

Study Report

on

Corporate Governance in Bangladesh: How Best to Institutionalize it, Critical Practices and Procedures

Introduction

This study examines the state of corporate governance (CG) in Bangladesh. Since the early 1990s, CG has been receiving increasing attention from regulatory bodies and practitioners worldwide. Corporate sectors are still in its initial stage; nevertheless awareness of the importance of CG is growing. Bangladesh's small size and lack of natural resources have necessitated an open trade policy. Bangladesh also has a liberal policy towards foreign direct investment (FDI). However, when compared to those of the India, Sri Lanka, Pakistan, Thailand and Malaysia, CG in practice and philosophy have up till now remained relatively under-developed in Bangladesh. Further, there appears to be a lack of either market or structural governance mechanisms to discipline errant managers. To govern the corporate environment in Bangladesh, following legal measures are in practice:

- Securities and Exchange Ordinance 1969
- Bangladesh Bank Order 1972
- Bank Companies Act 1991
- Financial Institutions Act 1993
- Securities and Exchange Commission Act 1993
- Companies Act 1994
- Bankruptcy Act 1997

However, to institutionalize the practice of CG in Bangladesh, first initiative was undertaken by the Securities and Exchange Commission (SEC). SEC issued a notification on Corporate Governance Guidelines (CG Guidelines) for the publicly listed companies of Bangladesh under the power vested on the Commission by Section 2CC of the Securities and Exchange Ordinance, 1969. The CG Guidelines were issued on a 'comply or explain' basis, providing some 'breathing space' for the companies to implement on the basis of their capabilities. Nevertheless, the overall framework for investor protection and CG has a number of important weaknesses that have hindered the capital market development.

Most of the companies depend on the banks as their major source of financing. Capital market in Bangladesh is still at an emerging stage with market capitalization amounting to only 6.5% of GDP with low investor confidence on corporate governance and financial disclosure practices in many companies listed in the stock exchanges.¹ The neighboring countries are well ahead vis-à-vis Bangladesh in terms of depth of capital market. For example, in India, Pakistan and Sri Lanka, the market capitalization is 56%, 30% and 18% of their GDP respectively.

CG practices in Bangladesh are gradually being introduced in most companies and organizations. 66.7 percent of the companies have adopted CG and 43.3 percent have compliance policy with national or international benchmarks. A considerable percentage of the top management does not fully understand the concept of CG.² However, Bangladesh has lagged behind its neighbors and the global economy in CG.³ One reason for this slow

¹ Du, Hua. 2006. *Roundtable Discussion on Corporate Governance Guidelines of SEC and its implementation practices in Bangladesh*. Asian Development Bank. 23 September 2006.

² *Ibid*

³ Gillibrand, M. 2004. Corporate Management Essential for Industrialization. *The Bangladesh Observer*, April 17, 2004.

progress in adopting CG is that most companies are family oriented.⁴ Such concentrated ownership structures affects the effectiveness of corporate governance mechanisms, which weaknesses cannot be rectified by laws and regulations. Motivation to disclose information and improve governance practices by companies is also felt negatively. There is neither any value judgment nor any consequences for CG practices. The current system in Bangladesh does not provide sufficient legal, institutional and economic motivation for stakeholders to encourage and enforce CG practices.

Plan of the paper

Principle objective of this study is to identify and facilitate the initiatives to institutionalize CG in Bangladesh. With this objective, this study paper is structured as follows. Section I of this study gives an overview of corporate governance, as that determines the scope of the issues. It briefly describes the growth of international practices to institutionalize CG. Section II examines the current state of CG practices in Bangladesh, India, Sri Lanka, Pakistan, Thailand and Hong Kong. From the outset, it has been observed that Bangladesh lagged behind its neighbors and important trading partners with regard to CG standards and practice. A comparative analysis provides regional examples of initiatives that could be applied in Bangladesh to improve the situation. Section III briefly assesses the contemporary CG issues to provide an overview of the weaknesses and regulatory efforts at implementing and enforcing good CG structure in Bangladesh. After analyzing the Bangladesh landscape, a brief policy outline has been formulated in the section IV. Section V leads to examine the modalities of guidelines to implement good CG practices in Bangladesh based on sector-specific approach. This policy paper identifies four categories of sectors: SOEs, FIs, PSEs and NGOs.⁵ Section VI identifies the forces that act as barrier for CG. In section VII, the paper concludes by identifying some important policy recommendations and research issues that require further study. In the concluding section VIII, possible role of DCCI in institutionalizing CG practices in Bangladesh has been suggested.

Limitations of the Study

This study has certain limitations that need to be taken into account when considering the recommendations and its implications. Some of these limitations can be seen as fruitful avenues for future research under the same theme. This study has focused on a phenomenon that is a very extensive and major one, i.e. corporate governance. In this paper, assessment of this complex phenomenon has been studied from a rather narrow empirical perspective. During this study, it has been found that not much of research has been conducted on the CG landscape in Bangladesh. Indeed, there are ample of studies available on the methods and principles of CG from Bangladesh's perspectives but there is a substantial lack of sector specific empirical and real-life studies. There is an absence of credible data and relevant information on the real CG concerns in Bangladesh. Given the time limitation, comprehensive access to information was a difficult task. A systemic and periodic survey of CG practices in Bangladesh has thus become an important task for the organizations like DCCI, BEI, and SEC.⁶

⁴ Most of the companies claim that they maintain a fair recruitment procedure where only merit and efficiency prevail rather than kinship or prejudice. Although a study conducted by CPD found that only 32.3 percent of the companies have formal policies on recruitment and promotion.

⁵ Acronyms: State-owned Enterprise (SOE), Financial Institution (FI), Private Sector Enterprise (PSE), Non-Government Organization (NGO)

⁶ Acronyms: Dhaka Chamber of Commerce and Industry (DCCI), Bangladesh Enterprise Institute (BEI), Securities and Exchange Commission (SEC)

Chapter I

1. Understanding Corporate Governance

The word 'corporate governance' has become a buzzword due to the Asian financial crises in 1997-98, the activities of the corporate sector affected entire economies, and deficiencies in CG endangered the stability of the global financial system. In general, CG deals with laws, procedures, practices and implicit rules that determine company's ability to take managerial decisions *vis-à-vis* its claimants—in particular, its shareholders, creditors, customers, the State and employees. However, a somewhat broader definition would be to define CG as a set of mechanisms through which a single country or firms within a country operates when ownership is separated from management. Therefore, *corporate governance is the system by which companies are directed and controlled.*⁷

There is a global consensus about the objective of 'good' corporate governance: *maximizing long term shareholder value.*⁸ Since shareholders are residual claimants, this objective follows from a premise that, in well performing capital and financial markets, whatever maximizes shareholder value must necessarily maximize corporate prosperity, and best satisfy the claims of creditors, employees, shareholders, and the State. Since the concept of government controlling the economy is gradually eroding, it has made the market a decisive factor in settling economic issues. This has also coincided with the thrust given to globalization because of the setting up of the WTO and every member of the WTO trying to bring down the tariff barriers.

Globalization involves the movement of four economic parameters namely, physical capital in terms of plant and machinery, financial capital in terms of money invested in capital markets or in FDI, technology, and labor moving across national borders. The pace of movement of financial capital has become greater because of the pervasive impact of information technology and the world having become a global village.⁹ When investments take place in emerging markets, the investors want to be sure that not only are the capital markets or enterprises with which they are investing, run competently but they also have good corporate governance. CG represents the value framework, the ethical framework and the moral framework under which business decisions are taken. In other words, when investments take place across national borders, the investors want to be sure that not only is their capital handled effectively and adds to the creation of wealth, but the business decisions are also taken in a manner which is not illegal or involving moral hazard.¹⁰

Corporate governance therefore calls for three factors:

1. Transparency in decision-making;
2. Accountability which follows from transparency because responsibilities could be fixed easily for actions taken or not taken, and;
3. The accountability is for the safeguarding the interests of the stakeholders and the investors in the organization.

Over the last few years different country groups have been establishing their own common set of benchmarks for corporate governances, for instance, the OECD Council called upon the OECD to develop a set of CG standards and guidelines and published in May 1999 a

⁷ Cadbury Committee (Committee on the Financial Aspects of Corporate Governance). 1992. *The Report of the Committee on the Financial Aspects of Corporate Governance*. London: UK.

⁸ Confederation of Indian Industry. 1998. *Desirable Corporate Governance*. www.ciionline.org

⁹ Khan, Shahab Enam. 2006. *Bringing the State Back In ? : Critique of Neoliberal Globalization*. African Journal of International Relations and Development. Vol. 11. No. 1.

¹⁰ Vittal, N. 2004. *Issues in Corporate Governance in India*. Paper for publication in the 5th JRD Tata Memorial Lecture Series.

common set of guiding principles on corporate governance for all OECD member countries. To institutionalize CG practice, OECD has introduced following principles are:

Rights of shareholders	<ol style="list-style-type: none"> 1. Recognition of basic shareholder rights 2. Shareholders have the right to participate in decisions concerning fundamental corporate changes 3. Voting rights of shareholders 4. Disclosure of disproportionate voting rights of certain shareholders to obtain a degree of control 5. Markets for corporate control should be allowed to function 6. Shareholders should consider the costs and benefits of exercising their voting rights
Equitable treatment of shareholders	<ol style="list-style-type: none"> 1. All shareholders of the same class should be treated equally 2. Insider trading and abusive self-dealing should be prohibited 3. Board members and managers should disclose material interests
Role of stakeholders	<ol style="list-style-type: none"> 1. Assure that rights of stakeholders are protected by law 2. Stakeholders should have the opportunity to obtain effectiveness redress for violation of their rights 3. Permit performance-enhancing mechanisms for stakeholder participation 4. Stakeholders should have access to relevant information in the corporate governance process
Disclosure and transparency	<ol style="list-style-type: none"> 1. Scope of material information to be disclosed 2. Information should be prepared in accordance with high accounting standards 3. Annual audit should be conducted by an independent auditor 4. Fair, timely and cost-effective means of disseminating information
Responsibilities of the board	<ol style="list-style-type: none"> 1. Board members should act on the best interest of the company with due diligence and care 2. The board should treat all shareholders fairly 3. The board should ensure compliance with the law and take account the interest of stakeholders 4. Definition of key functions of the board 5. The board should exercise objective judgment independent from management 6. Board members should have access to accurate, relevant and timely information

Source: OECD Principles of Corporate Governance (1999).

However, members of APEC considered that the OECD guidelines have the problem of ‘one size cannot fit all’ and some may be applicable to some, but not all. APEC countries therefore called upon the Pacific Economic Cooperation Council (PECC) to develop a set of guidelines which were in line with the OECD principles. The APEC guidelines can be considered as a middle step for emerging markets to achieve a better practice of good corporate governance. This set of guidelines forms the standard for individual Governments, regulatory bodies and professional bodies to develop their agendas and with a view to setting up acceptable codes of practice.¹¹

¹¹ Cheung, Stephen, YL., and, Chan, Bob, Y. 2004. Corporate Governance in Asia. *Asia-Pacific Development Journal*. Vol. 11. No. 2. December 2004.

Chapter II

Corporate Governance in Some Asian Countries

As CG is the product of a complex set of cultural, economic, and social issues and that the governance structures of corporations differ from country to country, it is appropriate that CG guidelines and practice codes be designed and adopted by each constituent country. In the end, CG should produce an environment within each country that corporations identify with and can adhere to in their decision-making processes. In Asian countries, the interest in corporate governance has been sporadic but has stepped up in the late 1990s following the 1997-1998 crises. Subsequent to the outbreak of the Asian currency crisis in 1997, the flow of capital from foreign investors suddenly dried up, leading to intense liquidity problems in local capital markets and a real impact on the economy due to insufficient capital and investor apprehensions.¹²

A report produced by Bangladesh Enterprise Institute (2004) has showed that, in India there was the securities scam (involving a large number of banks) leading to the stock market crash in 1992, followed by the consolidation of equity ownership by multinational companies listed on the stock markets, and then by the stock market bubble in 1993 and crash of the 'disappearing companies' in 1994, which devastated the primary market until the end of the century. These led to the formation by the Confederation of Indian Industry of the Bajaj Committee on corporate governance in late 1995, well before the East Asian financial crisis.¹³

In Sri Lanka, the concern for CG originated in the numerous company failures, especially finance companies, in the late 1980's and early 1990's, which caused investors to lose faith in the regulatory and semi-regulatory frameworks, as well as the standards of financial reporting. Accordingly, the Institute of Chartered Accountants of Sri Lanka set up a task force in 1992 (about the same time as the Cadbury committee in UK) to enforce Sri Lankan accounting standards, and then extended this initiative in 1996 (again before the East Asian financial crisis) to set up a committee to make recommendations on the financial aspects of corporate governance.¹⁴

Pakistan commenced its CG programmes later, following the Securities and Exchange Commission of Pakistan Act in 1997, the commencement of operations by the Commission in 1999, and the introduction of the national Code for Corporate Governance in early 2002. But despite the later start, it is evident that the initiatives in Pakistan were driven by home-grown realities, in particular the recognition that the traditional structures and operations of the capital market, especially lending from state-owned banks, could no longer sustain the financing needed for growth, hence there is a critical need for reform of the capital markets in order to mobilize domestic savings and foreign portfolio investment. In fact, despite the later start with formal national policies, it could be said that Pakistan focused on corporate governance earlier than many countries in the world, not just the region – the Pakistan country report emphasizes the importance of the 1984 Companies Ordinance Act, which introduced a number of key features of good corporate governance, at a time when the very term 'corporate governance' had only just been coined and was still effectively unknown outside very specialized academic circles.¹⁵

¹² *Ibid.*

¹³ Sobhan, Farooq, and Werner, Wendy. 2004. *A Comparative Analysis of Corporate Governance in South Asia: Charting a Roadmap for Bangladesh*. Bangladesh Enterprise Institute.

¹⁴ *Ibid.*

¹⁵ *Ibid.*

In Hong Kong, since 1993 the Stock Exchange of Hong Kong (SEHK) has incorporated the Code of Best Practices as an appendix to the Exchange Listing Rules with an intention to increase the accountability of the directors to shareholders and to improve shareholders' access to information. However, the Code is a set of voluntary guidelines for boards of directors. Thus, all publicly listed companies in the SEHK are only required to explain in their interim and annual reports whether or not they comply with the Code and give reasons for non-compliance. In 1994, the SEHK Listing Rules required listed companies to appoint at least two independent non-executive directors on the board in an attempt to improve corporate governance. Besides, in December 1995 and in January 1997, the Hong Kong Society of Accountants in its reports of the working group on corporate governance made a recommend that as a self-regulatory good practice, that listed companies should try not to have members of the same family making up more than half of the members of the boards. It believes that this measure will help to increase the effectiveness of the independent directors and tackle the domination of the board in the Hong Kong companies more effectively. Further, in 1999, the SEHK has established GEM (Growth Enterprise Market or Hong Kong's second board) to encourage listings by smaller companies with short track records.¹⁶ The GEM Listing Rules are less strict than the main board. For example, companies do not need to show three years of clear profit. However, like listed companies in the main board, the companies in GEM must have at least two independent directors.¹⁷

In Thailand, the Stock Exchange of Thailand (SET) first published 'Code of Best Practice for Directors of Listed Companies' in December 1997. However, most of the listed companies in Thailand are controlled by majority shareholders. The majority shareholders can appoint board members without approval of other minority shareholders through the majority vote. Therefore, the board of directors is often neither independent from management nor accountable to small shareholders. To tackle this problem, the SET requires that there must be at least two independent non-executive directors on the board in order to monitor the management of the company. An audit committee in Thailand is compulsory. In January 1998, the SET notified listed companies that they would have to form audit committees no later than December 1999, while newly listed companies would require them from the start. Such audit committees should comprise at least three directors, all of whom should be independent and at least one must have expertise in accounting or finance. The concept of shareholder's protection is first appeared in Thailand in 1993 when the Public Limited Companies Act B.E.2535 was introduced. The law offers a relative comprehensive protection of basic shareholders' right.¹⁸

¹⁶ Hong Kong Society of Accountants. *Report of the Working Group on Corporate Governance*. December 1995.

¹⁷ Wong, Daniel W.K., and Peggy S.L. Yeung. 2000. Corporate Governance in Hong Kong. *The Business Environment in Hong Kong*.

¹⁸ Cheung, Stephen, YL., and, Chan, Bob, Y. 2004. Corporate Governance in Asia. *Asia-Pacific Development Journal*. Vol. 11. No. 2. December 2004.

Chapter-III

Issues in Corporate Governance in Bangladesh

Most of the companies in Bangladesh depend on the banks as their major source of financing. Capital market in Bangladesh is still at an emerging stage with market capitalization amounting to only 6.5% of GDP with low investor confidence on corporate governance and financial disclosure practices in many companies listed in the stock exchanges.¹⁹ The neighboring countries are well ahead vis-à-vis Bangladesh in terms of depth of capital market. For example, in India, Pakistan and Sri Lanka, the market capitalization is 56%, 30% and 18% of their GDP respectively. Nevertheless, the past few years have witnessed a silent inclination towards CG due to a variety of forces that are acting today and would become stronger in years to come:

- *Deregulation:* Economic reforms have not only increased growth prospects, but they have also made markets more competitive. This means that in order to survive companies will need to invest continuously on a large scale.
- *Disintermediation:* Meanwhile, financial sector reforms have made it imperative for firms to rely on capital markets to a greater degree for their needs of additional capital.
- *Institutionalization:* Simultaneously, the increasing institutionalization of the capital markets has enhanced the disciplining power of the market.
- *Globalization:* Globalization of Bangladesh's markets has exposed issuers, investors and intermediaries to the higher standards of disclosure and CG that prevail in more developed capital markets.

While these factors will make the markets more effective in disciplining the dominant shareholder, there are many things that the government and the regulators are yet to do to enhance this ability. Ahmed and Yusuf (2005) argue that there has been failure in most of the elements of CG.²⁰ Some of these individual elements can be portrayed with a view to seeing their weaknesses in implementing CG:

Corporate ownership structures: All corporate governance systems revolve around four core principles: Fairness, accountability, responsibility and transparency. The specific challenges of upholding these principles depend on the ownership structure of the corporate sector. However, in Bangladesh, general practice is that the corporate structure is dominated by family members. Such practice hinders the level of fairness, accountability and transparency.²¹

¹⁹ Du, Hua. 2006. *Roundtable Discussion on Corporate Governance Guidelines of SEC and its implementation practices in Bangladesh*. Asian Development Bank. 23 September 2006.

²⁰ Ahmed, Mamtaz Uddin, and, Yusuf, Muhammad Abu. 2005. Corporate Governance: Bangladesh Perspective. *The Cost and Management*. Vol. 33. No. 6. November-December 2005. pp. 18-26.

²¹ It is revealed that in Bangladesh 72.5% of the outstanding shares are owned by households/ sponsors and individuals. Insignificant concentration is observed by bank and financial institutions i.e., 3.1 % and foreigners held 16% and Government / financial institutions held only 16% of the outstanding shares in 2000. It is also reported that even when the company is listed on the stock exchange, few shares are available for trading, as majority remain held by the original sponsors. The original sponsors often buy additional shares from the market to raise their holdings to as high as 70 percent or 80 percent though shares are floated in the primary market on 50:50 basis. Chowdhury, AA Mahboob Uddin. 2006. Role of corporate governance for the development of Bangladesh capital market. Editorial Page. The New Nation. 17 May 2006. http://nation.ittefaq.com/artman/publish/article_27929.shtml

Inadequate Bankruptcy Laws: Bankruptcy laws and processes are inadequate in terms of provisions and not strong in terms of enforcement in Bangladesh. No country can have good CG standards with poor bankruptcy laws and processes. Besides, inefficient foreclosures and securitization processes have compounded the problems in Bangladesh.²²

Lack of initiatives to drive for CG from the International Investor Community: Most companies in Bangladesh have a pessimist approach in attracting foreign investment. As a result, there is a lack of drive from the international investor community for better corporate governance. Level of penetration of Bangladeshi companies in the foreign stock exchanges is also very low. Lately though, BEXIMCO Pharmaceutical Company has been given with the clearance by SEC for listing with the London Stock Exchange.

Accounting standards, audit and disclosure: The scenario of internal audit; accounting standards and disclosure and its impacts on CG and management practices in Bangladesh are mixed. There are now elements of both positive scopes and new challenges and risk for the corporations in these areas. Following the tradition of English law, Bangladesh accounting standards are not based on codified law, but rely on Generally Accepted Accounting Principles (GAAP) developed by accounting profession. These principles are primarily shareholder oriented and are independent of tax considerations. In Bangladesh the companies have to make disclosure of information required by law. Disclosure requirements for Initial Public Offerings are defined by the Companies Act and the orders under the Securities and Exchange Ordinance, 1969. Periodic disclosure requirements are mentioned in the Securities and Exchange Rules, 1987.²³

*Inconsistency between Companies Act, BAS and SEC Requirements:*²⁴ The companies Act, 1994 provides, among others, provisions regarding preparation and publication of financial statements, disclosures and auditing. However, in many cases, the Act lacks clarity with regard to statutory requirements on disclosures in the financial statements of listed companies. Moreover some accounting requirements mentioned in the Act are incompatible with International Accounting Standards (IAS) which is required by the SEC. For example, contrary to IAS, the Companies Act requires capitalization of gains and losses arising from changes in foreign exchange rates under all circumstances. Another inconsistency is that the Companies Act does not require a consolidated balance sheet for a holding company but it is required under the IAS. Inconsistencies between IAS and the Companies Act need to be eliminated.²⁵

Limited or No Disclosure regarding Related Party Transactions: Related party transactions are not disclosed properly in the financial statements. It is an impediment towards achieving good CG in Bangladesh.²⁶

Weak Regulatory System: Bangladesh still follows the hybrid system of legal system inherited from the British administration. Currently, the Companies Act of 1994 is the law that governs the incorporated domestic corporations and institutions. The other significant laws which has important role in governing the corporate sectors are: Securities and Exchange Ordinance 1969, Bangladesh Bank Order 1972, Bank Companies Act 1991, Financial Institutions Act 1993, Securities and Exchange Commission Act 1993 and the

²² Hossain, M. 2005. Why shareholders' activism is still an illusion in Bangladesh. *The Financial Express*, Dhaka (1-8-2005).

²³ Chowdhury, AA Mahboob Uddin. 2006. Role of corporate governance for the development of Bangladesh capital market. Editorial Page. *The New Nation*. 17 May 2006. http://nation.ittefaq.com/artman/publish/article_27929.shtml

²⁴ Ahmed, Mamtaz Uddin, and Yusuf, Muhammad Abu. 2005. Corporate Governance: Bangladesh Perspective. *The Cost and Management*. Vol. 33. No. 6. November-December 2005. pp. 18-26.

²⁵ World Bank. 2003. *Report on the observance of standards and codes (ROSC) Bangladesh Accounting and Auditing*. The World Bank Report. www.worldbank.org/ifa/rosc_aa_bgd.pdf

²⁶ *Ibid.*

Bankruptcy Act, 1997. Therefore, weak regulatory system along with board interference with the management retards the improvement of CG in the country.²⁷

Capital Market Role: Capital market facilitates good governance through information production and monitoring.²⁸ The capital market of Bangladesh consists of two stock exchanges: Dhaka Stock Exchange (DSE) and Chittagong Stock Exchange (CSE). Bangladesh does not have depth in its equity market. The capital market of Bangladesh is still a weak link in the movement towards strengthening CG. The overall performance measures of its stock market show low trading volume, intermittent bumps, not many new offerings and unsteady valuations more on the declining side than otherwise.²⁹ The stock market scandals in 1996 have seriously eroded investor confidence in the stock market.³⁰ One vital aspect is that capital market in Bangladesh does not react significantly to corporate performance in terms of higher stock valuation for accurate disclosure and poor stock price for failure of accurate and full disclosure. There is little incentive in becoming a public company and listing on the stock exchange in Bangladesh. Companies with good reputations can get bank financing relatively easily than through share issue. Moreover, there are no bonds, fixed income or debt instruments in the capital market. This means there are no pressure groups³¹ for enforcing CG principles.³² Unlike the private mutual funds, the state-owned investment company – Investment Corporation of Bangladesh (ICB) – has not, until recently, been required to publish the net asset value of its mutual funds or submit performance reports to the SEC.³³

General Meeting Scenario: General meetings of a company, in particular the Annual General Meeting (AGM) are the primary platform where shareholders can raise their concerns and make their influence felt over the management towards attaining good governance. Although a good number of provisions in the Act provided sufficient leverage to allow shareholders a voice in companies, most companies in Bangladesh, are closely held. Small groups of shareholders own or control the majority of shares, and by using that majority, control the decision making processes of the companies.³⁴ In number of studies it has been found that there is a negative correlation exists between good CG and defaulting in holding annual general meetings in due time.

Board Committees: Board committees (audit, remuneration and nomination) are of critical importance in CG. Audit Committee is now being treated as a principal player in ensuring good CG and rebuilding public confidence in financial reporting. The role of Audit Committee, among others are: monitoring integrity of financial statements, reviewing internal financial controls, recommending appointment of external auditor and reviewing auditor independence and objectivity and audit effectiveness.³⁵ The Remuneration Committee's responsibilities include establishment and review of the Managing Director's remuneration package and senior management salary packages. Remuneration Committee assists the Board to attract, retain and motivate high caliber executives and director through proposing

²⁷ Chowdhury, AA Mahboob Uddin. 2006. Role of corporate governance for the development of Bangladesh capital market. Editorial Page. The New Nation. 17 May 2006. http://nation.ittefaq.com/artman/publish/article_27929.shtml

²⁸ Tadesse, S. 2004. The Allocation and Monitoring Role of Capital Markets: Theory and International Evidence. *Journal of Financial and Quantitative Analysis*. December. Vol. 39. No. 4.

²⁹ Hossain, M. 2005. Why shareholders' activism is still an illusion in Bangladesh. *The Financial Express*. Dhaka. 01 August 2005.

³⁰ Bangladesh Enterprise Institute. 2003. *A Comparative Analysis of Corporate Governance in South Asia: Charting a Roadmap for Bangladesh*. Dhaka: BEL.

³¹ If there are debt markets, investors in bonds and other debt instruments may emerge as an important pressure group for encouraging good corporate governance.

³² Bangladesh Enterprise Institute. 2003. *A Comparative Analysis of Corporate Governance in South Asia: Charting a Roadmap for Bangladesh*. Dhaka: BEL.

³³ Ahmed, Mamtaz Uddin, and, Yusuf, Muhammad Abu. 2005. Corporate Governance: Bangladesh Perspective. *The Cost and Management*. Vol. 33. No. 6. November-December 2005. pp. 18-26.

³⁴ *Ibid*.

³⁵ Lambe, A. 2005. Audit Committees step into the limelight. *Accountancy Ireland*. February. Vol. 37 No. 1. Pp. 48-51.

remuneration that commensurate to their performance. Despite significant importance of the board committees (as described), few boards (except for banks) has Audit Committees and almost none have nomination or Remuneration Committees in Bangladesh.³⁶

The Boards of Directors: The Companies Act, 1994 provides for many stringent rules in respect of any negligence, default, breach of duty or trust on the part of director, manager or officer of a company. However, experience suggests that these are more honored in the breach than observance. In an overwhelming majority of the non-bank listed companies, the board is heavily dominated by sponsor shareholders who generally belong to a single family. The boards are actively involved in management. Most independent directors represent current or former government officials or bureaucrats. They are appointed directors to assist company in getting licenses or as payback for previous favors. In the context of Bangladesh, independent directors do not act as an advocate for minority shareholders or as a source of innovative ideas.³⁷

Lack of Shareholder Activism: Shareholder rights are today recognized in countries across the globe as relevant to efforts for improving and strengthening CG. The average non-controlling or minority shareholders do not possess significant level of education, understanding and sophistication required to exert pressure on a company to change behavior. The number of shareholders with sufficient knowledge and skills to understand company operations and to hold management and the board of directors accountable is very low. Moreover, general shareholders do not pay attention on issues of performance, business strategy, future business plans, disclosures and processes that could give them a greater voice in the policy decisions of a company. In fact, there is very little awareness about shareholders' rights and responsibilities. Shareholders' activism is still an illusion in Bangladesh.³⁸

No Market for Corporate Control: A market for corporate control plays an important monitoring function in CG, as poorly managed companies will become takeover targets.³⁹ In Bangladesh, there seems to have no market for corporate control.

Weak Pressure Groups: Shareholders, investor associations, institutional investors and the financial press can play significant role in ensuring better CG. Each of these potential pressure groups is weak in Bangladesh. The numbers of journalists who possess knowledge on financial reporting are limited and there are lacks of investigative reports. Similarly public shareholders are not organized under a common platform (such as shareholder associations) to demand better corporate governance. Unlike institutional investors in most capital markets across the globe, the few State-owned Enterprises (SOEs) lack performance spirit and motivation to force companies to improve CG as well as performance.⁴⁰

Lack of Auditor Independence: Auditors in Bangladesh are not considered independent or sufficiently qualified to attest to the validity of the financial statements of corporate entities.⁴¹ A study shows that 64.4 percent of the companies conduct regular audit for effective implementation of the core labor policies. Of the companies which audit the implementation of core labor policies, 91.1 percent meet their labor policy objectives. Only 2.2 percent of the

³⁶ Bangladesh Enterprise Institute. 2003. *A Comparative Analysis of Corporate Governance in South Asia: Charting a Roadmap for Bangladesh*. Dhaka: BEI.

³⁷ *Ibid.*

³⁸ Hossain, M. 2005. Why shareholders' activism is still an illusion in Bangladesh. *The Financial Express*, Dhaka. 01 August 2005.

³⁹ Morrison, J. 2004. Legislating for Good Corporate Governance: Do We Expect Too Much? *The Journal of Corporate Citizenship*. Autumn. Issue 15. Pp. 121-133.

⁴⁰ Ahmed, Mamtaz Uddin, Yusuf, Muhammad Abu. 2005. Corporate Governance: Bangladesh Perspective. *The Cost and Management*. Vol. 33. No. 6. November-December 2005. pp. 18-26.

⁴¹ Bangladesh Enterprise Institute. 2003. *A Comparative Analysis of Corporate Governance in South Asia: Charting a Roadmap for Bangladesh*. Dhaka: BEI.

companies confessed that they make unfair dismissals and 4.4 percent of the companies confessed that they violated labor laws in last 5 years. Around 67 percent of companies have a formal policy to ensure clean, healthy and safe working conditions. Procedures to implement policy and specific assignment to senior management for implementation are found only in 26.7 percent of the companies.⁴²

Poor Audit Report: Audited financial reports are rarely reliable and free from the control of the owners. Despite irregularities (in respect of non compliance with the applicable IASs) in the audit report, the auditors issue unqualified audit report on the financial statements.⁴³

⁴² Raihan, Ananya. 2003. *Corporate Responsibility in Bangladesh: Where Do We Stand?* Report No. 54. Centre for Policy Dialogue: Dhaka. www.cpd-bangladesh.org

⁴³ World Bank. 2003. *Report on the observance of standards and codes (ROSC) Bangladesh Accounting and Auditing*. The World Bank Report. www.worldbank.org/ifa/rosc_aa_bgd.pdf

Chapter-IV

A Need for Corporate Governance is Urgent

Above scenarios suggest that for effective CG in Bangladesh; it requires a clear understanding of the respective roles of the board and of senior management and their relationships with others in the corporate structure. Removing these weaknesses requires appropriate reform and implementation thereof are highly necessary in Bangladesh.⁴⁴ Following policy is intended to clarify these relationships and responsibilities and to promote effective CG:

- Disclosure of information should be the pre-requisite for the shareholders or for the capital market to act against errant managements. The regulator can enhance the scope, frequency, quality and reliability of the information that is disclosed.
- Regulatory measures that promote an efficient market for corporate control would create an effective threat to some classes of dominant shareholders as discussed earlier.
- Reforms in bankruptcy and related laws would bring the disciplining power of the debtholders to bear upon recalcitrant managements.
- Large blocks of shares in corporate Bangladesh are held by public sector financial institutions who have proved to be passive spectators. These shareholdings could be transferred to other investors who could exercise more effective discipline on the company managements. Alternatively, these institutions could be restructured and privatized to make them more vigilant guardians of the wealth that they control.

⁴⁴ Ahmed, Mamtaz Uddin, Yusuf, Muhammad Abu. 2005. Corporate Governance: Bangladesh Perspective. *The Cost and Management*. Vol. 33. No. 6. November-December 2005. pp. 18-26.

Chapter V

Corporate Governance Practice for Sector-specific Firms:

Above scenario stresses the need for a comprehensive framework for implementation of CG in Bangladesh. Following are the suggested practice for sector-specific firms:

State-owned Enterprises (SOEs):

In spite of privatization over the last three decades, state-owned enterprises (SOEs) are still a mainstay in Bangladesh economy. Like Bangladesh, China, India, Russia and South Africa are just a few countries where wholly or partly government-owned SOEs remain productive and influential. Good CG is crucial for SOEs in Bangladesh, because they face even more governance challenges than private companies do. Unlike a widely-held private company, an SOE usually cannot have its board or management changed via a takeover or proxy contest, and they usually cannot go bankrupt. In addition, they may have “free” equity and a very low cost of subsidized loans.⁴⁵ Thus, the incentives for board members and managers to maximize the value of the company and keep costs in check are reduced. Accountability and performance may also be hindered by political interference, poorly defined non-commercial objectives, and an absence of transparency. Strong internal controls, good disclosure, independent boards of directors, and other CG tools can help state-owned enterprises perform well and act in the best interests of citizens and other shareholders. To help make state-owned enterprises more competitive, efficient and transparent, OECD has introduced following guidelines⁴⁶:

Ensure a level-playing field for state-owned enterprises competing with the private sector by

- Clearly separating the state’s ownership role from its regulatory role
- Allowing more flexibility in capital structures while making sure that state-owned enterprises face competitive access to finance

Become more informed and active shareholders by

- Simplifying the chain of accountability through centralizing or more effectively coordinating shareholding responsibilities within the state administration
- Reducing political interference in day-to-day management
- Introducing a transparent nomination process for boards, based on competence and skills

Empower boards by

- Clarifying their mandates and respecting their independence
- Separating the role of Chairman and CEO and giving boards the power to appoint CEOs
- Systematically monitoring the board’s performance

Improve transparency by

- Strengthening internal controls
- Carrying out independent, external audits based on international standards
- Disclosing any financial assistance from the state
- Producing aggregate performance reports

⁴⁵ World Bank. 2006. *Held by the Visible Hand: The Challenge of SOE Corporate Governance for Emerging Markets*. World Bank: Washington.

<http://ru.worldbank.org/Documents/Other/CorpGovSOEs.pdf>

⁴⁶ OECD. 2004. *OECD Guidelines on Corporate Governance of the State-owned Enterprises*. OECD: Paris.

Corporate Governance in the Private Sector Enterprises (PSEs):

The basic principles of good CG for the PSs are identified as involving⁴⁷:

- Appropriate disclosure
- The development of codes of conduct for company directors, and the
- Development of internal structures which provide for independent review of processes and decision making within a company.

Ensuring the basis for an effective corporate governance framework: The CG framework should promote transparent and efficient markets, be consistent with the rule of law and clearly articulate the division of responsibilities among different supervisory, regulatory and enforcement authorities.

The rights of shareholders and key ownership functions: The CG framework should protect and facilitate the exercise of shareholders' rights.

The equitable treatment of shareholders: The CG framework should ensure the equitable treatment of all shareholders, including minority and foreign shareholders. All shareholders should have the opportunity to obtain effective redress for violation of their rights.

The role of stakeholders in corporate governance: The CG framework should ensure behavior and the rights of stakeholders established by law or through mutual agreements and encourage active co-operation between corporations and stakeholders in creating wealth, jobs, and the sustainability of financially sound enterprises.

Disclosure and transparency: The CG framework should ensure that timely and accurate disclosure is made on all material matters regarding the corporation, including the financial situation, performance, ownership, and governance of the company.

The responsibilities of the board: The CG framework should ensure the strategic guidance of the company, the effective monitoring of management by the board, and the board's accountability to the company and the shareholders.

Corporate Governance in the Financial Institutions (FIs):

The need for a competent financial sector is important to stimulate and support economic growth through efficient resource allocation. Good CG practices are essential to the effectiveness, competitiveness and safety and soundness of financial institutions.

*Streamlining the Guidelines with the Code of Corporate Governance*⁴⁸: A Code of CG has been published by BEI can be streamlined to reduce duplication and resources to comply with CG requirements for the FIs.

Protection of depositors: Given the special nature of banking institutions, a broad view of CG where regulation of banking activities is required to protect depositors. In developed economies, protection of depositors in a deregulated environment is typically provided by a system of prudential regulation, but in developing economies such protection is undermined

⁴⁷ *Ibid.*

⁴⁸ Bangladesh Enterprise Institute. 2004. *Code of Corporate Governance for Bangladesh*. Dhaka: BEI. www.bei-bd.org

by the lack of well-trained supervisors, inadequate disclosure requirements, the cost of raising bank capital and the presence of distributional cartels.⁴⁹

Improvements in prudential regulation: Liberalization policies need to be gradual, and should be dependent upon improvements in prudential regulation. Bangladesh needs to expend resources enhancing the quality of their financial reporting systems, as well as the quantity and quality of bank supervisors.⁵⁰ Given that bank capital plays such an important role in prudential regulatory systems, it is necessary to improve investor protection laws, increase financial disclosure and impose fiduciary duties upon bank directors so that banks can raise the equity capital required for regulatory purposes. A further reason as to why this policy needs implemented is the growing recognition that the CG of banks has an important role to play in assisting supervisory institutions to perform their tasks, allowing supervisors to have a working relationship with bank management, rather than adversarial one.⁵¹

*Political determinants of Corporate Governance*⁵²: CG of financial institutions, particularly banking sector, in Bangladesh is severely affected by political considerations. Given the trend towards privatization of government-owned banks in Bangladesh, there is a need for the managers of such banks to be granted autonomy and be gradually introduced to the CG practices of the private sector prior to divestment.

Role of the shareholders: Where there has only been partial divestment and governments have not relinquished any control to other shareholders, it may prove very difficult to divest further ownership stakes unless CG is strengthened.⁵³

Governance in the NGOs⁵⁴:

The orientations of NGOs are defined, updated and widely communicated: Like other non-profit organizations, NGOs cannot escape from the need and requirement to explain and make known their major orientations and the strategic framework of their action regularly. This ‘*communicational activity*’ is found in all the principles. It implies the defining and appropriateness of what is going to be communicated. Good governance verifies that this is true at each level of the NGO’s aims and projects.

Relationship with the stakeholders: Good governance devotes itself to federating the internal stakeholders and to managing the interfaces with the external stakeholders. This is how it builds its legitimacy, its image and its representativeness. Good governance also strengthens the support that its stakeholders give it.

- The **internal stakeholders** are: the members, trustees, volunteer help, expatriate staff, employees, local non-profit organization partners and national staff (in the country of intervention).
- The **external stakeholders** are: the beneficiaries, financial backers, private donors (including sponsors), public sector of the country of the NGO, public sector of the country of intervention, public opinion in the country of the NGO, public opinion in the country of intervention, suppliers, partners in the field, other non-profit organizations and NGOs, and non-profit organization collectives, etc.

⁴⁹ Arun, TG. 2003. *Corporate Governance of Banks in the Developing Economies: Concepts and Issues*. Development Economics and Public Policy Working Paper No. 02. IDPM: Manchester.

⁵⁰ *Ibid.*

⁵¹ *Ibid.*

⁵² Roe, Mark, J. 2003. Political Determinants of Corporate Governance: Political Context, Corporate Impact. *John M. Olin Center for Law, Economics and Law*. Working Paper No. 451. Harvard: Massachusetts.

⁵³ *Ibid.*

⁵⁴ For closer exposition see Khan, Safi Rahman. 2006. *NGO Governance Principles*. Bangladesh Enterprise Institute. www.bei-bd.org

Information is sincere, reliable and available: Each person receives all the information appropriate for his or her position, in an appropriate form. The quality of the information is checked, and its circulation is adapted to the use that must be made of it.

The NGO's financial management is impartial. The notion of the NGO's impartial management must be subject to internal discussion, because it can be interpreted in different ways. *Synergie Qualité* defines it as follows: 'The people who manage and administer the NGO, by themselves or by people who intervene for them, have no direct or indirect advantage from the financial results of the operations'.⁵⁵ The balance between administrative and organizational costs and the resources allocated to the operational projects is to be examined regularly, out of concern for efficiency. Good governance, for example, has a cost, but it contributes to improving the interventions to the beneficiary's advantage. The building up of reserves, investments, loans, guarantees and deposits is governed by the required rules of exactness and carefulness.

The representative bodies: The representative bodies of the internal stakeholders can be consulted before a significant expenditure is made (purchase of buildings, for example). The members of a Board of Trustees of an NGO must be volunteers.

⁵⁵ Guide Synergie Qualité. 2004. *Proposal for Quality Humanitarian Actions*. <http://216.239.59.104/search?q=cache:kKr9whHirIJ:www.politika.lv/index.php%3F%3D431+NGO+governance+principle&hl=bn&ct=clnk&cd=3&gl=bd&client=firefox-a>

Chapter-VI

Forces Against and For Corporate Governance

Resistance comes from vested interests (oligopolists, relationship-based investors) who wants to retain status quo.⁵⁶ In Bangladesh there is a tendency to make large investments in highly-capital intensive enterprises with an eye to price incentives through relationship. This leads to wastage of scarce capital resources. Many firms now need foreign capital to finance expenses that again can lead to demand for better CG. Political turmoil and vested interests are the key factors to hinder the process of good CG framework in Bangladesh. Thus, policy makers have to focus not only on regular / accurate financial accounts & transparency, but they have to address issues like whether a large business group should also be allowed to own a bank. In brief, following are the issues that hinder the enforcement of CG in Bangladesh:⁵⁷

The Boards of Directors:

- Inadequate examples of role in formulating vision and strategy
- Lack of independent representation
- Lack of power held by CEO
- Absence of accountability structure of management to the board/shareholders
- When the Board Chairman is also a Cabinet Minister there may be a tendency to treat the SOE as a Government department

Commercial focus:

- Procedures are set and not easy to deviate from
- Price controls are not market driven
- Sometimes face unfair competition from the private sector

Accountability and Monitoring

- Access to accurate information is difficult
- Ample of evidence of management collusion with trade unions
- Control Audits of Internal Audit, Government Commercial Audit, and External Audit
- Commercial Audits results are doubtful and not transparent

Employee incentives

- No genuine incentive for better performance
- Quality people not attracted to SOEs
- Pressure from trade unions

⁵⁶ Afzal, Mueen. 2007. *Role and Responsibilities of Independent Directors* Key note paper. Roundtable discussion on the Role and Responsibilities of Independent Directors. Bangladesh Enterprise Institute. March 18 2007.

⁵⁷ Rahman, Lopa. 2006. *Corporate Governance for SOEs: The Bangladesh Context*. Bangladesh Enterprise Institute: Dhaka.

Chapter-VII

Implementation of Corporate Governance in Bangladesh

In an earlier section, this study has reviewed the problems and existing CG practices in Bangladesh. Findings are presented as a matrix in the following box which also highlights the scopes for policy intervention in this regard:

Matrix: an overview of Corporate Governance Mechanisms in Bangladesh⁵⁸

Corporate Governance Mechanism	Importance in Bangladesh	Scope for policy intervention
Large block-holders	Likely to be an important governance mechanism in Bangladesh	Strengthen rules protecting minority shareholders
Market for Corporate Control	Market does not exist in Bangladesh. Unlikely to be important in a concentrated ownership structure. Can still take place through debt contracts, but requires adequate bankruptcy laws	Strengthen the bankruptcy laws
Proxy votes	Unlikely to be important in a concentrated ownership structure	AGMs needs to be effective and SEC may oversee the outcomes of AGMs
Board activity	Non-transparent recruiting system of the board members are widely practiced, and lack of separation of ownership and management	Implement Code of CG and introduce guidelines for Best Practices, training of directors, transparent recruitment of the Board members
Executive compensation	Less important when owner can hire and fire and has private benefits	SEC or Bangladesh Bank can introduce codes for Executive compensation, transparent compensation policy
Bank monitoring and regulatory environment	Critically important for Bangladesh	Strengthen banking regulation and institutions; encourage accumulation of information on credit histories, develop supporting credit bureaus and other information intermediaries
Employee monitoring	Potentially very important for SMEs with highly skilled human capital threat of leaving is very high	Proper incentive practice on human capital should be institutionalized
Litigation	Depends on quality of general enforcement environment, however it sometimes work in Bangladesh	Facilitate communications among the shareholders
Media and social control	Potentially important in Bangladesh as competition and independence of media is rising	Encourage competition and diversification of media, active public campaigns can empower public
Reputation	Important at general enforcement is	Encourage competition in factor

⁵⁸ Author's compilation

and self-enforcement	relatively weak	markets by enabling competition policy
Arbitration and auditors	Potentially important, often the origin of public law, but the enforcement is a problem in Bangladesh, audits are often abused	Facilitate laws for the third party mechanisms, Auditing processes needs to be strengthened
Competition	Determines scope for potential mistreatment of factors of production including financing	Proper competition policy can be introduced

To implement reforms in CG, based on the above matrix, with a view to have good corporate governance in Bangladesh, the following proposals/recommendations can be put forward:

Short-term

Code of Corporate Governance and Best Practice Recommendations:

The current status is that many Asian countries have adopted governance guidelines and codes of best practice. Like these countries, Bangladesh needs to have a “Code of Corporate Governance and Best Practice Recommendations” which can be either rule based or principles based. Bangladesh Enterprise Institute (BEI), Corporate Governance Committee of ICAB, and SEC have developed separate Codes for Corporate Governance for Bangladesh. The Government must take initiatives to make these implemented by making necessary changes in the Companies Act.

Implement Competition Policy:

An effective competition policy fosters a flexible, dynamic, and competitive private sector that leads to sustained and widely shared economic development. Bangladesh needs to formulate a Competition Policy which will ensure a culture of good corporate governance to thrive. Competition policy helps bring about efficiency, reduce price distortions, lower the risk of poor investment decisions, promote greater accountability and transparency in business decisions, and lead to better corporate governance.⁵⁹

Medium-term

The legal and regulatory framework should ensure that non-controlling shareholders or minority shareholders are protected from exploitation by insiders and controlling or sponsor shareholders:

Government should introduce measures, or enhance existing measures, to provide non-controlling shareholders with adequate protection from exploitation by controlling shareholders.

These measures may include, among other things: (i) strengthening disclosure requirements (particularly of self-dealing/related-party transactions and insider trading);⁶⁰ (ii) ensuring that regulators have the capacity to monitor companies for compliance with these requirements and to impose substantial sanctions for wrongdoing; (iii) clarifying and strengthening the fiduciary duty of directors to act in the interest of the company and all of its shareholders; (iv) prohibiting indemnification of directors by companies for breaches of fiduciary duty; and (v) providing shareholders who suffer financial losses with private and collective rights of action against controlling shareholders and directors.

⁵⁹ Organizations like Bangladesh Enterprise Institute have already undertaken comprehensive project on Competition Policy.

⁶⁰ Disclosure should be in line with IASs/IFRSs.

Improve the capacity of the Boards of directors:

The directors must improve their participation in strategic planning, monitoring of internal control systems and independent review of transactions involving managers, controlling shareholders and other insiders. There is a need for director training, voluntary codes of conduct, expectations for professional behavior and directors' resources and authority *vis-à-vis* management. Also it is required to reduce or eliminate loopholes by tightening standards for director "independence", by making "shadow" directors liable for their actions, by increasing sanctions for violations of duties of loyalty and care and by advocating delineation of a core set of related-party transactions (such as company loans to directors and officers) that should be prohibited outright. It is important to facilitate mechanisms to adequately empower the shareholders to seek redress for violations of their rights and to ensure director accountability. The most vital thing that can ensure good CG is high standards of ethical and personal behavior. This can only be ensured if the value system of society imposes this on their people as the norm in every aspect of life. Good CG must become an unshakable social and moral imperative.⁶¹

Long-term

Strengthen the Capacity of the Government to Monitor and Enforce the Implementation of Corporate Governance:

The Securities and Exchange Commission (SEC) of Bangladesh need to be strengthened so that it can devise and enforce a code for good CG. The Companies Act has to be amended and updated to have consistency with Bangladesh Accounting Standards (BAS), SEC requirements and the Bank Companies Act. Independent Audit Committee should be made compulsory for all listed companies. Strict implementation of accounting and auditing standards are very important. As the lead regulatory body overseeing corporate accounting and reporting, the SEC has a critical role to ensure that public company boards are properly structured and organized and have the resources to accomplish the objectives of adding value to shareholders, minimize risk of key shareholders and hold management responsible for corporate results. Ruthless monitoring of compliance and severe punishment of transgressors can ensure good CG. But Bangladesh has to wait a lot to ensure enforcement of any corrective measures properly. If the policymakers implement the recommendations suggested above, undoubtedly a good CG environment will prevail in Bangladesh.⁶²

Strengthen the Capacity of Public-Private partnership:

Public- and private-sector institutions should continue to raise awareness among companies, directors, shareholders and other interested parties of the value of good CG. Bangladesh has made little progress in raising awareness of the value of good CG. To Achieving the desired CG framework in Bangladesh, requires not only a strong national commitment to CG, but one that is also broad based.

Government should intensify its efforts to improve the regulation and corporate governance of SOEs:

Shortcomings in the governance of SOEs and FIs not only lower returns to the bank's shareholders, but, if widespread, it destabilizes the financial system. To restore confidence to both debt and equity markets, policy-makers and regulators need, in addition to ensuring adequate banking laws and regulations and supervision of banks' operations, to promote

⁶¹ Chaudhury, A.M. 2004. Corporate Governance – An Industry Perspective. *The Bangladesh Accountant*, October-December, Quarterly journal of the Institute of Chartered Accountants of Bangladesh.

⁶² Ahmed, Mamtaz Uddin, Yusuf, Muhammad Abu. 2005. Corporate Governance: Bangladesh Perspective. *The Cost and Management*. Vol. 33. No. 6. November-December 2005. pp. 18-26.

sound corporate-governance practices in the banking sector. Ownership and financial relationships should be disclosed. Self-dealing/related-party transactions should be subject to both banking and corporate-governance restrictions. Bank directors should be able to pass “fit and proper” tests for service. These directors should also assume responsibility for bank systems and procedures that ensure sound lending and monitoring practices, as well as the capacity to handle distressed debt. Lastly, local insolvency systems must protect and enforce creditors’ rights and provide efficient liquidation of debtors which cannot be expeditiously restructured into commercially viable enterprises.

Introduction of Good Governance Practices in SOEs:

In order to provide a strong demonstration effect, CG reforms in strategic SOEs that handle electricity generation and distribution, gas distribution, telecommunications, and air-transportation can be undertaken. These enterprises are fully owned by the Government.

All jurisdictions should strive for effective implementation and enforcement of corporate-governance laws and regulations:

Over the past several years, most South Asian countries have substantially revamped their laws, regulations and other formal corporate-governance norms. Bangladesh is still lagging behind in this matter. Leadership from the uppermost reaches of government is necessary to promote public confidence in the state’s commitment to the rule. In this regard, adoption of international accounting, audit and financial disclosure standards and practices will facilitate transparency, as well as comparability, of information across different jurisdictions. Such features, in turn, strengthen market discipline as a means for improving CG practices.

Institutional Capacity Building:

There is a need for disseminating CG and enterprise restructuring principles and for implementing the related guidelines and standards. Public awareness and development of governance structure i.e., enforceable regulation, ensuring financial transparency, stop financial malpractice and any form of market manipulation are essential for enabling a sound framework for CG. It is, therefore, required to educate the public about their rights as shareholders and about the work of modern corporations through our own specialized publications and through the national and regional mass media.

Improving the quality of Financial Reporting:

In Bangladesh, quality of financial reporting needs to be improved. This requires a robust regulatory regime and effective enforcement of the accounting and auditing standards. True independence of the auditor is at the crux of good CG. Auditors need to be able to function with real independence and without fear or favor. Simultaneously, auditors also need to be monitored through strict enforcement of professional code of ethics of auditors. In the long run, auditors will become irrelevant if they fail to act independently.⁶³ There must be a consolidating financial report for the group of companies.

⁶³ Chaudhury, A.M. 2004. Corporate Governance – An Industry Perspective. *The Bangladesh Accountant*, October-December, Quarterly journal of the Institute of Chartered Accountants of Bangladesh.

Chapter-VIII

Role of Dhaka Chamber of Commerce and Industry

Experience from around the world shows that good CG helps enterprises attract capital, strengthen their operations, and reduce conflicts between shareholders and management. Implementing and enforcing sound CG systems and practices is essential for Bangladesh in order to build confidence, strive to revitalize production, and further market reforms. To strengthen the overall environment for CG in Bangladesh, following issues are required to be undertaken:

Assist the Government of Bangladesh:

Implement the policy recommendations/interventions asserted in this study paper and assist the government on improving CG regulations, including the development and adoption of national CG codes.

High-level discussions on standard setting:

The long-term sustainability of promoting good governance practices requires that high-level support from the Government, regulatory bodies and stock exchanges is present. It could be suggested that high-level forums and conferences on corporate governance be organized on a regular, i.e., annual, basis. These activities will form a major component in building awareness and a positive culture for CG.

Capacity Building and advocacy initiatives:

- Work with the NGOs, such as institutes of directors, banking associations, civil society think tanks to increase their ability to advocate for further CG reforms.
- Training for the managers, board members and executives should be undertaken on regular basis in consultation with various stakeholders.
- Adopt a long-term strategy to educate the relevant stakeholders about the issues CG through conducting seminars, workshops and by conducting regular surveys of CG practices.

Education and studies on Corporate Governance Issues:

Develop and deliver CG course materials to potential researchers, business schools to ensure that future managers and lawyers understand the importance of good CG and have the skills to practice it.