Arabia. In V. K. Zimmerman (Ed.), *The recent accounting and economic developments in the Middle East* (pp. 197-211). Urbana-Champaign, IL, the USA: University of Illinois.
48. Riyadh Chamber of Commerce and Industry. (2007). *Corporate governance: The definition, the principles, and the Saudi experience*.
49. Saudi Arabia General Investment Authority (SAGIA). (2000). *Foreign direct investment law 2000*. Retrieved from <https://old.boe.gov.sa/ViewSystemDetails.aspx?lang=en&SystemID=50&VersionID=60#search1>
50. Saudi Arabian Market Information Resource (SAMIRAD). (n.d.). *Supreme economic council*. Retrieved from SAMIRAD website: www.saudinf.com/main/e111.htm
51. Saudi Arabian Monetary Agency (SAMA). (2007). *The Saudi insurance market survey report*. Retrieved from SAMA website: http://www.sama.gov.sa/en-US/Insurance/Publications/Sur_4600_R_InsuaMarketSurvey2007_En_2008_06_04_V1.pdf
52. Saudi Arabian Monetary Agency (SAMA). (2008). *The Saudi insurance market survey report*. Retrieved from SAMA website: http://www.sama.gov.sa/en-US/Insurance/Publications/Sur_4600_R_InsuaMarketSurvey2008_En_2009_05_16_V1.pdf
53. Saudi Arabian Monetary Agency (SAMA). *Saudi Arabian Monetary Agency*. www.sama.gov.sa
54. Saudi Organisation for Certified Public Accountants (SOCPA). (2007). *The annual report of the Saudi Organisation for Certified Public Accountants*. Retrieved from SOCPA website: <https://socpa.org.sa/SOCPA/files/09/09ad5f21-1556-428b-96f2-0d635a49e14e.pdf>
55. Saudi Organisation for Certified Public Accountants (SOCPA). (2015). *Auditing standards*. Retrieved from SOCPA website: <https://socpa.org.sa/Socpa/Technical-Resources/Auditing-Standards.aspx>
56. Saudi Organisation for Certified Public Accountants (SOCPA). (2017). *Accounting standards*. Retrieved from SOCPA website: <https://socpa.org.sa/Socpa/Technical-Resources/Accounting-Standards.aspx>
57. Saudi Stock Exchange (TADAWUL). *Saudi Stock Exchange*. www.tadawul.com.sa
58. Shleifer, A., & Vishny, R. W. (1997) A survey of corporate governance. *The Journal of Finance*, 52(2), 737-783. <https://doi.org/10.1111/j.1540-6261.1997.tb04820.x>