The Evolution of Corporate Governance and Consequent Domestication in Kenya

Rita Ruparelia

Amos Njuguna

Chandaria School of Business
P.O Box 14634-0800
Nairobi

Abstract

Governance determines the exercise of power in the management of economic and social resources for sustainable human development. Corporate governance is vital as it influences growth in financial markets and plays a central role in corporate performance, capital formation, and maximization of shareholder value as well as protection of investors' rights. This paper traces the evolution of corporate governance principles and practices, via the committees that produced the Cadbury Report, Greenbury Report, Hampel Report, Higgs Report and the Combined Code, and in the Organisation for Economic Co-operation and Development (OECD). These developments influenced the introduction and growth of corporate governance principles and best practices in Sub-Saharan Africa and Kenya, ultimately leading to the promulgation of the guidelines on principles of corporate governance for public listed companies in 2002 by the Kenyan Capital Market Authority.

Keywords: Corporate governance, Capital Markets Authority, Capital Markets Act (Cap. 485A)

1.0 Introduction

The word 'Governance' is derived from the Latin word 'Gubernare' which means to rule or steer (Hunt, Diane, Garling, & Sanders, 2008). Initially, governance exclusively referred to the normative framework for exercise of power and acceptance of accountability thereof in the running of kingdoms, regions, and towns. Over the years, it has found significant relevance in the corporate world (Hunt, *et al.*, 2008; Bhavik, 2012). Irrespective of these differences, the importance, and the inherent meaning remains same across the world (Bhavik, 2012). The definitions of corporate governance vary from simple to the more complex definitions that encompass various aspects of corporate governance depending on differences in legal, regulatory, institutional, financial, and political framework, status of the capital market, and stakeholder's perception, among other things (Bhavik, 2012).

Corporate governance is a "the system by which companies are directed and controlled" (Cadbury, 1992) so as to protect the interest of all stakeholders and ensure reasonable return on investments (Sullivan, 2009). When a corporation is understood as an association of explicit and implicit contracts, corporate governance can be defined as "a socially constructed force of field of driving and preventing forces that shape a firm's strategic behavior (Carney & Gedalovic, 2001, p. 337). Corporate governance is also defined as a structure in which managers at the top of the organization are controlled by the board of directors, who control the managers through a corporate structure, executive incentives, and an assortment of tools for monitoring the performance of organizational functions (Donaldson, 1990, 2008).

On the other hand, Shleifer and Vishny (1997) define it in terms of how the suppliers of finance in a company assure themselves that the organization is controlled and monitored in such a way that they will get a return on their investment (p. 737). From this definition, it is clear that corporate governance encompasses the authority to direct, organize, and control the corporate entity. It relates to the relationship between the legitimate stakeholders in a firm and makes certain that there is appropriate direction in the company for reasonable return on investments (Abdul-Qadir & Kwanbo, 2012). The corporate governance structure of the firm specifies how the rights and responsibilities of various participants are distributed in the corporation.

The board, managers, shareholders and all other stakeholders are guided by specific rules and procedures for making decisions on corporate affairs (Abdul-Qadir & Kwanbo, 2012).Corporate governance is defined by the Organisation for Economic Co-operation and Development (OECD) as “the system by which business corporations are directed and controlled. The corporate governance structure specifies the distribution of rights and responsibilities among different participants in the corporation, namely; board of directors, shareholders and other stakeholders and spells out the rules and procedures for making decisions on corporate affairs” (OECD, 2004). By doing this, it also provides the structure through which the company objectives are set and the means of attaining those objectives and monitoring performance.

This is the most comprehensive definition that is accepted by most of the countries and multilateral organizations like the World Bank Group (WB), the United Nations (UN), and the Basel Committee for Banking Supervision (BCSB), the International Organization of Securities Commission (IOSCO), the Asian Development Bank (ADB), the Islamic Financial Services (IFS). To this end, corporate governance is concerned with the processes, systems, practices, and procedures that govern institutions. It is also concerned with the resolution of collective action problems among dispersed investors and the reconciliation of conflicts of interest between various corporate claim holders, corporate governance rules can be seen as the outcome of the contracting process between the various principals or constituencies and the Chief Executive Officer (CEO) (Becht *et al*, 2005).

The purpose of the paper is to analyze historical development of corporate governance, with specific reference to the sequential development of corporate governance in the United Kingdom, OECD, Sub-Saharan Africa, and Kenya. The paper analyzes the nature of corporate governance guidelines and practices introduced in each epoch from pre-1900s to the 21st Century.

2.0.The Evolution of Corporate Governance

The foundation of corporate governance can be traced to the pioneering work of Berle and Means (1932) who observed that once modern corporations have grown to very large sizes, they could establish a separate system of control from that of direct ownership. This observation created interest in the behavioral dimension of firms. As a term, governance, originated from the work of Chaucer, where ‘governance’ was associated with being “wise and responsible,” or doing that which is appropriate. When applied to companies, governance, from its Latin root ‘Gubernare’ means to steer (Cadbury, 1992).

Corporate governance is not a recent historical development. While the concept is often presented as a new development, various mechanisms for controlling executive actions have existed since the rise of the corporation (Cadbury, 2002). One of the main drivers in the evolution of corporate governance over the centuries remains corporate failures and systemic crises. The first of these is the South Sea Bubble financial crisis reported in the 1700s that lead to the legislation of new business laws and practices in England. These laws targeted financial mismanagement identified as the main cause of corporate failures. This created the foundation for the changes which would follow the 1929 stock market crash in the United States. In the 1970s, there was a secondary banking crisis in the United Kingdom, the 1980s saw the savings and loans crisis in the United States, and the mid-1990s was marked by the East-Asian economic crises (Flannery, 1996).

Corporate governance gained prominence in the 1980s and 90s due to stock market crashes and general corporate failure across the world (Dagli, Eyuboglu, & Ayadin, 2012). Cutting & Kouzim, 2000) notes that these crises led to the realization that for managers to run effectively and in the right direction, there must be an effective board (Gompers, Ishii, & Metrick, 2003). A long history of company failures such as the collapse of Bank of Credit and Commerce International, Enron, WorldCom, and Parmalat among others also created renewed focus on corporate governance (La Porta, *et al.*, 1999). For example, at Enron, its meteoric growth was fueled by a landmark regulation in the United States that deregulated the electrical power market. This legislation opened the way for Enron to engage in electricity trading and collection of substantial margins from the differences in wholesale and retail prices between States. By 1994, Enron had grown into one of the biggest companies in the world with revenue of nearly $9 billion and net income of $453 million (Aebi, Sabato, & Schmid, 2011). However, the company engaged in fraudulent accounting practices by misstating its income and equity value by billions of dollars. The company also created several partnership agreements with companies it had created and used these partnerships to hide huge debts and heavy losses on its trading businesses.

This was exacerbated by the fact that the auditor was complicit in perpetrating the fraudulent activities by neglecting to recognize the company's problems. When Enron declared bankruptcy in 2001, thousands of people were thrown out of work and thousands of investors lost billions. These developments created the necessity for corporate governance reform to minimize economic risks and foster public and investor confidence in the financial market, develop appropriate risk management structures and techniques in financial organizations, and improve financial risk management and financial performance (Aebi, Sabato, & Schmid, 2011; OECD, 2009).

In recent years, the collapse of Lehman Brothers Holdings during the 2008-2009 financial crisis exposed weaknesses in the corporate governance structure even in large corporate entities (Aebi, Sabato, & Schmid, 2011). Investigations have attributed the collapse of these companies to corporate governance failures, corporate incompetence, and financial fraud and abuse. Most importantly, they provided the opportunity for reforms and revolution in the laws and practices governing corporate governance (Iskander & Chamlou, 2000). The evolution of corporate governance has been summarized in Table 1.

Table 1: Overview of the Evolution of Corporate Governance

Year	Evolution of Corporate Governance
Corporate Governance Globally	
Pre-1900	The origin of corporate governance can be traced to the creation of the registered company under the Joint Stock Companies Act of 1844 (UK). This marked the beginning of the modern corporation that separates control from ownership (Berle & Means, 1967)
	Corporate governance frameworks began developing to protect firms from the actions of professional managers with the passage of the Limited Liability Act of 1855 (UK) to protect shareholders from debt beyond their investment (Parker *et al*, 2002).
1980s	Corporate governance gains prominence in the 1980s due to stock market crashes across the world and inability of corporate governance frameworks to prevent corporate failures (Francis, 2000)
1990s	Different corporate governance structures are adopted across the world. • Countries that followed civil law (such as France, Germany, Italy, and Netherlands) developed frameworks that focused on stakeholders (Solomon & Solomon, 2004) • Countries that followed common law (such as USA, UK, Canada, Australia and New Zealand) developed frameworks that focused on shareholders returns/interests (Department of Treasury).
1997	Commonwealth Heads of Government develop the International Corporate Governance Network to promote and coordinate research and development in corporate governance.
1999	Commonwealth Heads of Government establishes Commonwealth Association for Corporate Governance (CACG), which developed CACG Guidelines – Principles for Corporate Governance in the Commonwealth
1999	Global Corporate Governance Forum was developed by the World Bank Group and OECD.
Corporate Governance in Sub-Saharan Africa	
1990s	The King's Committee Report and Code of Practice for Corporate Governance in South Africa published in 1994 stimulate corporate governance in Africa.
	South Africa, Ghana, and Zimbabwe establish national institutional mechanisms to promote good corporate governance.
	World Bank Group and Commonwealth Association provide training and technical support to Botswana, Mali, Cameroon, Mauritania, Senegal, Sierra Leone, Tunisia, Zambia, Gambia and Mozambique to establish national corporate governance mechanisms
1998,1999, 2000	Regional conferences held in Kampala, Uganda in June 1998 and September 1999 to create awareness and promote regional co-operation in corporate governance. • June 1998 conference: there is a resolution that each member state should develop a corporate governance framework and code of best practice, with particular emphasis on harmonizing frameworks under the East African region by establishing a regional body under East African Cooperation to promote corporate governance. • September 1999 conference: the June 1998 resolutions are re-affirmed and the need for good corporate governance strengthened. • Uganda establishes the Institute of Corporate Governance of Uganda to formulate a national code of best practice for corporate governance. • Tanzania organizes the East African Regional Workshop on corporate governance early in the year 2000. • In Kenya, the Private Sector Initiative for Corporate Governance continues to liaise with Uganda and Tanzania towards the establishment of a Regional Center of Excellence in Corporate Governance.
Corporate Governance in Kenya	
1998, 1999	Consultative Corporate Sector seminars held in November 1998 and March 1999 resolves to establish a Private Sector Initiative for Corporate Governance charged with the responsibility to formulate and develop a code for best practice for corporate governance in the country; exploring ways of establishing a national body for corporate governance; and coordinating developments in corporate governance in Kenya with other initiatives in East Africa, Africa, and globally.
October 1999	The Private Sector Initiative for Corporate Governance develops and adopts a national code of best practice for corporate governance to guide developments in Kenya.
2002	The desire to institutionalize the principles of corporate governance in Kenya led to the promulgation of the Guidelines on Principles of Corporate Governance for Public Listed Companies in 2002 by the Capital Market Authority (CMA)

Various principles, guidelines, and codes have been developed over the past decades around the world. The Western world has greatly influenced the growth in theory and practice of corporate governance. The subsection below presents a comprehensive examination of the main countries that have served as the epicenter for the growth in guidelines and standards and provided the foundation for the development of corporate governance coded in Sub-Saharan Africa and Kenya.

2.1. United Kingdom

The UK has contributed immensely to the research in corporate governance. The UK is the origin of the major committees that began addressing corporate governance issues. The main committees include The Cadbury Report (1992), The Greenbury Report (1995), The Hempel Report (1998), The Higgs Report (2003); and The Combined Code on Corporate Governance (2003).

The Financial Reporting Council, London Stock Exchange and the professional accountancy institutions set up the Committee in May 1991 to assess "The Financial Aspects of Corporate Governance". The Chairman of the committee was Sir Adrian Cadbury, from which the findings "The Cadbury Report" took its name. The main responsibilities of the committee were to outline the responsibilities of executive and independent directors, board audit committees, responsibilities of auditors with respect to the shareholders and the board. The Committee recommended that listed companies at the London Stock Exchange should adopt and comply with the Code of Best Practice. Companies were therefore requested to disclose a statement of compliance/non-compliance with this code in their annual financial statements. Companies were also expected to follow guidelines which called for the establishment of a sound governance structure, and a board of directors to monitor and govern the organization. One of the major recommendations in the report was the need to increase the number of independent non-executive directors, separate the posts and responsibilities of the CEO of the company and the Chairman of the Board, and set up sub-committees in the board with the capacity of monitoring and judging the activities of the management.

The Greenbury Report (1995) came into being in 1995 to examine issues surrounding directors' remuneration arising from public complaints and concerns by shareholders. The report drew its name from the Chair, Sir Richard Greenbury. The Committee developed a Code of Best Practice that was to act as a guidance framework for listed companies to make decisions on director's remuneration. The report recommended the creation of Remuneration Committees in the boards consisting of independent directors to determine both the director remuneration to avoid the potential of interest caused when the directors' pay is set by the management. The board was also required to publish and disclose the remuneration policies guiding the remuneration of executive and non-executive directors as well as the policies guiding how long a director can serve in a company.

In 1998, Sir Ronald Hampel chaired the Committee set up to review the recommendations of the Cadbury Report (1991) and The Greenbury Report (1998). The Committee drew membership from various organizations and individuals. The findings of the committee included a review of the roles of executive directors and non-executive directors, as well as auditing committees and their role in corporate governance. From the review, a list of approximately twenty corporate governance principles were isolated and promoted as being necessary for good corporate governance. These principles encompassed: the specific role of directors, recommendations about board remuneration, shareholders rights and roles, and measures for ensuring accountability and transparency. It also recommended the establishment of clear roles for executive and non-executive directors and reiterated the separation of the CEO from that of the Board Chairman. Finally, it recommended that the process of nominating directors, remuneration, and auditing should be driven mainly by independent directors.

In 2003, Derek Higgs was appointed by the UK government to carry out a review of the responsibilities of independent directors. The terms of reference included assessing the population of non-executive directors, the process of appointing non-executive directors, their independence and effectiveness, accountability mechanisms and board remuneration. The review also touched on board effectiveness, with particular emphasis on the association between independent directors and the financial performance of listed firms. The committee generated a final report; "Review of the role and effectiveness of non-executive directors," popularly called the Higgs Report, published in 2003. One of the major recommendations of the review was to establish a clear definition of an independent non-executive director (Solomon & Solomon, 2004). The definition of independence was to take into account relationships that may affect the director's objectivity. Another recommendation was that at least 50% of the board must be independent directors.

Further, the appointment of directors must take into account the concerns of shareholders. The report maintained that the CEO and board chairman should separate. The board should establish a nomination committee charged with the responsibility of evaluating individual directors, the board, and sub-committees annually. Finally, the report recommended that the level of director's remuneration should be sufficient and fair in order to attract highly qualified individuals (Mallin, 2005)

Drawing from the recommendations of The Cadbury Report (1991), The Greenbury Report (1995), The Hampel Report (1998), and The Higgs Report (2003), a combined code was generated in 2003. The main components of the Combined Code of Corporate Governance included the corporate principles of corporate governance; the role of the board and board chairperson; the role of independent directors, and the formation and roles of the audit and remuneration committees. The committee also recommended a revised Code of Principles of Good Governance and Code of Best Practice, in addition to guidelines on the recruitment, appointment, and professional development of non-executive directors, as well as the roles of the various board committees and a performance evaluation checklist.

2.2. Organisation for Economic Co-operation and Development

Many governance problems arise from the separation of ownership and control. Given the pre-eminence given to shareholder rights in corporate law, one of the most important tasks of any corporate governance framework is to ensure the maximization of shareholder value (Aquilera & Cuervo-Cazurra, 2004). In this regard, the best governance mechanism is that which minimizes the agency costs in the system while keeping an optimum balance between power and accountability. A good corporate governance system should provide incentives for the management to freely pursue the objectives of the firm in the interests of the shareholders facilitate monitoring and ensure better firm performance (Aquilera & Cuervo-Cazurra, 2004).

The OECD principles were promulgated in 1999. The aim of these principles was to provide a framework that governments could adopt to improve the legal, institutional, and regulatory framework for corporate governance (OECD, 1999). These principles could also be adopted by stock exchanges, companies, and investors. The OECD principles are not legally binding, and uptake is voluntary, because they only act as a broad-based framework that can be used by a country in developing its own corporate governance codes. Since the principles were published, they have been widely adopted by governments, stock exchanges, and companies. Over the past decade, representatives of 30 countries have played a central role in constantly reviewing the principles to ensure that they are in tune with changing demands in the corporate and regulatory environment.

The principles that were released by OECD in 1999 and they have received worldwide recognition as an international benchmark for sound corporate governance. They have been adopted by governments, regulatory agencies, corporations and shareholders, and investors in OECD and non-OECD countries. The principles have been revised in 2004 and advanced to capture developments since the initial release, and emphasis on shareholder rights and value maximization has been strengthened (Manawaduge, 2012). The reworked principles now cover the foundation of an effective corporate governance framework, shareholder rights, roles of shareholders, and guidelines for ensuring that disclosures are done in an accountable and transparent manner.

2.3. Sub-Saharan Africa

Owing to the effects of corporate governance in promoting the performance of the firm, market, and economy, poor governance has increasingly been cited as one of the most important factors contributing to poor economic performance in most developing countries (Ongore & K'Obonyo, 2011). The World Bank has repeatedly argued that poor economic performance in most developing countries, particularly in Sub-Saharan Africa (SSA), is attributed to poor governance. The issue of governance in Africa was first raised in 1988 in the World Bank report evaluating ten years of structural adjustment lending experience. The report noted that "severe institutional and managerial weaknesses in the public and private sector have proved unexpectedly serious as constraints to better performance" (World Bank, 1988; Kerandi, 2008). The issue of "good governance" was further amplified by the 1989 World Bank report on SSA when the crisis in the region was termed as a "crisis of governance" (World Bank, 1989; Kerandi, 2008). International financial institutions (IFIs) have since then focused on improving the effectiveness of public sector institutions and the performance of public policies. Naim (1999) observed that the rediscovery of institution has become the key focus of IFIs in as far as reforms are concerned. Naim explains that "no speech or policy paper could be written about market reform without including a fashionable reference to the need to strengthen institutions" (Naim, 1999).

International financial institutions have repeatedly justified their involvement in promoting governance in developing countries arguing that it falls directly within their mandate and expertise (IMF, 2002). The International Monetary Fund (IMF) states that it "places great emphasis on good governance when providing policy advice, financial support, and technical assistance to its 184 member countries" (IMF, 2002). On its part, the World Bank says that its fundamental role is to help countries work better and it cannot afford to turn away when "a country is plagued by deeply dysfunctional public institutions that limit accountability, set perverse rules of the game, and are incapable of sustaining development" (World Bank, 2013). Therefore, since the 1990s both multilateral and bilateral donors have factored governance agendas into their financial assistance to developing countries (World Bank, 1997). For example, Santiso (2002) notes that since 1996 World Bank had been actively involved in over 600 governance-related programs in 95 countries and is involved in supporting significant programs of governance and public sector reform in 50 countries. Other donors are also doing the same and thus leading to increased focus in governance agendas for most countries in the SSA region (Grindle, 2004).

Economic globalization has been one of the driving forces behind the major economic reforms in many Sub-Saharan African countries (Asiedu, 2004; Berry, 2009). However, these reforms are still incomplete, particularly from the point of view of foreign investors (Asiedu, 2004). Good corporate governance practices, both at the country and the company level, are regarded as important factors for attracting domestic investment and ensuring greater inflows of foreign direct investment (Claessens, 2006). Thus, to attract investors companies need to implement good corporate governance practices. In other words, company's adherence to good corporate governance practices is thought to be an important factor in investment decisions (OECD, 2004). Owing to these benefits, a number of Sub-Saharan African countries have adopted codes of corporate governance similar to those advocated and used in developed countries. These codes or recommended "best practices" are based on similar codes promoted by organizations (OECD, 2004), private scholars (Shleifer & Vishny, 1997) and practitioners (Cadbury, 1992, Greenbury, 1995). For example, the corporate governance codes of Sub-Saharan African countries such as Nigeria, Kenya, and Ghana recommend that companies have non-executive directors, form audit committees with independent members, and separate the positions of chairperson and chief executive as among of good practices of corporate governance. Many of these corporate governance practices promoted in Sub-Saharan Africa originate from developed countries (Hearn, 2011).

On the contrary, developed countries have, over a long period of time, developed and implemented systems of laws and regulations that govern stock markets and other economic activities (La Porta *et al*., 2008). These systems set the "rules of the game" in the market (North, 1990), and accordingly help different stakeholders to interact with each other more easily. Even though many reforms have been undertaken, Sub-Saharan African countries still have rather undeveloped stock markets, and in most cases the stock markets only opened in the 1990s, except in the cases of Kenya and Nigeria, whose stock markets started trading in 1954 and 1960, respectively. Before the recent economic reforms that opened up the market for private ownership, the distribution of profits to owners was not a major concern. Previously, executives had few incentives to ensure that their companies made a profit and paid dividend; hence, the application of good corporate governance practices was not important, to either the executives or the owners (Munisi & Randoy, 2011).

The enforcement of laws and regulations is regarded as a central issue of good corporate governance practice (Berglöf & Claessens, 2006, La Porta *et al*., 2008). Strong law enforcement reduces the gap in information quality between company insiders and outsiders, which consequently reduces the costs of external financing. Many developing countries, including those in Sub-Saharan Africa, have relatively weak systems of laws and regulations (Rossouw, 2005). Some of these countries lack some of the laws and regulations that would protect the interests of different stakeholders. Even when good laws and regulations exist, enforcement is often relatively poor (Okpara, 2011). Many of these countries are perceived to be highly bureaucratic and corrupt (Kaufmann *et al.*, 2009).

According to the Transparency International Indices, many Sub-Saharan African countries are ranked among the most corrupt countries in the world (Transparency International, 2009). Corruption and bureaucracy alter the effectiveness of legal systems (Deflem, 1995), and particularly the enforcement of laws, even in countries where good laws exist. Poor legal systems hinder the effectiveness of market activities and this leads to low productivity (Lambsdorff, 2003). The existence of weak legal systems and their effects on economic activities have major implications for the types of corporate governance practices that can be applied effectively across Sub-Saharan Africa.

2.4. Kenya

Before liberalization of Kenya‘s economy in the 1990s which institutionalized privatization of government corporations, accountability in the public sector was largely lacking. Lack of accountability in the public sector was replicated in the private sector. Furthermore, inefficiency had been institutionalized (Bebchuck, Cohen, & Ferrell, 2004). This was further compounded by the absence of a corporate governance framework. With senior government officials owning shares in the few publicly held companies, the government was not fervent on enforcing securities laws (Gakeri, 2013). The boards of directors of many listed company consisted of friends, relations and political associates of government officials. The situation was exacerbated by the fact that the NSE was under the control of family owned and managed stock brokers whose driving force was business not regulation. Consequently, the NSE had a cordial relationship with listed companies and seldom invoked regulatory sanctions for non-compliance with listing or membership rules (Gakeri, 2013).

Privatization of government enterprises introduced new dynamics into the market place, for instance, new companies floated securities, and the public subscribed for them with enthusiasm. These companies were subsequently listed on the Nairobi Securities Exchange. The establishment and subsequent inauguration of the Capital Markets Authority (CMA) in 1990 did not fundamentally alter the corporate governance landscape in the country (Mulili & Wong, 2011).The desire to institutionalize the principles of corporate governance in Kenya led to the promulgation of the guidelines on principles of corporate governance for public listed companies in 2002 by the Capital Market Authority (CMA) (Gakeri, 2013; Musikali, 2014).

The guidelines are contained in Gazette Notice No. 3362, The Capital Markets Act (Cap. 485A) which confers the powers to issues the guidelines to the Capital Markets Authority. The guidelines were developed taking into account the work undertaken by various jurisdictions through task forces and committees in the United Kingdom, Malaysia, South Africa, OECD, and the Commonwealth Association for Corporate Governance. CMA has also supported in the development of the code of best practice for corporate governance in Kenya issued by the Private Sector Corporate Governance Trust in Kenya.

The guidelines were developed as a response to the growing importance of corporate governance issues in both emerging and developing economies and for promoting growth in domestic and regional markets. The guidelines recognize the role of good governance in corporate performance, capital formation, and maximization of shareholder value as well as protection of investors’ rights. The primary objective of the guidelines is to strengthen corporate governance practices by public listed companies in Kenya and to promote the standards of self-regulation so as to bring the level of governance in line with international trends. The guidelines are both prescriptive and non-prescriptive to promote creativity and innovative dynamism to corporate governance in listed companies. CMA expects companies to adopt, nurture, and encourage the evolution of practices into best practices, while also expecting that directors must comply with minimum requirements. Therefore, compliance is an essential part of disclosure obligations in corporate annual reports and every listed company is required to disclose, on annual basis, in its annual report, a statement of the directors as to whether the company is complying with corporate guidelines. The guidelines took effect in 2002 as Capital Markets (Securities) (Public Offers, Listing and Disclosures), Regulations, 2002.

The guidelines are divided into two parts: principles of good corporate governance and recommended best practices in corporate governance.

2.4.1. Principles of Good Corporate Governance Practices

The principles of good corporate governance revolve around guidelines governing directors, Chairman and Chief Executive, shareholders, audit and accountability and general practices. The guidelines governing directors are concerned with the establishment of the board and board committees, director’s remuneration, supply and disclosure information, board balance, appointments to the board, multiple directorships, re-election, and resignation of directors. Listed companies are required to establish a board with relevant committee; the audit and nominating committee, among others. Director remuneration should be sufficient to attract and retain directors. Executive director’s compensation should be competitively structured and linked to performance, while non-executive director’s remunerations should be competitive in line with remuneration in competing sectors (CMA, 2002).

The board should, at all times, be supplied with relevant, accurate and timely information to enable it to discharge its duties. The board must also annually disclose in its annual report, its policies for remuneration, including incentives to the board. On board balance, the board should compose of a balance of executive directors and non-executive directors (including at least one third independent and nonexecutive directors) of diverse skills or expertise in order to ensure that no individual or small group of individuals can dominate the boards' decision making processes. On appointments, there should be a formal and transparent procedure for appointment of directors to the board, and disclosure of any potential area of conflict. Directors in the boards of listed companies are required to hold not more than five directorships in public listed companies. Finally, the regulations governing directors also separate the role and responsibilities of the chairman and chief executive to ensure that there is a balance of power of authority and adequate checks and balances. Further, a person holding a chairperson position in a publicly listed company cannot hold such a position in more than two listed companies at the same time (CMA, 2002).

Regulations governing shareholders revolve around the procedures for approving major decisions and annual general meetings. The guidelines note that shareholders must participate in making major decisions in the company. It is the responsibility of the board to provide all shareholders with information on all relevant matters, but not limited to major disposal of the Company's assets, restructuring, takeovers, mergers, acquisitions, or reorganization. The board should also communicate to shareholders all the information on annual general meetings and satisfy the shareholders' demands about the performance of the company. Another important principle is accountability and audit. The guidelines stipulate that the board must present an objective and understandable assessment of the Company's operating position and prospects, in line with International Accounting Standards. Boards in listed companies must establish and maintain a sound system of internal control to safeguard the shareholders investments and assets.

Additionally, the board should establish a formal and transparent arrangement for shareholders to effect the appointment of independent auditors at each annual general meeting; and maintain a professional interaction with the Company's auditors (CMA, 2002).

The general principles concern public disclosures, integrity of chief financial officers of listed firms, company secretaries, and auditors. In summary, there should be public disclosure in respect of any management or business agreements entered into between the Company and its related companies, which may result in a conflict of interest; the Chief Financial Officers and persons heading the accounting department of every issuer shall be members of the Institute of Certified Public Accountants established under the Accountants Act; Company Secretary of every public listed company shall be a member of the Institute of Certified Public Secretaries of Kenya established under the Certified Public Secretaries of Kenya Act; and auditor of a public listed company shall be a member of the Institute of Certified Public Accountants and shall comply with the International Auditing Standards (CMA, 2002).

2.4.2. Recommended Best Practices in Corporate Governance by Public listed companies

The guidelines also list recommended best practices in corporate governance by listed companies revolve around best practices relating to the board of directors, chairman and chief executive, shareholders, conducting general meetings, and accountability and the role of audit committees. The adoption of these practices is essential for public companies in Kenya in order to maximize shareholders value through effective and efficient management of corporate resources (CMA, 2002).

The board of directors has the primary responsibility of fostering long-term business of the corporation and ensuring that it achieves its fiduciary responsibility to shareholders. The board of directors is responsible for defining the mission, strategy, goals, risk policy, and objectives of the firm. They also oversee corporate management and operations, management accounts, major capital expenditures and review corporate performance and strategies at least on a quarterly basis; identify the corporate business opportunities, evaluate business risks, and guide the implementation of appropriate strategies; develop appropriate staffing and remuneration policy; review company's internal control mechanisms; establish information sharing system with shareholders; monitor corporate governance practices; and advance the company's interests at all time(CMA, 2002).

The board should be constituted in such a way that there is a balance between independent, non-executive, and executive directors, with independent and non-executive directors constituting at least one third of the board. The membership of the board should also reflect the company's shareholding structure.

The recommended board size is not defined but it should not be too large to undermine an inter-active discussion during board meetings or too small such that the inclusion of a wider expertise and skills to improve the effectiveness of the board is compromised. Finally, the board should have the ability to monitor and manage potential conflict of interest between the board, management, and shareholders (CMA, 2002).

Regulations also recommend that the board must have a nominating committee, equipped to nominate persons of high calibre, expertise, and credibility to the board. Of importance in the composition is that boards of listed companies should have equitable gender representation and should have a national outlook. Finally, no board member should be a director in more than five listed companies. It is recommended that a remuneration committee be set up to determine remuneration packages that are linked to corporate performance. The board must report consolidated total remuneration of directors in the annual statements of financial performance. On the other hand, audit committees, composed of at least three independent and non-executive directors, should be established to effectively oversee the financial reporting process and ensure that the company has appropriate internal controls (CMA, 2002).

The CMA guidelines recommend that the position for the Chairperson to the board and the Chief Executive of the company should be separate. In case, these positions are combined, there should be a rationale. This can only be justified it the dual role is for a limited in duration and it must be approved by shareholders. The Chairperson must be an independent and non-executive director. The board must establish clear succession plans (CMA, 2002).

On shareholders, the best practices relate to ensuring equitable terms of shareholders, access to relevant information about the corporate performance, security in the transfer and registration of ownership, right to participate and vote at the general shareholders meeting including the election of directors, entitlement to ask questions and seek clarifications on annual reports, and entitlement to distributed profit in form of dividend and other rights for bonus shares, script dividend or rights issue, as applicable and in the proportion of its shareholding in the Company. All shareholders should be encouraged, to participate in the annual general meetings and to exercise their votes. The guidelines further stipulate the best practices for conducting general meetings (CMA, 2002).

3.0.Conclusion

Corporate governance is concerned with the processes, systems, practices and procedures that govern institutions as well as the resolution of collective action problems among dispersed investors and the reconciliation of conflicts of interest between the board of directors, management and shareholders. A strong commitment from the board and the senior management, effective risk control, high level of transparency and disclosure of financial and non-financial information, well defined shareholders rights, effective monitoring of the corporate governance practices and long term commitment to good corporate governance practice, are essential to listed companies in Kenya. Sound corporate governance regimes are a positive development that has the ability to generate positive returns for a company, boost investor confidence, and maximize shareholder returns. Understanding the evolution of corporate governance is therefore an important step in strengthening compliance with corporate governance principles and best practices.

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