THE ROLE OF INSTITUTIONAL SHAREHOLDERS ACTIVISM IN THE CORPORATE GOVERNANCE

BY T-6302

SYEDA SAIMA SHABBIR
Registration No: 185/ LLMCL/ F07F
L.L.M Corporate Law
Faculty of Sharia and Law
International Islamic University
Islamabad.

A thesis submitted in partial fulfillment
of the requirement for the degree of
Masters of Law
Faculty of Sharia and Law
International Islamic University Islamabad
November 2009

Accession No TH6302

Corporate governance -
Share holders activism
Institutional investors

THE ROLE OF INSTITUTIONAL SHAREHOLDERS ACTIVISM IN THE CORPORATE GOVERNANCE

BY

SYEDA SAIMA SHABBIR

Supervised by:

Sir Mohummad Younus
Assistant Professor of Law

Faculty of Sharia and Law
International Islamic University Islamabad

FINAL APPROVAL

It is certified that we have read the dissertation submitted by Mrs. Syeda Saima Shabbir, Registration No 185/LLMCL/ FO7 F, titled "The Role of Institutional Shareholder Activism in Corporate Governance" as a partial fulfillment for the award of degree of LLM (Corporate Law). We have evaluated the dissertation and found it up to the requirements in its scope and quality for the award of degree.

1. Supervisor

   Mr. Mohummad Younus

   (Assistant Professor)

   Faculty of Shariah and Law

   International Islamic University Islamabad.

2. Internal Examiner

   Mr. Attaullah Mehmood

   (Assistant Professor)

   Faculty of Shariah and Law

   International Islamic University Islamabad

3. External Examiner

   Chaudhry Akhtar Ali

   Advocate Supreme Court

   Islamabad.

DEDICATION

This work is dedicated to my sweet father Syed Shabbir Hussain Shah (Judge Anti- Terrorism Court Mardan) may his soul rest in peace, who will always remain my ideal and source of inspiration for me in the legal profession.

Acknowledgment

First of all, I thank Almighty Allah who is the most merciful and most beneficent.

In the preparation of my thesis, I thank Honourable Mr. Justice Sardar Mohummad Raza Khan of the august Supreme Court of Pakistan, who has helped me with his profound knowledge in the field of law and provided me with relevant material on the subject. I also thank my husband Syed Jawwad Hussain who has always supported me after my father's death and never made any hurdle for me in pursuing my studies as well as my career. I felt esteemed to be placed under the kind supervision of my respectable supervisor Col. (Ret) Mohammad Younus, Assistant Professor of Law, Faculty of Sharia and Law International Islamic University Islamabad, whose advice and support enabled me to accomplish my research work.

ABSTRACT

Institutional shareholders activism can play an important role in promoting good corporate governance activities in the listed companies of Pakistan. In developed countries like UK and US, much has been said and much has been done pertaining to the effectiveness of the institutional shareholders activism. However, in Pakistan very less research and work has been done in this respect. The main reason being that in Pakistan share ownership was mainly concentrated in the hands of individual investors whereas in developed countries this share ownership has moved from individual investors to powerful institutions like pension funds, insurance companies and mutual funds etc. This research paper aims at exploring the role of institutional shareholders activism in promoting good corporate governance practices in investee companies.

List of Abbreviations

AGM	Annual General Meeting
CalPERS	California Public Employees' Retirement System
CCG	Code of Corporate Governance
ECGI	European Corporate Governance Institute
FFC	Fauji Fertilizer Company Limited
ICGN	International Corporate Governance Network
ISC	Institutional Shareholders Committee
PKIC	Pakistan Kuwait Investment Company
SECP	Securities and Exchange Commission of Pakistan

Table of Contents **Page No**

THE ROLE OF INSTITUTIONAL SHAREHOLDERS ACTIVISIM IN THE CORPORATE GOVERNANCE.

CHAPTER ONE INTRODUCTION

1.1 Introduction

Institutional shareholders activism can play an important role in promoting good corporate governance activities in the listed companies of Pakistan. In developed countries like UK and US, much has been said and much has been done pertaining to the effectiveness of the institutional shareholders activism. However, in Pakistan very less research and work has been done in this respect. The main reason being that in Pakistan share ownership was mainly concentrated in the hands of individual investors whereas in developed countries this share ownership has moved from individual investors to powerful institutions like pension funds, insurance companies and mutual funds etc. This research paper aims at exploring the role of institutional shareholders activism in promoting good corporate governance practices in investee companies.

"Shareholders are often described as owners of corporations"[1] meaning thereby that owning shares in corporations tantamount to owning any other property. Shareholders being owners of corporations can play their part to discipline an unruly corporate system. Shareholders may be individual investors or institutional investors. "Institutional shareholders can be instrumental as agents of change towards improving corporate governance".[2] Institutional investors as compared to individual investors own large shareholdings in the investee companies and therefore they can have

---

1 A.G. Monks and N. Minow, *Corporate Governance, p.* 98, England: Blackwell Publishing 2004.

2. http://www.secp.gov.pk/divisions/Portal_CS/PDF/WORKING%20PAPER.pdf. (accessed May 4, 2009).

a better say in the managerial affairs of the same. Contrary to this, individual investors/ shareholders owning small shares cannot influence the investee companies' affairs.

The issue of shareholders activism was addressed exhaustively in the developed countries, particularly US and UK, after the occurrence of major corporate scandals like Adelphia, WorldCom and Enron. These major corporate scandals served as an impetus to the promulgation of the Sarbanes-Oxley Act 2002. The said Act is "considered to be the most sweeping corporate governance regulation in the past 70 years and enhancing the long standing bandwagon for increasing the shareholder power".[3] Corporate scandals occurring in strong economies like US and UK, also triggered suspicions and doubts in the corporate environment of developing countries. Pakistan being one of them also felt a need to provide the country with such a legislation that could secure the rights and confidence of stakeholders. Therefore, in the year 2002, the Code of Corporate Governance was issued by the Securities and Exchange Commission of Pakistan (SECP) "....to establish a framework for good governance of companies listed on Pakistan's stock exchanges".[4] After the issuance of the Code, all stock exchanges of the country were directed by the SECP to incorporate the provisions of the Code in their respective listing regulations, which was done accordingly.

Corporate Governance in the broader sense postulates the way in which corporations are governed in accord with "the highest prevailing standards of ethics and efficacy upon assumption that it is the best way to safeguard and promote the interests of

---

3. Moshe Pinto, "The Role of institutional Investors in the Corporate Governance", page 1 (PhD diss., University of Hamburg and Bolonga 2005)

4. http://www.secp.gov.pk/dp/pdf/manual-CG.pdf .(accessed January 24 , 2009).

all corporate stakeholders".[5] Institutional stakeholders \ investors having an influential force can shape the corporate governance of the investee companies by demanding the implementation of these standards of ethics and efficacy. Cadbury Committee (1992) viewed the role of the institutional investors by making the following observation:-

"We look to the institutions in particular.....to use their influence as owners to ensure that the companies in which they have invested comply with the Code".[6] Similarly, Greenbury Report (1995) observed that "The investor institutions should use their power and influence to ensure the implementation of best practice as set out in the Code".[7] On the same lines it was observed in the Hampel Report (1998) that "It is clear.....that a discussion of the role of shareholders in corporate governance will mainly concern the institutions".[8]

The observations made in all these three reports manifestly emphasized the influential role of institutional shareholders pertaining to the enforcement of good corporate governance standards.

In Pakistan the role of institutional investors has increased in the last few decades.[8.1] This research paper aims at exploring the role of institutional shareholder activism from different aspects like encouragement for institutional investor activism, shareholder monitoring, and disclosure of voting policies, proper record of resolutions at Annual General Meeting, appointment of non-executive directors and appointment of external

---

5. Supra note 4.

6. Sir Andrian .Cadbury, *Report of Committee on the Financial Aspects of Corporate Governance* (London : Gee & Co.Ltd., 1992).

7. Sir Richard Greenburry, *Directors Remuneration* (London. : Gee & Co Ltd. , 1995).

8. Sir Ronnie Hampel, *Committee on Corporate Governance: Preliminary Report* (London : Gee & Co .Ltd , 1997).

8.1 Supra note 2.

auditors. The research paper then goes on to discuss the effectiveness of negotiations between the institutional investors and the management, disclosure of beneficial ownership, role of nominee directors on the board. The issue as to whether the legal environment in Pakistan is conducive for institutional shareholder activism has been discussed. The research paper concludes by discussing as to how the Code of Corporate Governance of Pakistan can facilitate/support institutional shareholders.

1.2 History of Shareholders Activism

Shareholders activism is not a novel concept. Its roots were there in the corporate system since long, growing with slow pace. For instance in US , its origin can be traced back to 1900s when the financial institutions like mutual funds , banks and insurance companies were actively participating in US corporate governance. 'But over the next three or four decades, laws passed with the aim of limiting the power of financial intermediaries also prevented them from having an active role in corporate governance.'[9] "The Glass Steagall Act prohibited U.S. banks from owning equity directly. And the regulatory reforms that followed the stock market crash of 1929 limited the liquidity of, and otherwise raised the costs to, investors of active participation in corporate affairs. The consequence of such laws and regulations was a progressive widening of the gap between ownership and control in large U.S. public companies—a process that continued until the emergence of corporate raiders and Labour organisations in the 1980s".[10]

The Securities and Exchange Commission was established in the US under the Security

---

9. M. Roe, Political and Legal Restraints on Ownership and Control of Public Companies, pp .7-41, Journal of Financial Economics 27, (1990).

10. A Bhide., Efficient markets, Deficient Governance: U.S. Securities Regulations Protect Investors and Enhance Market Liquidity. But Do They Alienate Managers and Shareholders? pages 128-140, Harvard Business Review 72, , 1990.

and Exchange Commission Act 1934. The main purpose of creation of the Security and Exchange Commission was "to restore investor's confidence in capital markets by providing investors and the markets with more reliable information and clear rules of honest dealing."[11] The Securities and Exchange Act also introduced provisions whereby shareholders were allowed to submit their respective proposals for inclusion on corporate ballots. "From 1942 through the end of the 1970s, shareholders activism was dominated by individual investors."[12] The role of institutional investors gained prominence in the 1980s when the public pension funds got actively involved in demanding the protection of their rights as investors. Later years witnessed the dominant role of labour union pension funds, banks, insurance companies as activist institutional investors.

Like US, in UK as well institutional shareholders activism evolved when the share ownership came to the hands of large institutions. The role of institutional investors was recognized by different corporate governance codes and reports promulgated from time to time like Cadbury Report (1992), Greenbury Report 1995 and Hampel Report 1998.

The Institutional Shareholders Committee (ISC) was established in the UK in the year 1991. "The ISC is a forum which allows the UK's institutional shareholding community to exchange views and, on occasion, coordinate their activities in support of the interests of UK investors."13

---

11. Supra note 4.

12. Profs Stuart L.Gillan and Laura T. Stark, The Evolution of Shareholders Activism in the United States, page 3 (PhD diss.,.University of Texas, 2007) .

13. http://www.institutionalshareholderscommittee.org.uk/index.html (accessed March 9, 2009).

ISC in the year 2002 issued the 'Statement of Principles' wherein the role and responsibilities of the institutional shareholders were defined. The purpose of issuance of the 'Statement' was to ensure the application of best practice to the relationship between institutional shareholders and the investee companies, with the aim of securing value for beneficiaries over the longer term. Similarly, in the year 2007 the International Corporate Governance Network also published a 'Statement of Principles' pertaining to the responsibilities of institutional shareholders.

In Pakistan, yester years have witnessed the concentration of equity ownership in the hands of rich families and feudal lords. The present scenario is, however, somewhat different. Large institutions are now powerful investors along with the individual investors. The Companies Ordinance 1984 and the Code of Corporate Governance 2002 contain various provisions regarding the active participation of the shareholders in the investee companies' managerial affairs.

In the reported case titled 'Kohinoor Raiwand Mills Limited through Chief Executive versus Kohinoor Gujar Khan Mills and others' the three petitioner companies filed petition under sections 284 to 288 of the Companies Ordinance1984, seeking sanction of the court to a scheme of arrangement approved by their shareholders in general meetings. The shareholders had opposed the scheme of merger for valid reasons documented by audited accounts of the petitioner companies. It was held by Justice Jawwad .S. Khawaja of the Lahore High Court that in case of amalgamation/merger of companies, "directors cannot act arbitrarily while proposing such scheme. Directors may have discretion in selecting one of various suitable courses of action, which may come

before them for consideration, but they have no discretion to choose a course of action not in the interest of shareholders"[14]

The famous case of 'Wattan Party through President versus Federation of Pakistan' relating to the privatisation of Pakistan Steel Mills is a good example of shareholders activism. In the present case the members of the workers union alleged that the Privatization Commission of Pakistan itself took into confidence the workers vide letter dated 20 December 2005 whereby the members of the Union were given a right to form the workers and management group for the purpose of giving a bid to purchase the shares of the Mill. However, when in pursuance of such offer the workers were ready to participate in the bid, at the eleventh hour they were called upon to deposit U.S. $30 Million as earnest money which they could not arrange hurriedly. The august Supreme Court of Pakistan in order to protect the rights of shareholders annulled the whole process of privatization.[15]

In Pakistan the activism on the part of shareholders, is still under process. The investors in Pakistan prefer short term investments in order to gain quick returns while investors in the developed countries prefer long term investments. There is infact lack of an organized level of shareholder activism in Pakistan. The level of shareholders activism can rise with the rise in the ratio of intuitional investors. Large institutions with long-term investment strategy could contribute towards stabilized market in Pakistan.

1.3 Concept, Meaning and Definition Of the Shareholders Activism

Shareholder activism is a term that is used oftenly but defined rarely. The European

---

14. 2002 CLD 1314.

15. PLD 2008 SC 697

Corporate Governance Institute (ECGI) defines the term as:-

> "Shareholder activism is the way in which shareholders can assert their power as owners of the company to influence its behaviour."[16]

In order to formulate a proper definition of the term 'Shareholder Activism', it is pertinent to know individually the meanings of the terms 'shareholder' and 'activism'. It is interesting to note that neither the Companies Ordinance 1984 nor the Code of Corporate Governance define the terms 'shareholders' and 'activism'. However the term member' has been defined in Section 2(21) of the Companies Ordinance 1984 as:-

> "Member means in relation to a company having share capital, a subscriber to the 'memorandum of the company and every person to whom, is allotted or who becomes the holder of, any share, scrip or other security which gives him a voting right in the company and whose name is entered in the register of members, and in relation to a company not having share capital, any person who has agreed to become a member of the company and whose name is so entered". [17]

It was held in the case of "Howrah Trading Co. Ltd v. CIT"[18] that the expression member', 'shareholder' and 'holder of shares' are interchangeable terms in the case of company having a share capital. Similar view was followed in the case titled "Killick Nixon Ltd v. Bank of India" [19]

The expression 'member' occurring in section 2(21) of the Companies Ordinance 1984 seems to be wider in scope than 'shareholder' and signifies a person who is a member of

---

16. http://www.ecgi.org/activism/index.php (accessed June 29, 2009).
17. Nazir Ahmad Shaheen, *Practical Approach To the Companies Ordinance 1984*, page 8, New Fine Printing Press, Lahore, 2004.
18. AIR 1959 SC 775
19. 1985 Company Cases 831(Bombay)

any company whether limited by shares or guarantee. The term 'Share' as per 'section 2 (35) of the Companies Ordinance 1984 means "Share in the share capital of a company".[20] Therefore we can say that a shareholder is a person who holds some share in the share capital of a company.

The term 'activism' as defined in the Oxford Dictionary means "policy of vigorous actions in politics".[21] In terms of corporate system we can say that activism means policy of vigorous actions in business. Shareholder activism can be defined as the policy of vigorous actions in business adopted by shareholders. "Activism covers a broad spectrum of activities. Activism includes 'voting with ones feet' (exit), private discussion or public communication with corporate boards and management, press campaigns, blogging and other e-ways of public 'naming and shaming', openly talking to other shareholders, putting forward shareholder resolutions, calling shareholder meetings and – ultimately - seeking to replace individual directors or the entire board'.[22]

1.4 Institutional Shareholders Activism

The International Corporate Governance Network in its 'Statement of Principles on Institutional Shareholders Responsibilities' approved in AGM dated 6th July 2007, observed that the "the terms 'institution' and 'institutional investor or shareholder' are used to refer to professional investors who act on behalf of beneficiaries , such as individual savers or pension fund members. Institutional shareholders may be the collective investment vehicles, which pool the savings of many or the asset managers to whom they allocate the funds. Examples of the former include pension funds, insurance

---

20. Supra note 17 at page 18.

21. J.B.Sykes, The Concise Oxford Dictionary, p.11, Oxford Printing Press, 1976

22. Supra 16

companies and mutual funds. The investment arrangements for these institutional shareholders will vary according to type and local law or regulation."[23]

The term 'institutional shareholders' include financial institutions as well as non-financial corporations. Sec 2(15-A) of the Companies Ordinance 1984 defines the term 'Financial Institution' in the following words:-

"Financial institution includes:-

(a) a company or an institution whether established under any special enactment and operating within and outside Pakistan which transacts the business of banking or any associated or ancillary business through its branches;

(b) a modarba , leasing company, investment bank, venture capital company, financing company, housing finance company, a non-banking finance company; and

(c) such other institution or company authorized by law to undertake any similar business , as the Federal Government may by notification in the official gazette, specify for the purpose"[24]

From the above definition it is apparent that the term 'financial institution' refers to both banks and non-banking financial companies. Institutions whether financial or otherwise may be owned by the government or the private investors. Therefore, institutional ownership can be defined as the share ownership by both financial institutions and non-financial corporations . Typical examples of institutional investors are Non-Banking

---

23. http://www.icgn.org/ (accessed March 30, 20099).

24. Supra note 17.

Finance Companies, Banking Companies, financial entities like Trusts and Non-profit Organizations, Development Financial Institutions, Insurance Companies, International Organizations and Fund Managers.

The role of institutional investors enhanced in UK and US in the twentieth century, due to decline in the individual share ownership and increase in the institutional share ownership. Now a days, institutional investors are playing key role in the corporate governance of many developed countries .For instance , in USA "The California Public Employees' Retirement System (CalPERS) provide retirement and health benefits to more than 1.6 million public employees, retirees, and their families and more than 2,500 employers."[25]. Similarly in UK, Hermes Pensions Management Ltd provide products which "are aimed exclusively at institutional and professional investors." [26] Pension funds and insurance companies are major institutional investors in UK.

Pakistan, unlike UK and US, in the past, had an underdeveloped corporate culture, as vast numbers of companies were owned and controlled by families. Institutional investors formed a small segment of the securities market. However, in the recent years the institutional investors have grown phenomenally. As for instance, in recognition of the increased importance of mutual fund as an investment vehicle, the Securities and Exchange Commission of Pakistan made certain guidelines in the Code of Corporate Governance 2002 to be followed and implemented by both the mutual fund and investee company. Even after the issuance of the Code of Corporate Governance in Pakistan, the institutional investors are not playing activist role. Institutional investors

---

25. http://www.calpers.ca.gov/index.jsp?bc=/about/home.xml .(accessed April 6 , 2009).

26. http://www.hermes.co.uk/. (accessed April 6 , 2009).

can be beneficial for promotion of good corporate governance norms only when they play proactive role. Institutional investors with large shareholdings can monitor the decisions of the board. They can also assert their part by voting and raising their voices through presentation of proposals in the annual general meetings of the investee companies.

The legal environment of a particular country greatly influences the extent of activity on the part of institutional investors. In USA, the institutional investors are playing proactive role and helping in building effective corporate governance practices. Institutional investors in USA, actively participate in voting and also present proposals in AGMs of the investee firms. Similarly, the institutional investors are also monitoring the decisions of the board of the investee companies. The force behind such an increased activism on the part of institutional investors was the Sarbanes-Oxley Act 2002. The Sarbanes Oxley Act was passed by the congress in USA in order to establish enhanced standards for corporate accountability. Sarbanes Oxley Act contains various provisions ensuring transparency and fairness in terms of financial statements. The institutional investors who review and study the financial statements of the companies in which they invest, benefit substantially from Sarbanes-Oxley. Section 404 listed under Title IV of the Act (Enhanced Financial Disclosures), and pertaining to "Management Assessment of Internal Controls", requires the corporations to publish information in their annual reports as to the scope and adequacy of the internal control structure and procedures for financial reporting .[27] Corporations are also required to assess the effectiveness of such internal controls and procedures in such a statement.

---

27. http://www.sarbanes-oxley.com/section.php?level=1&pub_id=Sarbanes-Oxley (accessed June 30, 2009)

Similarly other provisions pertain to the appointment of independent directors, transparency and disclosure in terms of audit, penalties for falsifying financial records and so on. Active institutional investors in terms of Sarbanes Oxley Act 2002 can ensure the implementation of these provisions by the investee companies, thus leading to better corporate governance.

In the United Kingdom as well the institutional investors are proactive, as the country has taken strong legislative measures to strengthen the corporate governance practices on their part. Cadbury Report 1992, Greenbury Report 1995, Hampel Report 1998 and Higgs Report made observations regarding the defined role of institutional investors in the corporate governance. Similarly the 'Combined Code of Corporate Governance' 2003 which is the amalgamation of all these reports, specifically incorporated a separate section titled 'Institutional Shareholders', wherein the main principle laid down is that the "Institutional shareholders should enter into a dialogue with companies based on the mutual understanding of objectives." [28] The Code manifestly and elaborately defines the role and powers of institutional investors in the implementation of corporate governance norms. For instance, Rule E-3 of Section 2 of the Code provides makes it obligatory upon the institutional investors to make considered use of their votes. The institutional investors are also directed to attend the Annual General Meetings of the investee companies. Moreover, the institutional investors are also required by the Code, to give due weight to all relevant factors drawn to their attention while evaluating companies' governance arrangements , particularly those relating to the board structure and composition.

The Combined Code of Corporate Governance 2003 makes it incumbent upon the

---

28. http://www.fsa.gov.uk/pubs/ukla/lr_comcode2003.pdf(accessed July 3,2009)

institutional investors to ensure that the investee companies have complied with the provisions of the Code and in case of non-compliance they should consider carefully explanation given for departure. The Code sets out guidelines and principles pertaining to the working of the board of directors, disclosure policy, accountability, corporate responsibility, role of non- executive directors and the audit committee. All these principles if applied and implemented in their true perspectives leave no ground for corrupt governance practices.

The corporate environment of UK and US is also influenced by international standards set out by international entities like the International Corporate Governance Network (ICGN). It is a body constituted in the year 1995 at the instance of major institutional investors with an aim to facilitate international dialogue on the issues concerning global corporate governance practices. The ICGN is of the view that where codes of best corporate governance practices exist, they should be applied pragmatically and where they do not exist they should be developed by the institutional investors. In its statement regarding the 'Principles on Institutional Shareholders Responsibilities' the ICGN has laid down certain parameters to be observed by the institutional investors in order to promote good governance practices.

The state of affairs in Pakistan is, however, different. Institutional investors are passive for the reason that institutional shareholder activism is still under development. In Pakistan the primary law regulating the relationship of shareholders with the investee companies, is the 'Companies Ordinance' 1984. The Companies Ordinance 1984 contains various rules pertaining to the corporate governance. Similarly the Securities and Exchange Ordinance 1969 contains provisions for investors' protection, insider trading

and market regulation. The Securities and Exchange Commission of Pakistan which is the chief regulator of capital markets and controller of corporate entities was established under the Securities and Exchange Act of 1997. The listed Companies (Substantial Acquisition of Voting shares and Takeovers) Ordinance 2002 is another legislation that contains additional take over and ownership disclosure rules. The Code of Corporate Governance 2002 lays down recommendations and guidance to be followed by the listed companies of Pakistan. However, in all these legislations there are certain lacunas which require to be fulfilled in order to boost the role of institutional investors in the corporate governance.

The Companies Ordinance 1984 under section 164 provides that the shareholder owning 10 % of the shareholding can propose the resolution and furnish draft to the company. Institutional investors usually having large shareholdings can take part in the future and existing development of the investee company. However, institutional investors owning less than 10 % shareholding cannot present draft resolution for consideration in the AGMs of the investee companies. Similarly same percentage of ownership is required for shareholders in order to seek a declaration from a court of law pertaining to the invalidation of proceedings of a general meeting. Those institutions which do not own ten percent shareholdings of the investee company cannot approach the court of law even if their interests went unprotected in the AGM. This issue has not been addressed in the Companies Ordinance mainly due to passivity on the part of minority institutional shareholders.

Institutional shareholders can become a force to be reckoned and listened to by boards of directors only when they discard this passivity and actively participate in the

companies affairs for the protection of their rights. Major corporate scandals that occurred in the developed countries were the result of this passivity on the part of shareholders. No doubt maladministration was the major cause of these corporate scandals but according to the 'Economist' "much occurred because owners allowed it to; they delegated their powers to managers leaving them to set pay and targets and to monitor their own performance." [29] In Pakistan as well corporate scams occurred due to the lack of activism on the part of shareholders.

In the recent case of "Mohummad Kaleem Rathore versus Institute of Chartered Accountants" Mr. Justice Tassaduq Hussain Jillani observed that "We have had our own Enrons and corporate scams. But unfortunately a swift, appropriate, retributive and deterrent response has been lacking making the corporate world vulnerable to human weaknesses of greed, temptation and lack of scruples leading at times to skewed audit reports. In the ordinary course of events, company or corporation which is responsible for its financial statements prepared by self-appointed mangers appoints its own accounting firm to give a clean chit to its financial health by endorsing those statements and then these auditors\accounting firms are compensated for giving this clean chit." [30] In this case the petitioner in his capacity as a Chartered Accountant impugned a directive issued by SECP whereby it was directed that only those persons should be appointed as external auditors who have been given a satisfactory rating under the Quality Control Review Programme of the Institute of Chartered Accountants of Pakistan. The court dismissed the petition by holding that the directive was in line with the provisions of the Securities

---

29. http://www.economist.com/surveys/displaystory.cfm?story_id=E1_TRVSGQJ (accessed July 5, 2009)

30. 2009 CLD212

and Exchange Ordinance 1969.

The economy of Pakistan is staggering due to political and social instability and energy crises. In the present scenario the capital market of Pakistan is overly- depressed. There is a need for domestic as well as foreign investment, in order to reboot the capital market. Institutional investors being long term investors could prove to be the riders of this positive change in the capital market of the country. Need of the hour is that the institutional investors should organize themselves and with mutual deliberation and consultation, bring to the notice of the legislators such measures that could protect their own rights and also provide a healthy corporate governance culture. In this respect the major aspects like board structure, appointment of auditors, voting rights, shareholders monitoring etc should be taken into consideration. The investee companies as well as the institutional shareholders should try to sort out those areas that need major reforms and better legislation. Together, they can lead the corporate governance culture to the zenith of good standards.

Chapter II.

Shareholders Activism and the Investee Company/Firm's Performance

2.1 The Influence of Shareholders Activism on the Investee Company/ Firm's Performance.

Institutional investors could bear substantial impact upon the performance of the company/firm they invest in. Large shareholdings owned by the institutional investors pave a way for them to assert their part in managing the affairs of the Investee Company / firm. Activism on the part of shareholders include activities ranging from raising voices through proposals in AGM, passing special resolutions, voting, demanding transparency and disclosure of financial position of the investee company/ firm, fair audit and ensuring the compliance of prevalent laws by the investee company/ firm.

Institutional investors having large shareholdings are the long-term investors. The institutional investors act as intermediaries making investments on behalf of the beneficiaries. As fiduciaries of the public money they prefer to make long term investments in order to meet the needs of the existing as well as future beneficiaries. The investee companies, in which the institutional investors hold shares, are also required to act in a responsible manner in order to support a healthy and stable economy. The investing and the investee companies are expected to comply with the standards of good corporate governance for making the economy grow.

Institutional Shareholders can play an effective role in bringing about changes in a company's behaviour, for adoption of good corporate governance standards. As compared to the individual investors, institutional investors can play a significant role where they own majority shares of the investee company. Large shareholding owned by

the institutional investors gave them enormous bargaining power with the management as compared to the small investors. Institutional shareholders, therefore, can monitor the performance and corporate governance of the investee companies. The performance of the investee companies can be monitored by the institutional shareholders by promoting efficient allocation of resources, by offering lower transaction costs, by providing liquidity to investors etc. Individual investors usually do not invest at the large scale, therefore, they can not have a say in the managerial affairs of the investee companies. More expertise can be brought by active institutional investors having portfolio managers as compared to the individual investors, thus contributing towards better corporate environment.

Different authors have expressed different views as to the impact of institutional shareholders activism on the performance of the investee company. Some are of the view that institutional investors can achieve sufficient benefits from the investee company as they have an incentive to monitor due to large shareholdings owned by them.[31] As compared to the members of the Board, the institutional investors are possessed of greater incentive to monitor the investee company's performance for the reason that the members of the Board have no substantial investments in the company.[32] Opportunistic behaviour of the mangers can be curbed by the institutional investors as they have the power to force them to concentrate more on the implementation of corporate governance

---

31. S.Grossman and O. Hart,Takeover Bids, the Free Rider Problem and the Theory of the Corporation, pp.42-64 , Bell Journal of Economics 11,1980.

32. A.Sheilfer and R.Vishny , Large Shareholders and Corporate Control,pp. 461-448, Journal of Political Economy 94, 1986

standards.[33] Large shareholding owned by the institutional investors acts as deterrent for the mangers in pursuing opportunistic goals.[34]

Some authors are of the view that the ability to monitor the investee company's performance depends upon the size of shareholdings owned by the institutional investors. Where the institutional investors are possessed of large shareholdings in the investee company then their shares are less marketable and can last for long periods. In such a case the institutional investors have the incentive to influence the managerial affairs of the investee company. However, where the institutional investors hold small shareholding of the investee company then these investors have lesser incentive to monitor the performance of the same. Institutional investors with small shareholdings can liquidate their investments in case of poor performance of the investee company.[35]

Institutional Shareholder activism bears considerable influence upon the working of a poorly performing company. Institutional shareholders participating actively in the corporate governance reduce the risk of mergers and acquisitions and enhance the asset divestitures. Activism on the part of institutional investors also curbs the abnormal increases in the share price.[36]

---

33. JJ.McConnell and H.Servaes, Additional Evidence on Equity Ownership and corporate Value,pp. 595-612, Journal of Financial Economics 27,1990

34. R.Chung, M.Firth and J. Kim , Institutional Monitoring and Opportunistic Earnings Management,pp.29-48,Journal of Corporate Finance 8, 2002.

35. E.Maug, Large Shareholders as Monitors: Is there a trade off between liquidity and control? pp. 65-98, Journal of Finance 53, 1998.

36. J. Bethel, J. Leibiskind and T. Opler, Block Share Purchases and Corporate Performance,pp. 605-635. Journal of Finance 53, 1998.

Institutional investors proposals pertaining to the corporate governance are likely to be voted upon more favourably as compared to those proposals rendered by individual investors.[37] Some authors see a positive relationship between institutional share ownership and the performance of the investee company,[38] however, others hold a contrary view. According to them the institutional investors activism does not bear a substantial impact upon the performance of the investee company. [39]

Institutional shareholder activism depends upon the pressure sensitivity and insensitivity of the investors. Those institutional investors who rely on the firm in which they invest in for business, are "pressure sensitive" and those who do not rely on the investee firm are "pressure resistant".[40] Institutional investor's preferences and motivations differ according to their size, need, location and legal and corporate culture of a particular country. They are not homogenous but rather heterogeneous. It cannot be said that all institutional investors are 'pressure sensitive' or all are 'pressure resistant'. The level of activism in 'pressure resistant' institutional investors is higher than those who are 'pressure sensitive'. Insurance companies and banks may be characterized as

---

37. S. Gillan and L.Starks Corporate Governance Proposals and Shareholder Activism: The Role of Institutional Investors, pp.275-305 Journal of Financial Economics, 57, 2000.

38. Supra note 33

39 A. Agrawal and C.R.Knoeber, Firm performance and mechanisms to control agency problem between managers and shareholders , pp.377-397, Journal of Financial Quantitative Analysis 31, 1996.

40 Michael J. Rubach, Institutional shareholder activism: the changing face of corporate ownership, p.19 , Garland Publishing Inc New York, 1999

'pressure sensitive' investors as they heavily rely for their business on the investee company/ firm while mutual funds and pension funds are 'pressure resistant' investors.

An institutional investor may be described as a "Universal owner one that …holds in its portfolio a broad cross section of the economy, holds its shares for the long term, and on the whole does not trade except to maintain its index".[41] The institutional investors like pension funds and mutual funds prefer to make long term investments for their beneficiaries. They play an effective role in the economy of a country as a whole for the reason that the long term investments contribute towards a stable market. Resultantly "a universal owner's cumulative long-term return is determined not merely by the performance of each individual firm it owns, but by the performance of the economy as a whole." [42]

Shareholder activism bears co-relationship with the performance of the Investee Company/ firm. The major areas where institutional investors can participate actively are given below supported with Pakistani case laws:-

Annual General Meeting

Extraordinary General Meeting

Insider Trading

Voting

Board of Directors

Auditing

---

41 James P. Hawley & Andrew T. Williams, The Rise of Fiduciary Capitalism (Philadelphia: University of Pennsylvania Press, 2000).

42. Ibid

2.2 Annual General Meeting :

The Annual General Meeting may be regarded as the highest authority of the company. In the Annual General Meeting the shareholders get the opportunity to ask questions and clarifications of various corporate issues. The Annual general meeting of a company is a forum where the Board, management and the shareholders, all can participate and deliberate over the important affairs of the company. Therefore, the shareholders must ensure their presence in the meeting. Non-holding of an Annual General Meeting deprives the shareholders of their valuable rights as conferred upon them under the Companies Ordinance 1984.

Whenever a company gets incorporated then as per Section 158 (1) of the Companies Ordinance 1984, it becomes incumbent upon the same to hold its annual general meeting within eighteen months and thereafter at least once every year.[43] Matters pertaining to the consideration of the accounts, declaration of dividend, appointment of directors and appointment and fixation of remuneration of auditors may be included in the agenda of the Annual General Meeting. Institutional investors must be vigilant enough to ensure that the investee company/ firm holds its annual general meeting. If it fails to do so then the institutional investors could bring legal action against the said investee company.

Section 158 makes it mandatory upon the companies to hold Annual General Meeting. Failure to do so cannot be justified in any case. In the case titled "Mian Mohummad Ilyas Miraj versus Appellate Bench No III Securities and Exchange Commission of Pakistan"

---

43. Supra note 17 at page 460

Justice Syed Hamid Ali Shah of the Lahore High Court observed that:-

> "Section 158(4) of the Companies Ordinance, 1984, in unqualified terms, provides for holding of Annual General Meeting. No departure is permissible from the compliance of the mandatory provisions of section 158. The company is artificial person and those who manage it's affairs are under legal as well as fiduciary obligation, to run the affairs of the company as the law (Companies Ordinance, 1984) requires. Corporate democracy is the essence of the corporate personality of a juristic person. The legislature in it's wisdom was conscious of the importance of holding of Annual General Meeting and that is why a company is made liable to be wound up, if fails to hold two consecutive Annual General Meetings."[44]

In the case of 'State versus Aziz Hussain Chief Executive Hyesons Sugar Mills Limited' a fine of Rs 10000/- (ten thousand) was imposed upon the Chief Executive of the sugar mill under section 158(4) as he was personally responsible for non-holding of the AGM. [45] Similarly in the case of 'Chief Executive, Punjab Lamp Works Ltd. Karachi', penalty was also imposed upon the Chief Executive in the shape of fine under section 158(4), for his default in holding of AGM.[46] In the matter of 'Noor Silk Mills Limited', the Securities and Exchange Commission of Pakistan held the directors of the company to be responsible for non- holding of the Annual General meeting without any

---

44. 2009 C L D 883

45. NLR 1990 TD 358

46 1990 CLC 1640

justifiable reason. The directors took the plea that the Accountant of the company had left the job and the new Accountant was not aware of the accounts, therefore, accounts could not be finalized in time. The Commission observed that the directors were duty bound to make necessary arrangements for the finalization of accounts and the resignation of the Accountant was not a cogent reason for not holding the Annual General meeting.[47]

In the matter of 'Quality Steel works Limited' the Securities and Exchange Commission imposed a fine of rupees thirty thousand on the Chief Executive and each of the Directors of the company for failure to hold Annual general Meeting. The directors took the stance that the Annual general meeting could not be held as the operation of the company remain suspended during the relevant period due to the non- availability of the staff to prepare the accounts. The Commission held that the non-functioning of the company or the suspension of its operation was not a valid reason for non-holding of the Annual general meeting and non-circulation of accounts to the investors.[48] In the matter of 'Messrs Ayaz Textile Mills Limited' also the Commission imposed a fine of rupees twenty thousand upon the Chief Executive, holding him responsible for making default in calling the Annual general Meeting of the company. [49]

The proviso to section 158(1) provides that the Securities and Exchange Commission of Pakistan may extend the time for holding AGM for any special reason. However, this extension may be granted for thirty days only. [50] In the case of 'Syed Amir

---

47. 2007 CLD 605

48 2007 C L D 1116

49 2006 CLD 378

50 Supra note 17 at page 460.

Hussain Shah versus Progressive Papers Limited' the respondent company failed to hold its Annual General Meeting in time and no extension in time was sought. The court held the Chief Executive of the respondent company to be responsible for the default in holding the Annual General meeting in time. The court observed that the Chief Executive could have applied under proviso to Section 158 (1) of the Companies Ordinance 1984, on behalf of the respondent company for extension in time for holding the Annual general meeting. [51]

Listed companies are required to hold their AGMs in the places where their registered offices are situated. It was held by the court in the case of 'Malik Mohummad Ishaq versus Messers Erose Theater' that:-

> "where the company was a private company, there was no legal bar of holding such meeting at any other place than in town of the registered office, though in respect of the listed company (public limited company) the Annual General Meeting had to be held in the town of registered office in terms of section 158(2) of the Companies Ordinace1984." [52]

Therefore, whenever the investee company fails to hold its AGM in the place of its registered office in contravention of proviso to section 158(1), the institutional investors are at liberty to bring legal action against the said company.

The investee company is also bound to serve notices of AGM on all its shareholders

---

51 PLD 1969 Lah 615

52 PLD 1973 Kar 52

under section 158 (3) of the Companies Ordinance 1984, which reads as follows:

> "The notice of an annual general meeting shall be sent to the shareholders at least twenty days before the date fixed for the meeting and in case of a listed company, such notice, in addition to its being dispatched in the normal course shall also be published at least in one issue each of a daily newspaper in English language and a daily newspaper in Urdu language having circulation in the Province in which the stock exchange ,on which the company is listed, is situated". [53]

This section manifestly provides that in case of listed companies, notices should be served upon the shareholders publically as well as personally. It is also necessary that notices of AGM should be sent to the shareholders atleast twenty one days before the date fixed for the meeting. In the case titled 'Col. Kuldip Singh Dhillon versus Paragon Utility Financers (Private) Limited', individual notices of AGM were not sent to all the shareholders in terms of section 158 (3) of the Companies Ordinance 1984. The court held that without service of notices to all the shareholders, holding of AGM on specified date by the respondents was invalid. [54] Similarly in the case of 'Central Cotton Mills versus Naveed Textile Mills' apart from public notices no personal notices were served upon the shareholders. Meetings of company on the specified dates were thus, declared to be null and void. [55]

---

53. Supra note 17 at page 461

54 (1988) 64 Company Cases 19.

55. 1993 MLD 42.

Consequences of non-holding of AGM include:

(1) Imposition of fine under section 158(4) of the Companies Ordinance 1984. Such fine may be imposed upon the company itself or any officer who is responsible for non-holding of the AGM.[56]

(2) Direction by registrar for holding of over-due AGM under section 170.[57]

(3) Initiation of winding up proceedings in case of non-holding of two consecutive AGMs, under section 305(b). [58] "The company would be under mismanagement if failed to convene two consecutive General Meetings in terms of Section 305(b) of the Companies Ordinance 1984." [59]

"The protection of the investors/ shareholders is one of the primary objectives of the Ordinance, it is investors/shareholders who provide seed for capital formation. If their interest is protected, they will invest more to save the Company, therefore the Company must ensure transmission of timely, adequate and meaningful information to them. It is the annual and interim accounts, which provide information to the shareholders about the affairs of the company and Annual General Meeting is a forum where they can freely speak, discuss and vote on important matters concerning , approval of accounts ,

---

56. Supra note 17 at page 461.

57. Ibid at pages 499-500.

58. Ibid at page 849

59. PLD 1973 Kar 52.

appointment of auditors, election of directors etc."[60]

The penal provisions contained in the Companies Ordinance 1984, aim at ensuring such protection to the investors. Vigilance and activism on the part of institutional investors is required for ensuring the compliance of these mandatory provisions by the investee companies.

2.3 Extraordinary General Meeting:

A meeting other than the statutory meeting and the annual general meeting is known as extraordinary general meeting. Institutional shareholders owning ten percent of the total equity of the investee company may demand the holding of an extraordinary general meeting under section 159 of the Companies Ordinance 1984. The directors become duty bound to call an extra ordinary general meeting whenever a requisition is made to this effect by the shareholders. If the directors fail to call the meeting within twenty one days from the date of the requisition then as per clause (4) of section 159 the requisitionists/ shareholders may themselves call the meeting. Agenda of such a meeting is provided by the requisitionists.

Every shareholder owning ten percent of the equity has a right to requisition an extraordinary general meeting. "He cannot be restrained by injunction from calling the meeting and is not bound to disclose his reasons." [61] The investee company is required to serve notices of an extraordinary general meeting on all its members in the same manner as required for an AGM. Non issuance of notices and non publication of notices in the

---

60. 2007 C L D 605

61. (1986) 59 Company Cases 548.

newspaper, are the acts punishable under section 159(8) (a) of the Companies Ordinance1984. Shareholders may sue the investee company itself or any officer who makes such a default. [62]

In the case titled Siddique Mohummad Malik versus Imdad Iftikhar Malik a joint notice of an extraordinary general meeting was served upon the shareholders. The court observed that "Notice under S.50, Companies Ordinance, 1984 issued jointly was illegal and wrong, for, every member was to be issued separate and independent notice and the same should have been issued and served on that member individually on his address---Joint notices were issued at the address of the company and the same were received by Accountant of the company--Address of the company was not the home address of the members and the Accountant of the company was. not their representative---Such material defect in issuance of notice, had the resultant effect of preventing the petitioners from participating in the proceedings of the meeting---When provisions as to issuance and service of notice as contained in S.50, Companies Ordinance, 1984, had not at all been adhered to, extraordinary meeting held was not lawful and proceedings taken therein were neither legal nor were binding on the company." [63]

Section 160-A [old section 161(8)] empowers the shareholders holding ten percent voting powers, file a petition in a Court of law for declaring a General Meeting to be invalid. The said petition may be filed on the ground of "a material defect or omission in the notice or irregularity in the proceedings of the meting which prevented members

---

62. Supra note 17 at pages 470-471

63. 2000 CLC 477

from using effectively their rights." [64] Mr Justice Munir.A. Sheikh in the case titled Shahid Saigol and others versus M/s. Kohinoor Mills Ltd and Others' declared the notice dated 8-9-1994 for Extraordinary General Meeting and the resolution passed in pursuance thereof on 1-10-1994 in the Extraordinary General Meeting to be invalid under section 161(8). Direction was made to the respondent company to hold afresh its Extraordinary General Meeting after complying with the provisions of section 160(1)(B) and section 208 of the Companies Ordinance 1984. [65]

Similarly in the case of 'Integrated Technologies and System Ltd versus Interconnect Pakistan (Pvt) Limited' notice of the extraordinary general meeting was not served upon the petitioner. The court held that the issuance of such a notice to all the shareholders including the petitioner was mandatory prior to the meeting. "Where such notice was not issued, shareholder was deprived of his right as a shareholder, to participate in the affairs of the company." [66] Meaning thereby that it is the right of each and every shareholder owning ten percent of the investee company's equity to be informed and allowed to participate in the affairs of the company through extraordinary general meeting. Institutional shareholders therefore must be well conversant with those laws and regulations which have been formulated especially for their protection and which could promote good corporate governance practices.

---

64. Supra note 17 at page 485

65. P L D 1995 Lahore 264

66 2001 CLC 2019

2.4 Insider Trading

The insiders of a company like managers and members of the board of directors are usually well acquainted with the state of the affairs of a company as compared to the outside shareholders. Having internal information about the company's affairs these insiders may indulge in malpractices like insider trading, concealing material information from the shareholders, misuse of information, non-transparency etc. Insider trading may be legal where the insiders buy and sell stock in their own companies with prior intimation to the company's management. However, where the insider trading is done surreptitiously in utter disregard of investors' protection, then it is purely illegal.

The confidence of the investors in the fairness and integrity of the securities market is undermined because of illegal insider trading. In USA, the Securities and Exchange Commission has introduced Rules 10b5-1 and 10b5-2 in the Securities Exchange Act of 1934. [67] These Rules make it unlawful for any person to indulge in the practice of insider trading. Similarly in UK, insider trading is regulated by the Model Code of the London Stock Exchange 1977 and the Companies Act 1985. The Financial Services and Markets Act (FSMA) of 2000 also contain provisions pertaining to the insider trading.

In Pakistan, SECP imposed the 'Listed Companies (Prohibition of Insiders Trading) Regulations, 2000' on March 27, 2001 in order to curb insider trading. Similarly 'The Stock Exchanges Members (Inspection of Books and Records) Rules, 2001' and the 'Proprietary Trading Regulations, 2004'. empowers the SECP to order the scrutiny of

---

67. http://www.investopedia.com/terms/s/seact1934.asp (accessed July 30, 2009)

books and record of any member of the stock. The 'Brokers and Agents Registration Rules, 2001' were enacted for the purpose of exercising direct control over brokers and agents. These rules aim at strengthening the surveillance capabilities of SECP and safeguarding the interests of the investors.

Chapter III-A of the Securities and Exchange Ordinance 1969 deals specifically with the insider trading. Section 15-A provides that:

Prohibition on stock exchange deals by insiders.

> "No person who is, or has been, at any time during the preceding six months, associated with a company shall, directly or indirectly, deal on a stock exchange in any listed securities of that or any other company or cause any other person to deal in securities of such company, if he has information which :-
>
> a) is not generally available;
>
> b) would, if it were so available, be likely to materially affect the price of those securities; or
>
> c) relates to any transaction (actual or contemplated) involving such company.
>
> Explanation.
>
> For the purpose of this section, the expression "associated with" shall mean a person associated with a company, if he
>
> (i) is an officer or employee of that company or an associated company; or

(ii) occupies a position which gives him access thereto by reason of any professional or business relationship between him or his employer or a company or associated company of which he is a director." [68.]

The perusal of section 15-A reveals that an insider may be any person, whether officer or an employee of the company. Section 15-B (3) speaks of compensation to be paid to the person who is the sufferer of an insider trading. In addition to compensation the insider may also be sentenced to imprisonment for 3 year and fine extending to three times the amount of gain or loss occurring due to such trading under clause 4 of section 15-B of the 'Securities and Exchange Ordinance 1969'. [69] Similarly under R.8 (b) of 'Brokers and Agents Registration Rules, 2001, penalty may be imposed on any broker or agent for practicing insider trading.

Penalty of Rs.100, 000 was imposed under R.8 (b) of Brokers and Agents Registration Rules, 2001, in the case titled 'Alfalah Securities (Pvt) Ltd versus Commissioner Securities Market Division SEC' with direction that "appellant should be careful and avoid making statements which were contrary to the required standards of integrity, due skill and care laid down in the Code of Conduct". [70] Similarly "Pakistan Kuwait Investment Company (PKIC) was fined Rs 0.536 million for insider trading in shares of Fauji Fertilizer Company Limited (FFC).That, somehow, looks like the work of an institutional director who sits on the Board of both PKIC and FFC."[71]

---

68. www.pakistanlawsite.com (accessed Aug 2, 2009)

69. Supra note 68

70. 2006 C L D 1068

71. The ' Daily Dawn' dated 22 November Monday 09 Shawwal 1425, 2004.

The matter of 'Zafar Moti Capital Securities (Pvt) Ltd and another' is a good example of shareholder activism. In this case the Securities and Exchange Commission of Pakistan issued a show cause notice under sections18 and 22 of the 'Securities and Exchange Ordinance, 1969' and Rule 8 read with Rule 12 of the 'Brokers and Agents Registration Rules, 2001' to 'Zafar Moti Capital Securities (Pvt.) Ltd.' and Mr. Zafar Siddique Moti, Chief Executive Officer. The said notice was issued upon the complaint of the investors filed by them before the Securities and Exchange Commission of Pakistan. The Company and its Chief Executive Officer had contravened the provisions of the Code of Conduct as laid down in the third schedule of the 'Brokers and Agents Registration Rules, 2001'. They were also guilty of furnishing wrong information to the Commission. The Company was enlisted on the Karachi Stock Exchange and was also a registered broker. One MR Tariq Saeed was dealing with the securities of the company as its agent although he was not a registered and authorized agent. Infact the said Tariq Saeed had maintained sub accounts with various brokers and dealing with their securities for the investors illegally. Section 5-A of the Securities and Exchange Ordinance 1969 completely debars a person from acting as an agent to deal in the securities unless he gets himself registered with the Commission. The Commission after hearing the parties imposed a fine to the tune of Rs.5, 000,000 (Rupees five million) upon the company itself and Rs.1, 000,000 (Rupees One Million) upon the Chief Executive Officer.[72]

Law in Pakistan is not lacking with respect to curbing insider trading. It is the capacity and spirit to enforce the law which is absent. Activist institutional investors may

---

72. 2008 C L D 6

control the trend of insider trading in the Investee Company / firm by adhering to a certain strategy that may make the law work in its letter and spirit. Activist shareholders monitoring the investee company may improve the performance of the same by promoting efficient corporate norms.

2.5 Voting

Immense influence can be exerted by the institutional investors over the companies in which they own stock through the exercise of voting power. Right to vote is a strong tool in the hands of the institutional investors, if used wisely. The significant voting power available to the institutional investors because of the large shareholdings, enable them to monitor the investee company's performance and to protect their own investments.

Conflict of interests arising between the investee company's management and the institutional investors may effectively be settled through voting. Moreover, through prudent exercise of voting power, the institutional investors can pressurize the investee company to make decisions beneficial to them.

Cadbury Report 1992 described the significance of voting power by institutional investors in the following words:

> "Given the weight of their votes, the way in which institutional shareholders use their power to influence the standards of corporate governance is of fundamental importance. Their readiness to do this turns on the degree to which they see it as their responsibility as owners, and in the interest of those whose money they are investing , to bring about changes in companies when

necessary, rather than selling their shares." [73]

The report also insisted upon positive use of voting rights and the registration of the votes by the institutional investors. The institutional investors were also encouraged to disclose their policies on voting.

The purpose of investing the shareholders with the right to vote is to give them an opportunity to maximize their wealth, through appointment of directors and auditors who would act in their benefit. Right to vote is a controlling tool in the hands of the shareholders. Where the investee company's management fails to solve any contentious issue with the institutional investors, then these investors have the right to vote against any resolution that is unfavourable to them. By voting against any resolution they can show the strength of voting power, to the investee company. The proper implementation of corporate governance system requires the improvement of voting levels by the institutional investors. Non-involvement by the institutional investors in the investee company's affairs through non- exercise of the voting power invests the management with increased power to manipulate the affairs of the investors.

The right to vote gives a controlling power to the institutional investors over the investee company's affairs. Corporate governance issues like remuneration of directors, the length of contract, appointment of auditors etc are most likely to raise differences between the investors and the investee company. Therefore, the institutional investors instead of acting passively should cast their votes in respect of these matters in order to solve these controversies. Institutional investors may cast votes in person or through

---

73. Supra note 6.

proxy. The Companies Ordinance 1984 prescribes the procedure for casting the vote in person or through proxy.

Section 160 (7) of the Companies Ordinance 1984 provides that "On poll, votes may be given either personally or by proxy". [74]

Proxy voting means that any shareholder who is unable to participate in voting personally may participate through an authorized agent. The person so authorized is usually entitled to have all such rights as respects speaking and voting as the shareholder has the rights himself. A shareholder, however, can appoint only one person as his proxy. Proxy voting in fact gives a facility to the shareholders to participate in voting even where they cannot ensure their presence personally. Proxy voting may be demanded as of right by the shareholders and the investee cannot deny this right to them without any legal justification.

The investee company is also bound to intimate the concerned shareholder about his right to appoint proxy, by specifically mentioning this fact in the notice of the meeting. Section 161(2) provides that:-

> "Every notice of a meeting of a company shall prominently set out the member's right to appoint a proxy and the right of such proxy to attend, speak and vote in the place of the member at the meeting and every such notice shall be accompanied by a proxy form". [75]

Hence, failure to intimate such 'right' and 'proxy form' to the shareholders amounts to

---

74. Supra note 17 at page 477

75. Supra 17 note at page 486

the contravention of Section 161 (2) of the Companies Ordinance. If such a contravention has resulted in preventing the shareholder from participation in the meeting or use of full rights by himself or the proxy then as per clause (10) of section 161 , the company itself or any officer who is responsible for such contravention may be fined upto five thousand rupees. The purpose of sending proxy form to the shareholder is to enable him to vote for or against any resolution even in his absence. Law in fact encourages proxy voting and it is the shareholders themselves who should actively participate in the voting either personally or through their respective proxies.

In the case titled 'Integrated Technologies & Systems Ltd versus Interconnect Pakistan (Pvt) Limited through Acting Chief Executive' , the petitioner company authorized the Company Secretary through power of attorney to attend the Annual General Meeting of the respondent investee company. The investee company did not allow the Company Secretary to attend the meeting upon the pretext that the power of attorney in his favour was not sufficient to make him a proxy. The court while deciding in favour of the petitioner company observed that the power of attorney by the company in favour of its Secretary was justified and he could represent the petitioner company as proxy in the Annual General Meeting. Debarring him from attending the meeting was held to be unjustified. [76]

In May 2003 the institutional investors of the Glaxo Smith Keline a blue chip company of UK, voted against the Remuneration Committee's recommendation in the Annual General meeting. The institutional investors were not satisfied with the fixation

---

76 2001 C L C 2019

of huge remunerations of the directors as well as chief Executive Officer of the company. The company accordingly had to revise the remunerations of the directors and the CEO.[77]

Generally the institutional investors adopt a passive behaviour in the exercise of their voting power and prefer to vote in favour of the investee company's resolutions. Institutional investors avoid to concern themselves with the managerial actions of the investee company. Through proposals the institutional investors can raise issue more effectively in the AGM. Through proper presentation of proposals and voting in the AGM , the institutional investors can solve various issues of the corporate governance.

Remaining passive means giving more power to the directors for doing whatever they want. Directors being the active managers of the company's affairs, if left unchecked, will obviously pass resolutions favourable to them. The passivity on the part of institutional shareholders in casting their votes would lessen the scope of monitoring investee company's affairs. Through active participation in AGM, the institutional investors may exert pressure on the management of the investee company to protect their rights as major investors.

2.6 Board of Directors

The fate of a company's progress depends upon the decisions of the Board of Directors. The directors being the managers and runners of a company are expected to be prudent and rational in the exercise of decision making power. Board of directors, if left unchecked and uncontrolled, is likely to get prejudiced. Therefore, Institutional investors should actively monitor its performance by passing resolutions and voting in AGMs and

---

77 Andrew L. Friedman and Samantha Miles, Stakeholders: theory and practice, p.201, Oxford University Press New York, 2006

other meetings. Highest standards of vigilance and surveillance are required to control the unauthorized use of decision making power by the board of directors.

Corporate Governance of a company can flourish only when the persons in holding the highest offices themselves provide better corporate environment for the same. The Board of directors can play a vital role in the corporate governance of the corporate entity. The development of policies and the communication of the company's objectives to the operational levels is the responsibility of the Board. The work of developing policies and setting out company's objectives should be done by the Board while keeping in view the interest of the shareholders and in accordance with the corporate governance standards .Proper monitoring and analysis of the practical application of the Code of Corporate Governance 2002, is the task of the Board.

The 'Combined Code on Corporate Governance' 2008 of UK postulates that:-

> "Every company should be headed by an effective board, which is collectively responsible for the success of the company".[78]

The primary objective of the Board of Directors should be to protect the assets of the shareholders and to ensure a good return on their investments. Being the highest governing authority of the company, the Board of directors owes so many duties towards its shareholders. The Board's duties include appointment of auditors and directors and fixation of their remuneration, establishment of the audit and compensation committees, selection of CEO, declaration and proper distribution of dividend, approval of company's financial statements, sale and purchase of securities and shares , issuance of debentures,

---

78. www.frc.org.uk (accessed Aug 6, 2009)

finalizing or rejecting acquisitions and mergers. In the performance of all these duties the board is expected to act in the best interest of the shareholders whether institutional or individual.

The Board of Directors is headed by a Chairman. The Cadbury Report 1992 specifically defined the role of the Chairman in the corporate governance in the following words:

> "The chairman's role in securing good corporate governance is crucial. Chairmen are primarily responsible for the working of the board, for its balance of membership subject to board and shareholders' approval, for ensuring that all relevant issues are on the agenda, and for ensuring that all directors, executive and non-executive alike, are enabled and encouraged to play their full part in its activities. Chairmen should be able to stand sufficiently back from the day-to-day running of the business to ensure that their boards are in full control of the company's affairs and alert to their obligations to their shareholders." [79]

The primary responsibility rests upon the Chairman of the Board to see that all the affairs of the company are in accord with bets corporate practices. The Chairman must ensure that the executive directors of the company are fairly performing their duties and they are not travelling beyond their powers. Similarly it is also the responsibility of the Chairman to provide relevant information to the non- executive directors whenever demanded by them. The non- executive directors must be briefed properly about the

---

79. Supra note 6.

company's affairs in the meetings so that they could contribute effectively towards the promotion of good corporate governance tenets.

There are many provisions in the Companies Ordinance 1984 that set out the responsibilities of the directors and also provide penalties for any unauthorized acts. Institutional investors as owners of the investee company should demand the implementation of best corporate practices from the Board of Directors .Section 187 of the Companies Ordinance 1984 provides for the ineligibility of certain persons to become directors. For instance a minor, unsound minded person, an undischarged insolvent, a convict and a person unqualified to act as director, cannot become a director.[80] "Main objective to disqualify a person from acting as a Director of a company was to save the community from the consequences of his mismanagement or fraudulent acts or incompetence." [81]

In the matter of Messrs Mukhtar Textile Mills Limited, the court took serious notice of the fact as to why the Securities and Exchange Commission had not imposed penalty under section 492 of the Companies Ordinance 1984,upon the Chief Executive and directors of the company for showing false financial statement. It was observed during annual examination of the accounts for relevant year that the capital of the company was increased considerably. The Security and Exchange Commission ordered inquiry which revealed that the share-holding of five Directors who were joint underwriters to the issue, had increased. That increase in the shareholding had resulted in

---

80. Supra note 17 at page 530.

81. 2007 CLD 165

the dilution of shareholding of shareholders .

The Court observed in the above titled case that:-

> "Management of listed-company should also be conscious of the fact that investment decisions of ordinary investors were effected by the information disseminated by them in the statutory document' circulated to share-holders---Management was responsible to ensure that undertakings were implemented in letter and spirit within the timeframe specified therein---In case of deviation of any sort, management was duty bound to disclose same to share-holders along with the effects thereof and measures taken to minimize the adverse effects---Deviation of the financial position of the company from that presented in the projections, appeared to be more attributable to lack of professionalism and ill-planning of the management, rather than any mala fide on their part to defraud general public---Securities and Exchange Commission, instead of imposing maximum penalty of Rs.100,000 on Chief Executive and each Director as prescribed by S.492 of Companies Ordinance, 1984 and ordering for inspection in terms of S.231 of the Ordinance, provided opportunity to the management to honour its commitments and deferred any action till such time the concerns of Commission were satisfactorily answered."[82]

---

82. 2006 CLD 627

In the matter of Messrs Bosicor Pakistan Limited, a fine of rupees fifty thousand was imposed under section 492 upon each director, chairman and the Chief Executive Officer of the company for violating the provisions of section 208 of the Ordinance. The company has made investments in associated companies without any resolutions approved by the shareholders. The Securities and Exchange Commission upon the complaint of the shareholders issued show cause notices to the company and its officials. After hearing it stood proved that the investments made by the company were not supported by any resolution by the investors therefore, the directors and the Chief Executive Officer were penalized accordingly.[83]

In the matter of Messrs JDW Sugar Mills Limited, company without seeking approval of its shareholders advanced amount in the shape of 'short-term working capital advance' to its subsidiary company. The Board and the CEO were well aware of this fact that the shareholders of the company have not rendered the approval still the Board acted in violation of section 208 of the Companies ordinance 1984. The Securities and Exchange Commission observed that the company had violated the mandatory requirements of Section 208, wherein it has been laid down in unequivocal terms that the company cannot advance any such amount without seeking authorization from its shareholders. Directors of the company holding fiduciary duty towards the shareholders are expected to act in their best interest and not to their detriment. Thus the CEO was penalized by way of imposition of fine under section 492 and the directors were reprimanded to remain careful .[84]

---

83. 2008 C L D 436

84. 2008 C L D 809

As per section 86 of the Companies Ordinance the directors of the company cannot increase the capital of the company by issuance of new shares without intimating this fact to the shareholders.[85] A listed company can issue such shares after complying with the provisions of the 'Companies (Issue of Capital) Rules, 1996'.the violation of the provisions of the said Rules make the company liable for legal action. In the matter of 'Altern Energy Limited', the company issuing right shares in order to increase its capital failed to make an intimation the Securities and Exchange Commission and the concerned Stock Exchange about the purpose of issuance of shares, in utter violation of Rule 5 [86] of the Rules 1996 and section 86 of the Ordinance. The company also failed to provide the financial plan as approved by the directors in the meeting. The directors and the Chief Executive Officer of the company were held to be guilty of violating the Rule 5 and section 86, hence were directed to pay Rs 50000 each as fine. [87]

Section 189 provides penalty of fine for an unqualified person acting as a director, which may extend to two hundred rupees per day during which the person acted as director.[88] The relation between a company and its director is that of a trust. The director is expected to act bonafide, in the best interests of the shareholders. Directors being the trustees of the money which come in to their hands may be held liable for misuse or misapplication of accounts. Misappropriations by the directors in the investee company can be detected by institutional investors only where these investors show activism and

---

85. Supra note 17 at pages 290-291

86. Supra note 68

87. 2006 C L D 1470

88. Supra at page 535.

not passivity. Passive institutional investors in a way protect the wrong acts of the directors.

Institutional investors should keep themselves aware of the total profits earned by the company, to see whether the company has declared its correct dividend and whether there is any malafide on the part of directors. The directors should be independent and impartial. It was observed in the Cadbury Report 1992 that

> "Every public company should be headed by an effective board which can both lead and control the business."[89]

The Report stressed upon the need of more independent non-executive directors in the following words:

> "An important aspect of effective corporate governance is the recognition that the specific interests of the executive management and the wider interests of the company may at times diverge, for example over takeovers, boardroom succession, or directors' pay. Independent non-executive directors, whose interests are less directly affected, are well-placed to help to resolve such situations."[90]

More independence on the part of the directors reposes more confidence in the institutional investors and they come forward with their large shareholdings, to invest in that company. The investee company enjoying good reputation of being fair and just towards its investors attracts more investments. The demand of good corporate

---

89. Supra note 6.

90. Ibid

governance practices by the institutional investors and its implementation by the investee company , result in increase in share values, transparent accounting measures, fair disclosure of financial position , correct declaration of dividend and most important of all the impartiality and independence of the Board.

2.7 Auditing:

The main purpose of auditing is to see whether the company has fairly disclosed its financial position in its financial statements. Although, the direct corporate governance responsibility does not rest upon the auditors as it is the job of the management; however, the auditors are expected to keep a check upon the information aspects of the company. Enron collapsed in the US because of mismanagement and misappropriation of accounts. WorldCom and Tyco met the same fate. The internal auditors well acquainted with the financial position of the company may exploit their authority by concealing true financial status of the company and by embezzling the accounts in collusion with the management.

The auditors of the company being the ultimate 'watchdog, of shareholders are expected to conduct the audit in accordance with the prescribed rules and procedures. Auditors should avoid performing their duties indulgently. The auditors are required to make a qualified report in case they find any irregularity in the books of account. Section 255 of the Companies Ordinance 1984, casts a statutory duty upon the auditors of a company to provide complete and true information to the shareholders about the accounts of the company in their report.[91]

---

91. Supra note 17 at page 675

The auditors should act responsibly while auditing the books of account and reporting thereon. The shareholders of the company are infact the providers of the company's capital. They make investments in the company in order to maximize their investment value. The investors are not in a position to control the affairs of the company pragmatically. The directors and the management of the company are the ultimate runners of the corporate entity. Therefore in order to provide safeguard to the investors who are the real beneficiaries, the law has provided the course of auditing.

The auditors are the protectors of the investors' interests. They have to see that the management has not misappropriated or embezzled the accounts of the company. Access to the books of account is granted to the auditors with an aim to ensure that directors have carried out the business in accordance with sound business principles and prudent commercial practices. They have to ensure that no money of the Company has been wasted or misappropriated. In their report they are expected to draw the true financial status of the company without fear or favour. The law, has therefore, made them liable by providing penal provisions in case of non-compliance with the statutory rules. Therefore, the auditors should be extremely vigilant while performing their duties.In the matter of 'M/s. Hafizullah & CO. Chartered Accountants' the Securities and Exchange Commission of Pakistan imposed a penalty under section 260 of the Companies Ordinance 1984, upon each partner of Hafizullah & CO. in the shape of fine of rupees 15000. The auditors had failed to perform their duties with reasonable skill and care and failed to make report pertaining to the financial statements of the company under audit in accordance with section 255 of the Ordinance.[92]

---

92. 2006 C L D 588

Section 254(3) (a) of the Companies Ordinance 1984 debars the director, officer or employee of a company from holding the office of the auditor.[93] Shareholders get the righty to bring legal action against such a person. Any person making default in compliance with the aforesaid provision is liable to be penalized under section 259 of the Ordinance. A fine to the tune of rupees fifty thousand may be imposed upon such a person under section 259.[94] In the case of 'Waseem Ahmad Siddiqi versus Zafar-ul-Haq Hijazi', the Securities and Exchange Commission imposed fine under section 259 of the Companies Ordinance 1984, upon the petitioner for acting as auditor of the company despite being its director.[95]

Section 257 of the Companies Ordinance 1984 requires the report of audit to be signed by the person who conducted the audit.[96] The said report is usually read over in the Annual General meeting and is open to inspection by the shareholders as per section 256 of the Ordinance. [97] In re 'Mehmood Ali Khan. Chartered Accountant and Nasim Akhtar' the Executive Director of Enforcement and Monitoring Division of the Securities and Exchange Commission found during examination of financial statements of the company that auditor's report was not signed by an appointed auditor of the company but by another person. The appointed auditor as well as the signatory took the defence t hat they

---

93. Supra note 17 at page 672

94. Ibid at page 696

95 2006 C L D 298

96. Ibid at pages 688-689.

97. Supra note 17 at page 687

had a verbal partnership and the signatory had signed the report in that context. The Executive Director of the Commission being dissatisfied with such the plea imposed fine on both the persons under S.260 (1) read with S.476 of Companies Ordinance. The petitioners filed appeal before the Appellate Bench of the Securities and Exchange Commission. The Commission dismissed the same by holding that the auditor's report could be signed by its author only and none other as per section 257 of the companies Ordinance 1984.[98]

Section 255 of the Companies ordinance sets out the powers and duties of an auditor. Any auditor travelling beyond the scope of his powers is to held accountable under sections 260, 476 and 492 of the Ordinance. In the matter of 'Mehboob Sheikh and Co. Chartered Accountants', the auditor company committed certain irregularities during auditing and contravened the terms of 'International Accounting Standards' and 'International Standards on Auditing'. As per section 255 it is a mandatory requirement for the auditor to make a report to the effect as to whether the accounts of the company conform to the approved standards of accounting. The auditor is also required to follow the approved standards while auditing the books of account. Penalty of fine Rs.25,000 was imposed on auditing company under S.260(1) of the Companies Ordinance, 1984.[99]

The above mentioned provisions of the Companies Ordinance 1984 reveal that the vigilant and activist shareholders can invoke the legal provisions wherever they found that the auditors are not acting in the interest of the shareholders. The various areas discussed in this chapter clearly envisage that the shareholders can

---

98. 2002 C L D 1164

99. 2008 CLD 305

influence the performance of the investee company by prudent exercise of activism.

Chapter III

3.1 Legal Environment in Pakistan for Institutional Shareholder Activism

A strengthened legal and regulatory framework is pertinent for a progressive corporate sector. This framework should be devised in such a manner that it should be in accord with the requirements of the corporate structure. The promulgation of corporate laws by itself is not sufficient for a well governed corporate system but it is the implementation and enforcement of these laws that matters. A legal system can work effectively only where the system to regulate these laws is also efficient. The edifice of regulatory framework can be built upon an effective legal system.

The principle of checks and balances is an important feature of sound legal system. Political pressures and weak corporate laws destroy the institutional growth of a country. A healthy environment is necessary for the flourishing of institutions. The development of the economy depends much upon the scheme of laws and policies introduced from time to time. Law is not static but dynamic. It can change its course according to the needs and requirements of a particular governing system. The dynamism of law allows it to bring in its fold new rules, policies and procedures.

Static laws and procedures result in the stifling of business expansion and economic growth. Therefore, proper updating of laws, rules and procedures is must for the stimulation of economic development. Institutional uncertainty often results due to weak legal and regulatory laws and the institutional investors avoid making investments in such a situation. This institutional uncertainty thus constrains the market development. The countries with effective laws and procedures progress by leaps and bounds. The

growth of a corporate sector depends upon the strong legal environment of a country. The country with proper laws, procedures and implementation gives boost to its economy.

In the proper enforcement of the laws all the three pillars of the State i.e. executive, legislature and the judiciary play their part. The legislators and the Government should take such legislative measures as would provide such an atmosphere to the institutional investors where they can play a progressive and active role. An effective legal framework for corporate governance system and efficient regulatory system can make the atmosphere feasible for the institutional growth.

The implementation of corporate laws and codes depend much upon the corporate culture of a particular country. USA introduced Sarbanes Oxley Act in 2002 in order to provide stricter and efficient corporate governance standards for avoiding future corporate collapses. It also introduced major changes in the listing standards for the New York Stock Exchange (NYSE) and NASDAQ stock market. These changes fostered an environment for increased shareholder activism. Pakistan being an underdeveloped country with weak economical structure shows poor sense for adoption of good corporate governance practices. Every sector in Pakistan is being politicized and laws are made and enforced not for the protection of general public but for extending favouratism to certain groups. Corporate sector is no exception. Most companies are owned by feudalists who do not enlist their companies on the stock exchanges in order to avoid payment of taxes etc.

Corporate Governance structures are designed with an aim to provide fair return to the shareholders on their investments. The efficient allocation of capital resources is possible only where the corporate governance structure is strong. The economies with

weak corporate governance structures can not bring positive changes for the improvement of investment climate and economic growth. Pakistan being an emerging market economy lacks the proper investor protection due to weak corporate governance structures.

Foreign Institutional investors do not prefer to make investments in Pakistan due to its underdeveloped corporate structure and no protective measures for investors. War on terrorism has also moved foreign investments away from the capital market of Pakistan. Energy crisis has also stabbed the corporate sector and most of the industries have stopped working. The domestic institutional investors, therefore, being an influential force can be a ray of hope in the gloomy corporate environment of Pakistan. Institutional investors can flourish only when a healthy legal environment is available to them for making investments and exercising activism.

The general law prevalent and applicable to all the companies in Pakistan is the 'Companies Ordinance 1984'. Stock exchanges are regulated by the 'Securities and Exchange Ordinance 1969' and the 'Securities and Exchange Commission Act 1997'. For Banking Companies, the legislators have provided the 'Banking Companies Ordinance 1962'. Similarly other legislations include 'Modaraba Companies and Modaraba (Floatation and Control) Ordinance, 1980', 'Insurance Act 1938', 'Insurance Ordinance 2000', 'Listed Companies (Substantial Acquisition of Voting Shares and Take-overs) Ordinance, 2002' and the like. There are so many laws prevalent in the Country yet the environment for corporate governance is not healthy. The reason being that many laws overlap, others lack proper amendments and implementation. Some overlapping provisions of the Companies Ordinance 1984 and the Code of Corporate Governance

2002 , deficient provions of the Ordinance , Code , Rules and Regulations are discussed as under:-

(3.1.1) Section 160(3) of the Companies Ordinance 1984 and Para (x) of the CCG

Many provisions in the Companies Ordinance pertain to the corporate governance. Similarly the Code of Corporate Governance 2002 also aims at providing best corporate practices. However, many principles of the Code overlap with the provisions of the Companies Ordinance. For instance, section 160(3) of the Companies Ordinance 1984 requires the general meeting of a company to be presided over by the Chairman of the Board of Directors.[100] The Code on the other hand in Para (x), makes it mandatory upon the Chairman of the listed company to preside over the meetings of the Board. [101]

(3.1.2) Section 173(1) of the Companies Ordinance 1984 and Para (xii) of the CCG

Similarly, section 173(1) of the Ordinance places the responsibility of maintaining proper record of the minutes of proceedings of AGMs and the directors, upon the company itself [102] while as per Para (xii) of the Code the Chairman of the listed company is required to perform this task. [103]

(3.1.3) Section 187(j) of the Companies Ordinance 1984 and Para (v) of the CCG

Section 187(j) completely debars a person to act as the director of a listed company

---

100. Supra note 17 at page 476

101. www.secp.gov.pk/corporatelaws/pdf/CodeofCorporateGovernance.pdf (accessed August 5, 2009)

102. Supra note 17 at page 506

103. Ibid 101

who himself as a member of the stock exchange is engaged in the business of brokerage. Moreover he\she cannot also act so if his/her spouse is a member of the stock exchange and carries out the business of brokerage.[104] On the other hand para (v) of the Code allows such a person to act as director of a listed company if he seeks exemption from the applicability of this rule, from the Securities and Exchange Commission of Pakistan. [105] This provision of the Code creates confusion for the reason that the Ordinance is to be followed by all the companies compulsorily while contravention of the same entails imposition of penalty while the SECP also requires complete compliance of the Code by the listed companies.

(3.1.4) Section 224 of the Companies Ordinance 1984 and Para (xxvi) of CCG

Section 224 of the Companies Ordinance 1984 requires the directors, officers, major shareholders and any person owning more than ten percent of equity securities as beneficial owner of a listed company, to make a report of any gain made by them from sale or purchase of such securities within a period of less than 6 months .The concerned person making such gain is also required to tender the same to the company and make intimation to this effect to the Registrar and the Commission.[106]The Code of Corporate Governance on the other hand in Para (xxvi) does not prescribe any time period and simply requires the person making such gain, to notify the same in writing along with the relevant record to the Company Secretary. The Company Secretary then

---

104. Supra note 17 at page 532

105. Supra note 101

106. Supra note 17 at page 607

has to place such notice and record before the Board of Directors in its meeting. The Code also prescribes that the listed company shall determine a 'closed period' before the announcement of results, interim or final as the case may be. During the closed period, no person shall be entitled to deal in the shares of that company. [107]

(3.1.5) Para (iii) of CCG

The Code in Para (iii) postulates that a person cannot act as a director of the listed company if he is also the director of ten other listed companies. [108] Meaning thereby that a person may act as the director of atleast ten listed companies at the same time. A person acting as the director of ten listed companies cannot do justice even with the affairs of one company of the ten. The office of the director carries too much responsibilities and the person acting as director is required to show highest level of rationality and prudence in settling the affairs of the company. Such level of prudence and rationality cannot be expected of a person who holds the directorship of so many companies. The Companies Ordinance, on the other hand, is silent as to the number of companies, of which a person may act as director at the same time.

(3.1.6) Para (xvi) and (xvii) of CCG

The Code in Para (xvi) while setting out the qualifications of the Chief Financial Officer , prescribes that the person so acting should be either a member of a "recognized body of professional accountants" or a graduate having experience of five years in handling financial and corporate affairs of the listed company, bank or financial

---

107. Supra note 101

108 Supra note 101

institution. This provision of the Code places an ordinary graduate at par with the Chartered Accountant. The success of a company depends upon the transparency and fairness of its financial position. The Chief Financial Officer being responsible to ensure such transparency and fairness should be a professional Chartered Accountant and not an ordinary graduate.

The Code does not debar a person from acting as the Chief Financial Officer as well as the Company Secretary at the same time. A person fulfilling the criteria of qualification as set out in Para (xvi) and (xvii) may act as the Chief Financial Officer as well as the Company Secretary although propriety demands that separate persons should hold these offices. Responsibilities of one office should be exclusive and independent of the other office. Good corporate governance standards can be ensured only when every person carries out his responsibilities exclusively with due diligence. Overburdening a person with two or more offices will result in the reduction of good quality of corporate governance norms.

(3.1.7) Section 190 of the Companies Ordinance 1984

There are many provisions under the Companies Ordinance 1984 which prescribe nominal penalties for the contravention of the ordinance. Section 190 prescribes a penalty of fine of rupees ten thousand or imprisonment for two years for an undischarged insolvent who acts as the director, chief executive or managing agent of the company.[109] The courts usually impose fine upon such a person. Therefore the amount of fine to be imposed must not be less then 50.000 atleast. The reason being that those persons who

---

109. Supra note 17 at page 535

being bankrupts act as directors, managing agents or chief executives , are likely to act to the detriment of the company and its shareholders. Therefore exemplary punishments should be imposed in order to prevent such behaviour for future prosperity of the company.

(3.1.8) Section 189 of the Companies Ordinance 1984

Section 189 of the Companies Ordinance prescribes the imposition of fine of just 200 rupees for each day upon the person who is not qualified to act as director or chief executive of the company, but he acts so.[110] The amount of fine should not be imposed on daily basis but should be a fixed amount. Whether the unqualified person acts for few days or so many days as director or chief executive he should be penalized strictly. A person not qualified to act as director or chief executive, if makes gain of huge amount of money and also acts in detriment to the interest of investors in just few days, then paying 200 rupees per day does not cost him anything.

(3.1.9) Section 193 of the Companies ordinance 1984

Section 193 of the Companies ordinance 1984, postulates the quorum for a meeting of directors of a listed company should not be less than four or one third of the total number of directors. If a meeting is held without quorum then the chairman and the directors entail liability to pay fine of ten thousand rupees. [111] This amount of fine should be enhanced as the public money of investors is involved in the listed companies. Moreover, the meetings of the Board decide the fate of the investors. If the meetings are not held properly then the ultimate sufferers are the institutional investors who have

---

110. Supra note 17 at page 535

111 Supra note 17 at pages 537-538

invested their huge shareholdings in the company.

(3.1.10) Section 197 of the Companies Ordinance 1984

The companies are not allowed to make contributions to any political party or any person for political purpose under section 197 of the Companies Ordinance 1984. A fine of ten thousand rupees may be imposed upon such a company and the director or the concerned officer may be subjected to imprisonment for two years or fine.[112] The section does not prescribe the fix amount of fine to be imposed upon the director or the officer contravening the provisions of section 197. The competent authority is left at liberty to impose a fine of just two rupees even under this section. This section clearly provides protection to politicians. Such provisions of law require to be amended and no favour should be accorded to a particular group.

(3.1.11) Section 197-A of the Companies Ordinance 1984

The company making gifts to its members in the meetings is liable to be proceeded against under section 197-A of the Ordinance. Penalty in the shape of fine of rupees five thousand may be imposed upon such a company or the officer concerned. In case of a listed company the amount of fine should be higher as compared to an unlisted company. The distribution of gifts in AGM or other meetings to the members of choice is clearly injurious to the healthy growth of capital market. It also interferes in the progress of sound corporate practices and culture.

The above mentioned provisions of the Companies Ordinance as well as many other provisions , do not prescribe the adequate penalties and remedies for

---

112. Supra note 17 at page 555

the contravention of laws. These sections should set out such penalties that the contraveners as well as the persons involved in the management should not dare to exploit the legal provisions. The stability of a corporate structure depends upon strong legal environment. The weaknesses in the legal framework also weaken the corporate edifice, ultimately leading to its deterioration. Investors do not prefer to put their investments at stake if the investee company is unable to protect their investments. Therefore, for the healthy promotion of corporate governance culture, healthy, strict and up to date laws are required.

The 'Code of Corporate Governance 2002' although contains so many principles of corporate governance of international standard yet in Pakistan we see that the companies are reluctant to adopt the same. The main reason being that the manual of the Code of Corporate Governance available on the website of the Securities and Exchange Commission of Pakistan in its opening page sets out that that the manual is for guidance only and no legal action can be brought against the company that fails to comply with the provisions of the Code. This opening Para should be removed from the Code to create a sense of compliance and responsibility in the listed companies.

(3.1.12) Rules and Regulations

There are also certain Rule s and Regulations that create embargo upon the institutional investors from exercising activism. For instance, Rule 4 of the 'Investment Companies and Investment Advisors Rules, 1971' prescribes the limit of not less than one hundred million rupees of capital for an investment company to commence its business. Rule 6 provides that an investment company at a time cannot

hold more than ten percent of the total paid up capital of the investee company.[113] Similarly, Rule 4 of the 'Asset Management Rules, 1995' prescribes the limit of not less than thirty million rupees of paid up capital for an asset management company for commencement of business. The investment policy as laid down in Rule 13(4) allows the investment company to invest upto twenty five percent of its net asset values in the securities of one any sector of the stock exchange. [114] 'Prudential Regulations for Modarbas, 2000' allows a modarba company to make investment in a listed company, not exceeding ten percent of the total paid up capital of that company or five percent of its own equity. These rules and regulations create obstacles for institutional investors in making investments and playing their part in the corporate governance of the investee companies.[115]

The Securities and Exchange Commission of Pakistan is empowered under section 34(4) of the Securities and Exchange Ordinance 1969, to make a direction to the Stock Exchange to make, amend or rescind any regulation already made within a certain period of time.[116] By exercising power under the said provision of law the Securities and Exchange Commission of Pakistan may endeavour to remove the confusions arising out of the overlapping provisions of various legislations pertaining to the enforcement of

---

113. INVESTMENT COMPANIES AND INVESTMENT ADVISERS RULES. 1971 [Gazette of Pakistan Extraordinary. 12th March. 1971]

114. ASSET MANAGEMENT RULES, 1995 [Gazette of Pakistan, Extraordinary, Part 11, 20th May, 1995]

115. Supra note 86

116. Securities and Exchange Ordinance 1969 , page 30-31, PLD 1970 Central Statutes.

corporate governance standards. Moreover, outdated laws may be updated by making appropriate amendments.

3.2 Measures To Improve Institutional Shareholders Activism and Corporate Governance of the Investee Companies

The Securities and Exchange Commission may take the following measures to improve institutional shareholders activism and corporate governance in the investee companies.

(3.2.1) Supervisory Board

The Code of Corporate Governance for listed companies in China provides for the establishment of a 'Supervisory Board'. According to clause 59 of the Code "The supervisory board shall supervise the corporate finance, the legitimacy of directors, managers and other senior management personnel's performance of duties, and shall protect the company's and shareholders' legal rights and interests". [117] In the same line the Code of Corporate Governance of Pakistan may prescribe the establishment of a supervisory board which should conduct the supervision of managers, directors and auditors. The financial matters of a company should be open for supervision and examination by the supervisory board.

The supervisory board of a company should comprise of those persons as members who are well acquainted with the existent corporate laws and procedures. The supervisory board should be governed by standardized rules and procedures inculcated in the articles of association of a particular company. The supervisory board should act as a

---

117. www.csrc.gov.cn (accessed Aug 17, 2009)

bridge between the company and its shareholders. The supervisory board should be in a position to make consultation with the institutional as well as individual shareholders with respect to the settlement of issue creating conflict of interests.

The supervisory board shall be able to convene its meetings periodically. These meetings should be attended by the directors, managers and the auditors to discuss important matters of the investee company and to answer queries made by the board. In Annual General Meetings the recommendations of the supervisory board should be taken into consideration. The supervisory board can improve the corporate governance of the investee companies, if it is empowered to report directly to the regulatory authority, any violation of law by the company or its officers. The establishment of a supervisory board will improve transparency of financial reporting and will curb corruption in the management.

(3.2.2) Corporate Strategy Committee

The Code of Corporate Governance of China also speaks of a "Corporate Strategy Committee". Clause 53 of the code postulates that "the main duties of the corporate strategy committee shall be to conduct research and make recommendations on the long-term strategic development plans and major investment decisions of the company". [118] The establishment of a corporate strategy committee by the companies will be a novel concept in Pakistan; however, it will improve the overall efficiency of the companies. In foreign countries every governing entity has a department for the research work. The corporate strategy committee should comprise of members from senior management of

---

118 Supra note 117

the company and professional researchers having experience in the corporate research. If every listed company also hires a professional for the research of up to date corporate laws, procedures, rules and regulations from local as well as foreign jurisdictions, then it will bear direct impact upon the improvement of corporate governance standards.

The corporate strategy committee should be able to assess the impact of prevalent corporate laws and regulations upon the working of the company. It should point out any rigidities or flexibilities in the laws. The committee should be able to propose measures that may be taken into consideration by the corporate regulators while formulating new laws and policies. The company's overall assessment as to the compliance with the corporate laws and procedures should be made by the corporate strategy committee and default on the part of the company should be reported to the regulatory authority.

(3.2.3) Negotiations with the Investee Companies

The 'Combined Code on Corporate Governance, 2008' UK emphasized the need for dialogue between the institutional investors and the investee companies in the following words:

> "Institutional Shareholders should enter into a dialogue with the companies based on the mutual understanding of objectives". [119]

There is a good example of a settlement of directors' remuneration issue through a constructive dialogue between the institutional investors and the investee company. In 2002, the institutional investors having large shareholdings in the Kingfisher plc (a UK based international retailer) severely criticized the directors' remuneration packages

---

119. www.frc.org.uk(accessed Aug 20,2009)

announced by the company. The company encouraged dialogue with its institutional investors and entered into a compromise with them whereby the remuneration terms were revised according to the demands of the institutional investors. [120]

Major controversies can be resolved through mutual consultation and deliberation. The Code of Corporate Governance of Pakistan does not speak of any dialogue or mutual understanding between the institutional investors and the investee companies'. Therefore, the code should specifically incorporate a particular clause to this effect in its provisions. Inserting such a clause in the Code will provide a specific way to the investors to solve their disputes and problems through negotiations first instead of invoking legal provisions. The institutional investors may get aggrieved of any particular decision of the board, excessive remuneration of the directors, undue favour to some investors or lack of transparency and disclosure policies. To settle all these issues, a dialogue between the investee company and the institutional investors will be a more prudent option.

(3.2.4) Responsibility to Vote by Institutional Investors

The institutional investors in Pakistan usually do not prefer to vote and keep themselves aside from the governance affairs of the investee company. Such a practice should be discouraged and they should be bound legally to cast their votes. Institutional investors being major shareholders of the investee company, by effectively exercising their voting power, can turn the tide of any unfavourable decision taken up by the management. Non- exercise of voting power by the majority shareholders, in fact allows

---

120. Christine .A. Mallin, Corporate Governance, p.95, Oxford University Press Inc. New York, 2007.

the management of the investee companies, to commit malpractices and severe irregularities by making decisions detrimental to the shareholders' interests.

In UK, the institutional investors have been encouraged specifically to exercise their rights of vote. The 'Combined Code on Corporate Governance, 2008' UK , in Section 2 clause E.3 specifically places a responsibility upon the institutional investors to use their right of vote in the following words:

> "Institutional shareholders have a responsibility to make considered use of their votes.....Institutional shareholders should take steps to ensure their voting intentions are being translated into practice. Institutional shareholders should, on request, make available to their clients information on the proportion of resolutions on which votes were cast and non-discretionary proxies lodged. Major shareholders should attend AGMs where appropriate and practicable. Companies and registrars should facilitate this". [121]

In the Code of Corporate Governance of Pakistan, the role of the institutional investors has not been defined specifically. Moreover, no such clause pertaining to the exercise of voting power by the institutional investors has been inserted by the Pakistani Code. Active participation by the institutional investors in the investee company's affairs can be expected only when a sense of responsibility to cast their votes, is created through legal provisions. The Securities and Exchange Commission of Pakistan in order to enhance the role of institutional investors in the corporate governance of the investee companies should allocate a separate section to the 'Institutional Shareholders Activism'

---

121. Supra 119

in the Code of Corporate Governance.

Voting by the institutional investors should be encouraged by inserting a separate clause titled 'Institutional Shareholder Voting' in the code of Corporate Governance. Non- exercise of voting power by the institutional investors should be curbed by way of imposition of penalty in the shape of fine etc. Moreover, electronic voting system should also be introduced instead of a paper based system, in order to ensure more transparency of the voting process.

(3.2.5) Council of Institutional Investors

The Securities and Exchange Commission of Pakistan established the 'Institute of Corporate Governance' under section 42 of the Companies Ordinance, 1984. The purpose of establishment of the institute is to promote healthy corporate governance practices in Pakistan. The Commission should also establish a 'Council of Institutional Investors' in Pakistan. In America the Council of Institutional Investors is working as a non- profit association. The council has been established there with an aim to provide information to the public, investors, and the policy makers about good governance practices. In Pakistan as well such a council should be established to rejuvenate and strengthen corporate governance practices.

The council shall act as a non profit association and the institutional investor foreign as well as local, making investments in Pakistani equities, must be given membership. The council should held conferences of the institutional investors periodically in order to create awareness about corporate governance system and exercise of activism by the investors. Experts in the field of corporate law should also be

participants of such conferences, so as to point out weaknesses in the prevalent laws and to suggest the measures that could be taken up by the corporate regulators.

The council shall grant membership to all the institutional investors of the listed companies. The Council of Institutional Investors should encourage investments by the institutional investors local and foreign, in all the three stock exchanges of the country. The Council should call its annual meetings to discuss the problems faced by the institutional investors in the corporate sector. The Council should be empowered to collect data of the institutional companies and the investee companies and to report to the SECP any violation of corporate governance norms by the investing and the investee company. Proper record of the poorly performing companies should be maintained and they should be kept on 'focus lists'. The company giving poor performance should be held answerable through explanation and imposition of fine.

In America the Council of Institutional investors is playing a significant part in enhancing the corporate governance role. The Council occasionally holds seminars, to educate investors and the public about corporate governance principles and standards. It also solves the issues concerning the investments and shareholders rights. In the same line, the establishment of a Council of Institutional Investors in Pakistan, will bridge the gap between the Board and the investors. It will also enhance the confidence of the general public in the institutional companies. The Institutional investors owe fiduciary duties towards the public as they hold the public money. It is, therefore, incumbent upon them to protect the interests of the public by making prudent investments.

The Council, if working, effectively can arouse the passive institutional investors' souls and could lead them towards activism in Pakistan. The seminars and conferences

held by the council will benefit the institutional investors in educating them about demanding the implementation of sound corporate governance practices. The Council will also help in pointing out irregularities committed by the investing and investee companies in the compliance of prevalent laws and procedures. Primary objective of the Council should be to encourage the Institutional investors to become activists in order to ensure that the shareholders interests are not put at stake while taking corporate actions.

The Council of Institutional Investors will observe the prevalent corporate laws and will make recommendations to the Securities and Exchange Commission of Pakistan to update the laws and policies according to the market requirements. The establishment of a Council of Institutional Investors in Pakistan will give stability to the capital market thus contributing towards the robust growth of the corporate sector.

(3.2.6) Mandatory Independent Directors.

The Code of Corporate Governance of Pakistan in Para i (b) provides for the appointment of atleast one independent director representing the institutional investors. The said clause of the code reads as follows:

> "The Board of Directors of each listed company includes atleast one independent director representing institutional equity interest of a Banking company, Development Financial Institution, Non-Banking Financial Institution (including modarba, leasing company or investment bank), mutual fund or insurance company".[122]

The Code although provides for the appointment of an independent director by the

---

122. Supra note 101

institutional investors, however, this provision is voluntary and not mandatory. In order to ensure more transparency, it is the need of the time that the Code shall compulsorily obligate the appointment of independent directors representing the institutional investors. Moreover, institutional investors being major shareholders of an investee company should be given more representation by appointing atleast three directors instead of one. The reason being that just one independent director on the Board cannot make any decision singularly if all the other directors of the board are against him.

(3.2.7) Legal and Accounting Experts

The Code of Corporate Governance 2002 should encourage the listed companies to employee legal and accounting experts. Legal and financial diligence will be expected of these experts in assessing the investee company's record in compliance with the prevalent laws, rules and regulations. These experts should be in apposition to advice the investing as well as investee companies to adopt legal and accounting standards of international level in order to improve their overall efficiency

(3.2.8) Mandatory Educational Qualification and Certification for Directors

There is no minimum educational qualification for a person to act as a director of a listed company in Pakistan. Neither the Companies Ordinance 1984 nor the Code of Corporate Governance 2002 prescribes any educational qualifications for the office of directorship. The office of directorship is a very responsible office and for the efficient working of the same the directors must be highly educated and experienced. Directors with proper educational qualifications and professional experience will be in a better position to implement the corporate governance principles and standards in their true perspective. Uneducated and non-professional persons acting on the posts of directors

cannot act with rationality and prudence, resultantly putting shareholders investments at stake. Therefore, special provisions should be made in the Companies Ordinance 1984 and the Code of Corporate Governance 2002, prescribing the specific educational qualification and experience for the office of directorship.

The law should also provide for mandatory certification for directors including mandatory training and examinations with an aim to improve competency of the directors. There is a dire need for certification of the directors in order to equip them with the corporate laws and practices in Pakistan. The Institute of Corporate Governance already working in Pakistan, should strive to properly train the directors in the field of corporate law. Non-attending of trainings and non- passing of examinations should disqualify a person from acting as the director of a listed company. Mandatory certification for the directors will help in reducing the corporate failures and will strengthen the accountable and professional role of the directors. The requirement of minimum educational qualifications for the investing as well as investee companies should be the same. Institutional investors with more experienced and well educated directors will show more activism.

(3.2.9) Effective Monitoring By the Institutional Investors

The effective monitoring of an investee company's performance by the institutional investors is pertinent for increased activism. This activism may be exercised by the institutional investors by periodically considering the annual accounts, board structure and audit reports of the investee company. The institutional investors should attend the meetings of the investee company regularly and should make effective exercise of voting power. They should also ensure that the independent directors are representing

their true causes. They should also ensure that their proposals have been presented in the meetings of the company properly and have been taken into consideration while solving contentious issues. An effective monitoring of the investee company's performance will identify the controversies at an initial stage and will maximize the shareholders' wealth.

(3.2.10) Effective Internal Controls

An effective internal control system is necessary for the smooth functioning of a corporate entity. External controls can work easily when the internal control system of a company is strong. In US, the Sarbanes-Oxley Act of 2002 particularly requires in Section 404 that the companies should publish in their annual reports about the effectiveness of the internal control systems. In Pakistan as well the companies whether small or large should be made responsible for furnishing information about their internal control systems in the annual reports. Specific provisions to this effect may be introduced in the Code of Corporate Governance.

(3.2.11) Removing Legal Constraints

As discussed earlier the legal environment in Pakistan is not conducive for institutional shareholders activism. In order to ensure proper representation and increased activism by the institutional investors in the corporate sector, laws and policies need to be reviewed. Legal hurdles need to be removed and laws should be made flexible to give more room to the institutional shareholders activism. The Companies Ordinance 1984 needs to be amended and updated, inserting stringent provisions for violation of corporate governance norms. Similarly various rules including the 'Investment Companies and Advisors Rules' 1971, 'Asset Management Companies Rules' 1995 and 'Prudential Regulations for Modarabas' 2000 also require necessary amendments in order to bring

more investments by the institutional investors on stock exchange. The Code of Corporate Governance 2002 should be reviewed by the Securities and Exchange Commission of Pakistan and provisions relating specifically to the role of institutional shareholders in the corporate governance may be inserted.

Moreover, as discussed earlier, provisions pertaining to educational qualifications for directors and their mandatory certification, establishment of corporate strategy committee, council of institutional investors, supervisory board, effective monitoring, mandatory independent directors and responsible voting should be made in the Code. Other regulations and policies lacking in ensuring proper compliance of corporate governance policies, should be reviewed in consultation with the legal and corporate experts. Passive behavior on the part of shareholders should be discouraged. Prudent rules and procedures should be laid down to attract more institutional investments from foreign as well as domestic investors.

There should be an attitude of zero tolerance by the corporate regulators, for the violators of the Code and prevalent corporate laws. Strict actions should be taken by the Commission and the Courts, against the management and the companies concerned for any contravention of the law. Strengthening of the legal tools can bring stability to the capital market and restore the investors' confidence.

3.3 Conclusion:-

Institutional shareholders activism has not taken its roots in the Pakistan's corporate sector. The reason is not that the corporate scandals like Enron and WorldCom have not happened here but the main reason is the lack of interest by the institutional investors in the corporate governance system. Moreover, the legal environment of the country is also not feasible for the same. The preponderance of family owned companies has also limited the scope of the institutional shareholders activism in Pakistan.

Pakistan is passing through hard times. Foreign investments have since long departed from the capital market of Pakistan due to the prevailing pathetic environment in the country. War on terror, energy crises, debt liability and other factors have brought the growth of the economy of Pakistan to a standstill. Foreign investors are reluctant to put their investments on the stock exchange of Pakistan due to prevalent instability. The only way available to the country to boost its economy is to raise capital from the domestic investors both individual as well as institutional.

Companies complying with the corporate governance norms can give greater dividend yields as compared to those companies which do not follow corporate governance principles. Substantial changes in the performance of an investee company are not possible without introducing significant changes in the legal environment alongwith the enforcement tools. The purpose of implementation of the corporate governance system is to monitor the market in order to make it profitable for a country's economy. The companies complying with sound corporate principles always contribute towards a well established, stable and strengthened market structure.

The institutional investors holding large blocks have the capacity to discipline an unruly corporate entity. Passivity on the part of institutional investors paves a way for mismanagement and corrupt practices by the managers of the investee companies. Institutional investors through active participation in the managerial affairs of the investee company can reduce the risk of malpractices and mismanagement. As compared to the individual investors the institutional investors having large shareholdings can exert great influence upon the investee company, by monitoring its performance.

Demanding the implementation of corporate governance practices by the investee company is a strong device in the hands of institutional investors. Active participation by the institutional investors in the meetings and voting of the investee company can ensure transparency and rationality by the Board in taking important decisions. The management of the investee company acting in detriment to the shareholders' welfare may be held accountable by the institutional investors. Such an activism is expected from the institutional investors only when the legal and corporate environment of the country is supportive of the same.

In order to enhance the role of institutional investors in the corporate sector, the SECP and the legislators are required to provide specific provisions in the prevalent laws and policies to this effect. The Companies Ordinance and other related laws need to be amended as suggested in chapter three of this research paper. The Code of Corporate Governance also requires to be reviewed. By strengthening the role of institutional investors legally, the corporate governance practices will automatically improve. The corporate structure of a country where the corporate governance standards are complied with in letter and spirit, always contribute towards the growth of its market and attract more and more investments.

Similarly, in order to inculcate corporate governance sense in the investment and investee companies in Pakistan, corporate laws and procedures have to be strengthened. Institutional investors , being major shareholders, by exercising activism, can stabilize the deteriorating economy of Pakistan by making more investments and demanding the handling of the same in accordance with best corporate governance practices.

Bibliography

- Agrawal, A. and C.R.Knoeber (1996)*Firm performance and mechanisms to control agency problem between managers and shareholders*, Journal of Financial Quantitative Analysis 31
- Bethel, J., J. Leibiskind and T. Opler, (1998) Block *Share Purchases and Corporate Performance*, Journal of Finance 53, 605-635
- Bhide, A., (1990) *Efficient markets, Deficient Governance: U.S. Securities Regulations Protect Investors and Enhance Market Liquidity. But Do They Alienate Managers and Shareholders*? Harvard Business Review 72, pp128-140.
- Cadbury Andrian ., (1992)*Report of Committee on the Financial Aspects of Corporate Governance* , ,London : Gee & Co.Ltd..
- Connell, JJ. Mc and H.Servaes, (1990) *Additional Evidence on Equity Ownership and corporate Value*, Journal of Financial Economics 27, 595-612
- Chung, R, M.Firth and J. Kim, (2002) *Institutional Monitoring and Opportunistic Earnings Management,* Journal of Corporate Finance 8, 29-48.
- Greenbury, Richard, (1995) *Directors Remuneration*, London. : Gee & Co Ltd.
- Grossman, S., and O. Hart, (1980) *Takeover Bids, the Free Rider Problem and the Theory of the Corporation*, Bell Journal of Economics 11, pp .42-64.
- Gillan, Stuart L. and Laura T. Stark, (2007) *The Evolution of Shareholders Activism in the United States,* PhD diss.,University of Texas, page 3.
- Hampel, Ronnie., (1997) *Committee on Corporate Governance: Preliminary Report* , London : Gee & Co .Ltd.

- Hawley, James P. & Andrew T. Williams, (2000) *The Rise of Fiduciary Capitalism*, Philadelphia: University of Pennsylvania Press.
- Maug, E. (1998), *Large Shareholders as Monitors: Is there a trade off between liquidity and control?* Journal of Finance 53, 65-98.
- Monks, A.G. and N. Minow.,(2004) *Corporate Governance,* England: Blackwell Publishing, *p.* 98,
- Pinto, Moshe., (2005) *The Role of institutional Investors in the Corporate Governance,* (PhD diss., University of Hamburg and Bolonga) page 1
- Roe, M., (1990). *Political and Legal Restraints on Ownership and Control of Public Companies*, Journal of Financial Economics 27, pp .7-41
- Rubach, Michael J. *Institutional shareholder activism: the changing face of corporate ownership*, (1999) New York Garland Publishing Inc, p.19.
- Shaheen, Nazir Ahmad ., (2004) *Practical Approach To the Companies Ordinance 1984*, New Fine Printing Press, Lahore, page 8.
- Sykes, J. B (1976) *The Concise Oxford Dictionary*, Oxford Printing Press, p.11.
- Sheilfer , A. and R.Vishny ,(1986) *Large Shareholders and Corporate Control*, Journal of Political Economy 94,461-448.

Websites

- http://www.secp.gov.pk/dp/pdf/manual-CG.pdf
- http://www.institutionalshareholderscommittee.org.uk
- http://www.ecgi.org/activism/index.php
- http://www.icgn.org
- http://www.calpers.ca.govt.
- http://www.hermes.co.uk
- http://www.sarbanes-oxley.com
- http://www.fsa.gov.uk.
- http://www.economist.com
- http://www.investopedia.com
- www.pakistanlawsite.com
- www.frc.org.uk
- www.secp.gov.pk/corporatelaws/pdf/CodeofCorporateGovernance.pdf
- www.csrc.gov.cn
- www.frc.org.uk

Case Laws:

- 2002 CLD 1314 at page 7
- PLD 2008 SC 697 at page 7
- AIR 1959 SC 775 at page 8
- 1985 Company Cases 831(Bombay) at page 8
- 2009 CLD212 at page 16
- 2009 C L D 883 at page 24
- NLR 1990 TD 358 at page 24
- 1990 CLC 1640 at page 24
- 2007 CLD 605 at page 25
- 2007 C L D 1116 at page 25
- 2006 CLD 378 at page 25
- PLD 1969 Lah 615 at page 26
- PLD 1973 Kar 52 at page 26
- (1988) 64 Company Cases 19. at page 27
- 1993 MLD 42. at page 27
- PLD 1973 Kar 52. at page 28
- 2007 C L D 605 at page 29
- (1986) 59 Company Cases 548. at page 29
- 2000 CLC 477 at page 30
- P L D 1995 Lahore 264 at page 31
- 2001 CLC 2019 at page 31
- 2006 C L D 1068 at page 34

- 2008 C L D 6 at page 35
- 2001 C L C 2019 at page 39
- 2007 CLD 165 at page 43
- 2006 CLD 627 at page 44
- 2008 C L D 436 at page 45
- 2008 C L D 809 at page 45
- 2006 C L D 1470 at page 46
- 2006 C L D 588 at page 49
- 2006 C L D 298 at page 50
- 2002 C L D 1164 at page 51
- 2008 CLD 305 at page 51