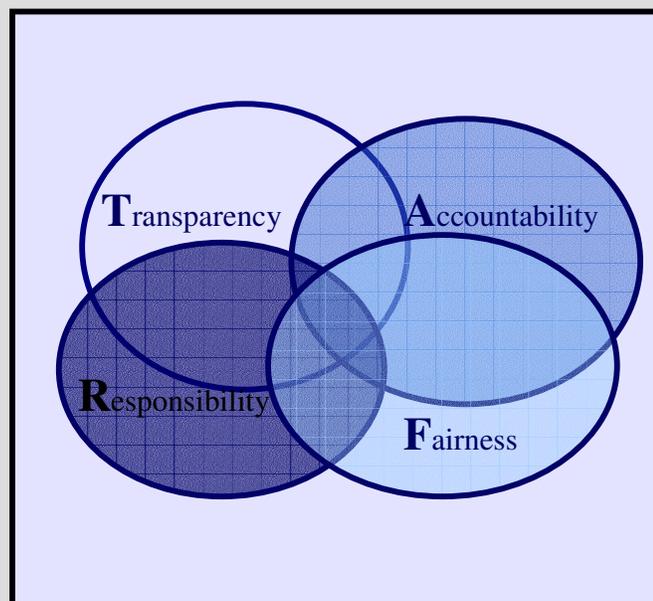


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**STATE OF CORPORATE
GOVERNANCE IN BANGLADESH**
Analysis of Public Limited Companies-
Financial, Non-Financial Institutions and
State Owned Enterprises

Dr. A. K. Enamul Haque
Mohammad Behroz Jalil
Farha Naz



CENTER FOR RESEARCH AND TRAINING

Working Paper Series



STATE OF CORPORATE GOVERNANCE IN BANGLADESH:

**ANALYSIS OF PUBLIC LIMITED COMPANIES – FINANCIAL, NON-
FINANCIAL INSTITUTIONS AND STATE OWNED ENTERPRISES**

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**EAST WEST UNIVERSITY CENTER FOR RESEARCH AND
TRAINING**

September 2007

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Abstract

Corporate governance (CG) is an important effort to ensure accountability and responsibility and is a set of principles, which should be incorporated into every part of the organization. This study focused on the state of Corporate Governance (CG) in three sectors of the economy: the private company (public-listed company), the financial enterprises, and the State Owned Enterprises (SOEs). To understand the state of CG, three broad aspects of governance and management issues were studied. These are: a) shareholders' rights, b) public disclosure of information, c) effectiveness of the Board. Within each of these many sub-categories were studied which were discussed in this paper. The study used interviews with key stakeholders, experts and executives of these types of companies, a questionnaire survey and also group discussions.

In terms of the three sectors, this study found that public-listed companies are more open to their shareholders with respect to shareholders rights and disclosures of information. With regards to public disclosure of information and transparency, companies use "box checking" method rather than understanding the spirit of the disclosure. On the issue of the active participations of the independent directors SOEs had a better rating than others. In public limited companies study found that in 40% of the cases independent directors rarely disapproved the agenda placed in the board. In the best practice guidelines of CG three major committees are recommended, study found other than SOE, financial and non-financial institutions are not complying with the best practices.

Keywords: State-Owned Enterprise, RAFT, FAT, Corporate Governance, Financial Institutions, Non-Financial Institution.

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Annexure -A: Questionnaire

I. Introduction

The need for corporate governance arises from the potential conflicts of interest among stakeholders in the corporate structure. These conflicts of interest often arise from two main reasons. First, different stakeholders have different goals and preferences. Second, the stakeholders have imperfect information as to each others actions, knowledge, and preferences. (Osman 2006)

Corporate governance (CG) is an important effort to ensure accountability and responsibility and is a set of principles, which should be incorporated into every part of the organization. Though it is viewed as a recent issue, there is, in fact, nothing new about the concept. Because it has been in existence as long as the corporation itself-as long as there has been large – scale trade, reflecting the need for responsibility in the handling money and the conduct of commercial activities. In the wake of accounting, leadership, and governance scandals at such large companies as Enron, Tyco, and WorldCom, corporate governance has succeeded to attract a great deal of interest as it focuses not only the long term relationship, which has to deal with checks and balances, incentives for managers and communications between management and investors but also the transactional relationship, which involves dealing with disclosure and authority. Numerous works, studies, and researches have been conducted to enact principles, codes, and guidelines for ensuring good corporate governance systems and culture within the organizations.

Sir Adrian Cadbury in 'Global Corporate Governance Forum', defined Corporate governance as: "Corporate Governance is concerned with holding the balance between economic and social goals and between individual and communal goals. The corporate governance framework is there to encourage the efficient use of resources and equally to require accountability for the stewardship of those resources. The aim is to align as nearly as possible the interests of individuals, corporations and society" (Cadbury, 2000)

The Dhaka Chamber of Commerce and Industry (DCCI) has been implementing a project, entitled Economic Reform and Research Enterprise, in co-operation with The Center for International Private Enterprise (CIPE) – an affiliate of the US Chamber of

Commerce, Washington D.C. One of the objectives of this project is to prepare economic policy papers on selected business sectors. DCCI requested to prepare a paper on “Principles of Corporate Governance for Public and Private Enterprise in Bangladesh.” According to the Term Of Reference (TOR) the scope of the study was limited to analyze the situation of corporate governance in the three types of Enterprises: Public limited companies - Financial and Non-Financial institutions and State Owned Enterprises (SOE).

II. Objectives of the Study

The broad objective of the research is to understand the state of corporate governance in Public limited companies - Financial and Non-Financial institutions and State Owned Enterprises (SOE) in Bangladesh. In particular, the research is expected to know the followings:

- a. The current practice of corporate governance in terms of accountability to its stakeholders
- b. How far the current practice of corporate governance passes the test of fairness.
- c. Whether corporate governance system in Bangladesh is transparent for all stakeholders.

III. Literature review

What is Corporate Governance?

Different authors view the meaning of corporate governance differently. For example, one school of thought describe corporate governance as a “system” by which companies are directed and controlled (Cadbury and Greenbury Report, CFACG 1992); another school views corporate governance as “structures and processes for decision making, accountability, control and behavior at the governing body” (Public accounts and Estimates Committee, 2002); to others corporate governance is about “finding ways” to ensure effective decision making (Pound 1995). But it must be kept in our mind that the fundamental concern of corporate governance is to ensure the conditions whereby a

firm's directors and managers are held accountable, ensure better and effective protection to all stakeholders. The World Bank argues that the framework of corporate governance should be based on four "pillars" – of Responsibility, Accountability, Fairness and Transparency (RAFT).

However, Kocourek (2003) believes that to counter the accounting, leadership, and governance scandals, organizations are rushing to institutionalize corporate governance, which may be even be counterproductive. The drive to more tightly regulate the membership and functions of corporate boards is already encouraging companies to view governance as a legal challenge rather than a way to improve performance. By reducing the critically important issue of corporate governance to what amounts to box-checking exercise, corporate directors and senior executives are addressing the symptoms, not the root cause, of the governance crisis. Kocourek states that governance begins at home – inside the boardroom, among the directors. It is embedded in *how, when, and why* they gather, interact, and work with one another and with management... in other words, the "soft" stuff. But qualitative reforms to the behaviors, relationships, and objectives of the directors and CEO are meaningless unless they are subject to the "hard" mechanisms of performance criteria, processes, and measurement. According to Kocourek, this combination of soft and hard solutions can turn corporate governance from vague concept into a means to deliver organizational resilience, robustness, and continuously improved performance.

Corporate Governance Scenario in Bangladesh

Corporate governance practices in Bangladesh are quite absent in most companies and organizations. In fact, Bangladesh has lagged behind its neighbors and the global economy in corporate governance (Gillibrand, 2004). One reason for this absence of Corporate Governance is that most companies are family oriented. Moreover, motivation to disclose information and improve governance practices by companies is felt negatively. There is neither any value judgment nor any consequences for corporate governance practices. The current system in Bangladesh does not provide sufficient legal, institutional and economic motivation for stakeholders to encourage and enforce corporate governance practices; hence failure in most of the constituents of corporate

governance is witness in Bangladesh. *Poor bankruptcy laws, no push from the international investor community, limited or no disclosure regarding related party transactions, weak regulatory system, general meeting scenario, lack of shareholder active participations* are some of the individual constituents that have been identified by Mamtaz Uddin Ahmed and Mohammad Abu Yusuf in their research study “Corporate Governance : Bangladesh Perspective” (Mamtaz and Yusuf, 2005).

Corporate Governance in Financial Enterprises in Bangladesh

As in many developing countries, banks play a vital role in Bangladesh economy, as the dominant financier for the industrial and commercial activities. Since the independence in 1971, the government until 1982, when the ‘ownership reform’ measures started in the financial sector, had carried out the regulation and ownership of all the financial institutions. During the reform period, two out of six National Commercial Banks (NCBs) were denationalized and private commercial banks were allowed to operate in the country. In 2003, out of the 49 banks operating in Bangladesh, 9 belong to the public sector, 30 are local private and 10 are foreign owned banks (Bangladesh Bank, 2003).

Despite the expansion, the operational efficiency of the banking institutions has continued to be dismal (Sayeed, 2002; Raquib, 1999). The sector witnessed decreasing profitability, increasing non-performing assets, provision and capital shortfalls, eroded credit discipline, rampant corruption patronized by political quarters, low recovery rate, inferior asset quality, managerial weaknesses, excessive interference from government and owners, weak regulatory and supervisory role etc (Hassan, 1994; USAID, 1995). Internal control system along with accounting and audit qualities are believed to have been substandard (World Bank, 1998; Raquib, 1999; CPD, 2001). Many of the problems have been attributed to lack of sound corporate governance among the banks. The reports by the Banking Reform Commission (1999) and BEI (2003) raises serious concerns on the banking sector and criticize the quality of governance that prevails in the banking sector in Bangladesh, which provides an impetus to explore the governance issues in detail in this paper.

Corporate Governance in State-Owned Enterprises in Bangladesh

In many developing countries, the state remains a significant owner of commercial enterprises that operate in comparative markets. State ownership includes businesses in several sectors, notably utilities and infrastructure, with energy, transport and telecommunication being usually the most important business. State Owned Enterprises have an undeniable capacity to deliver a positive contribution to the economy of a country, provided they are well managed and good management is built on strong foundations of good governance.

State Owned Enterprises, like any company, have a body of shareholders that the directors and management are accountable to, the only difference is that in this instance the shareholder happens to be government via a ministry.

State Owned Enterprises face specific difficulties regarding their governance. These governance difficulties derive from a number of characteristics that may be more or less acute depending on countries' *administrative traditions, the recent state sector reforms and the degree of liberalization of the economies concerned*. In order to grasp the specificity of SOE governance one should keep in mind the following two issues:

- Firstly, SOEs are often effectively protected from two major threats that are essentials in policing management behavior in public corporations i.e. the threat of takeover and bankruptcy.
- Secondly, accounting and disclosure may not reach private sector standards but rather be oriented towards public expenditure control, which may at the same time more burdensome and not fulfill the requirements of timeliness and materiality central to private sector disclosures practices.

There are 44 non-financial public enterprises in Bangladesh of which

- Six belong to industrial sector, under these six sector corporations there are a number of factories and industries.

- In Power, gas and water there are five
- Transportation and communication have eleven, and
- Trade three, Agriculture two, Construction four, and Service thirteen.

State Owned Enterprises in Bangladesh are besieged with same problems common to State Owned Enterprises throughout the world. Matter is more compounded by the vagueness in statutory reporting, non-existence of stakeholder pressure, nonexistence of peer pressure, political patronage.

Corporate Governance - Best Practices and Guidelines

Public Limited Company – Non Financial Institutions

In practice, corporate governance and monitoring mechanism recently focused on matters like the composition of the Board of Directors, the duties and responsibilities of the executive directors, regular monitoring by shareholders, voting rights of shareholders and detailed disclosure of company information that are material for decision making by interested parties. The guideline that good corporate governance frameworks project and facilitate is the exercise of shareholders' rights. Shareholders should have right to participate in, and to be sufficiently informed on, decisions concerning fundamental corporate changes. The equitable treatment of all shareholders, including minority and foreign shareholders should be ensured by corporate governance also. Stakeholders, including individual employees and their representative bodies, should be able to freely communicate their concerns about illegal and unethical practices to the board and their rights should not be compromised for doing this. Another important responsibility of corporate governance is time and accurate disclosure of all matters regarding the corporation. Information should be prepared and disclosed in accordance with high quality standards of accounting and financial and non-financial disclosures. Board members should act on fully informed basis, in good faith, with due diligence and care, and in the best interest of the organization and shareholders.

The board of Directors is the central entity in a functioning corporate governance system, since it is the governing body of any organization. The board is accountable to the

shareholders and/or stakeholders of the organization. To meet its organizational objectives the board must provide strategic policy and directions to the management, but should not be involved in day-to-day operational decisions. Management is accountable to the board, and therefore information systems that provide relevant, transparent, and material information to the board are imperative. (The Code of Corporate Governance For Bangladesh, Mar 2004, BEI)

The board size should be optimal with diverse expertise and experience to ensure a well-functioning and involved board. BEI guidelines state that ideally internationally successful corporate boards have memberships of 7 to 15 directors. BEI also stresses the need for mandatory retirement by rotation of 20% of the board; and the vacancies to be filled at the AGM. SEC in their notification dated 20th March 2006 in order to enhance corporate governance in the interest of investors and the capital market, imposes some further conditions to the companies listed with any stock exchange in Bangladesh. These conditions are imposed on a 'comply or explain' basis. The companies listed with any stock exchange in Bangladesh should comply with these conditions or shall explain the reasons for non-compliance. Board size proposed by SEC is not to be less than 5 (five) and not more than 20 (twenty). Cadbury report, Sarbanes-Oxley Act, BEI, SEC and other major works on CG also emphasize on the importance of independent directors in the board. All companies should encourage effective representation of independent directors on their Board of Directors so that the Board, as a group, includes core competencies considered relevant in the context of each company. For this purpose, the companies should comply with at least one tenth (1/10) of the total number of the company's board of directors, subject to a minimum of one, should be independent directors. According to SEC "Independent Director means a director who does not hold any share in the company or who holds less than one percent (1%) shares of the total paid-up shares of the company, who is not connected with the company's promoters or directors or shareholder who holds one percent (1%) or more than one percent (1%) shares of the total paid-up shares of the company on the basis of family relationship; who does not have any other relationship, whether pecuniary or otherwise, with the company or its subsidiary/associated companies, who is not a member, director or officer of any

stock exchange, and who is not a shareholder, director or officer of any member of stock exchange or an intermediary of the capital market.” The independent director(s) should be appointed by the elected directors.

Few other guidelines and best practices on corporate governance which receive considerable emphasize are:

- The position of the Chairman of the Board and CEO should be filled by different individuals.
- A company should appoint Chief Financial Officer (CFO), a Head of Internal audit and a Company Secretary.
- A company should have an audit committee as a sub committee of the board.
- Directors, in the Annual Report, should give representation of the true and fairness of accounts, compliance with accounting standard and proper internal control.

Public Limited Company – Financial Institutions:

Given the important financial intermediation role of banks in an economy, their high degree of sensitivity to potential difficulties arising from ineffective corporate governance and the need to safeguard depositors’ funds, corporate governance for banking organizations is of great importance to the international financial system and merits targeted supervisory guidance. The Basel Committee on Banking Supervision published guidance in 1999 to assist banking supervisors in promoting the adoption of sound corporate governance practices by banking organizations in their countries. This guidance drew from principles of corporate governance that were published earlier that year by the Organization for Economic Co-operation and Development (OECD) with the purpose of assisting governments in their efforts to evaluate and improve their frameworks for corporate governance and to provide guidance for financial market regulators and participants in financial markets.

Banking companies pose unique corporate governance attention as they differ greatly with other types of firms in terms of broader extent of claimants on the banks assets and funds. A group of entrepreneurs and/or executives could set up a banking business by putting very little equity from their own pocket as the nature of business itself guarantees

flow of enormous amount of funds in the form of deposits. The general approach to corporate governance argue in favor of the shareholders rights only, as managers/executives may not always work in the best interest of the shareholders (Henderson, 1986; Jensen and Meckling, 1976; Fama and Jensen, 1983). But the shareholders actually account for a very tiny portion of the bank's assets and funds. Rather almost every bit of banks' investments are financed by the depositors' funds. In case of losses or failures it will be depositors' savings that the banks would lose. Such risks demand priority in protection of depositors that ushers in a broader view of corporate governance that suggests the interest and benefits of the suppliers of funds for a firm should be upheld (Shliefer and Vishny, 1997; Vives, 2000; Oman, 2001). Macey and O'Hara (2001) also argue that a broader view of corporate governance should be adopted in the case of banking institutions, arguing that because of the peculiar contractual form of banking, corporate governance mechanisms for banks should encapsulate depositors as well as share holders. Arun and Turner (2003) supported the need for the broader approach to corporate governance for banking institutions and also argue for government intervention to restrain the behavior of bank management. In many countries, deposit insurance is used as a mechanism to safeguard the banking system as well as the depositors. However, Macey and O'Hara (2001) argues that in many instances, the presence of deposit insurance mechanism by the governments may encourage many bank insiders to embark upon self-benefiting risky deals taking the advantage of insurance protection. The self-dealing activities by the bank insiders are very dangerous to the performance and survival of the banks as scores of previous bank failures have been caused by risky self-dealing by the bank insiders (Jackson and Symons, 1999; Clarke, 1988). The presence of heavy liquid assets and potential lack of depositors' interest to actively control and monitor banks' risky decisions as a result of the insurance guarantees simplifies and aggravates the sharking in the banking firms.

Banks in developing countries are faced with high risk of sharking as a result of heavy government ownership, lack of prudential regulation, weak legal protection and presence of special interest groups ((BCBS, 1999; Arun and Turner, 2003). The independent regulatory agencies are important in developing countries to act against the frequent collusion among government, businesses and bankers to serve special interest groups

(Shleifer and Vishny, 1997; Arun and Turner, 2002). However, there is an argument that active role by regulators may cause problems as well, as regulators may not have a convincing/sufficient motivation to monitor the banks as they do not have much at stake in case of bank failures (Macey and Garrett, 1988). Recently, the financial markets of developing economies have experienced rapid changes due to the growth of wider range of financial products. As a result of this, banks have been involved with high risk activities such as trading in financial markets and different off-balance sheet activities more than ever before (Greuning and Bratanovic, 2003), which necessitates an added emphasis on quality of corporate governance of banks in developing economies.

Asian Roundtable on Corporate Governance (ARCG) Task force developed the *Policy Brief on Corporate Governance of Banks in Asia* (June 2006). The main issues and priorities for reforms in CG of banks in Asia that were identified are:

- The responsibility of individual board members – *fiduciary duties of bank' board members, need of skills, personal abilities, training programs on integrity and professionalism.*
- The roles/functions of the board – *guiding, approving and overseeing strategies/policies rather than being immersed in day-to-day operations. Creating clear accountability lines and internal control systems. Sufficient flows of information and managerial support.*
- The composition of the board – *banks are more encouraged to have independent directors than other firms. Separation between Chairman and CEO.*
- The committees of the board – *audit committee, the Risk Management Committee, The Governance Committee with combined responsibilities of Nomination, remuneration, succession planning, training, performance evaluation, etc.*
- Preventing abusive related party transactions – *inspection of the existing firewall. Creation of specialized committee to monitor and approve related-part transaction. Publicly disclose such transaction.*

- Bank holding companies and groups of companies holding banks – *a bank's parent company should not impede the full exercise of the CG of the bank within the banking group.*
- Disclosure – *effort on convergence into international standards on accounting, etc. should be encouraged.*
- Bank's autonomy in relation to the state – *state as owner should respect the legal corporate structures of State Owned Commercial Banks (SOCB).*
- Bank's monitoring of the CG structure of its corporate borrowers – *Extent to which banks should assess/monitor CG of their corporate borrowers or seek to improve it.*

State-Owned Enterprises (SOE)

Organizations for Economic Co-operation and Development (OECD) guidelines for State Owned Enterprises are:

- Ensuring an Effective Legal and Regulatory Framework for State Owned Enterprises: The legal and regulatory framework for State Owned Enterprises should ensure a level-playing in markets where State Owned Enterprises and private sector companies compete in order to avoid market distortions.
- The State Acting as an Owner: The state should act as an informed and active owner and establish a clear and consistent ownership policy, ensuring that the governance of SOE is carried out in a transparent and accountable manner, with the necessary degree of professionalism
- Equitable Treatment of Shareholders: The state and SOE should recognize the rights of all shareholders and ensure equitable treatment and equal access to corporate information.
- Relations with Stakeholders: The state ownership policy should fully recognize the SOE responsibilities towards stakeholders and request that they report on their relation with stakeholders.
- Transparency and Disclosure: SOE should observe high standards of transparency.
- The Responsibilities of the Board of State-Owned Enterprises: The boards of SOE should have the necessary authority, competencies and objectivity to

carry out their function of strategic guidance and monitoring of management. They should act with integrity and be held accountable for actions.

IV. Methodology

The state and nature of corporate governance in Bangladesh are guided by several factors: a) company law, b) government regulations, c) SEC requirements, and d) pressure from buyers or peer pressure. The cumulative impact of these factors results in a corporate behavior which is followed in Bangladesh. However, this may not be the 'best' practice in the world of good corporate governance. Some of the best practices and guidelines of corporate governance are coded in the company laws and regulations and are expected to be practiced in Bangladesh. In this regard, it is possible that companies follow them because it is mandatory and yet may not fully comply with the essence of the rules and regulations. Considering all these, the multiple methods were used to study the state of corporate governance in Bangladesh.

In the first instance, extensive literary reviews indicated that corporate governance has been addressed, analyzed, defined from various perspectives. In order to narrow it down the scope the study concentrated on three sectors of Bangladesh. These are: a) state owned-enterprise (State Owned Enterprises), Public limited companies both b) financial institutions, and c) non-financial institutions.

After this, a series of discussions and meetings with key personnel of the organizations such as active board members, board secretaries, and company executives were held to identify the focus of the study within the context of Bangladesh. Similarly, consultation with academics and researchers were also conducted to further broaden the study.

It was found that the key issues related to ensuring good governance in the corporate sector includes a) transparency to all stakeholders, b) accountability of the management and the board, c) fairness in the decision making, and d) responsibility of the management and the board . Ensuring these in a corporate culture requires following rules and regulations both in the spirit and in the practice.

Based on these preliminary findings, a questionnaire was developed to collect specific information on the state of corporate governance in some selected industries. The

questionnaire was divided into several sections: a) company profile, b) shareholders' rights and disclosure, c) public disclosure and transparency, d) effectiveness of the board, e) function of the board, and f) effectiveness of the independent directors. Preliminary discussion with key stakeholders also revealed that the corporate sector is yet not ready to reveal information beyond their statutory requirements. At this point, the questionnaire was made semi-structured to allow for in-depth interviews with key individuals of the companies. In each company, this led to several rounds of discussions and interviews with more than one individual.

Category	Interviewed (Formal, Informal)	Discussed
Companies	16	2
MDs/CEOs	9	5
Experts	4	14

However, because of the political changes in Bangladesh, and because of the actions taken by the government on several key companies (due to allegation of tax evasion and other malpractices), it became extremely difficult to collect information. The Dhaka Chamber of Commerce and Industries (DCCI) also provided assistance through its members so that the companies cooperate with the study team. However, even after repetitive assurance some organizations were reluctant to answer all the questions in writing. As a result, while the study team took interviews of some 20-25 individuals, information remained incomplete. This has limited the ability of the study team to analyze the results using quantitative techniques.

V. Findings

The state and nature of corporate governance has been studied under five general headings. Three types of companies were studied: a) the public corporations - these are mainly public utility companies operated by the government with a board of director consisting of civil bureaucrats and few experts, b) financial institutions like banks which are listed in the Dhaka Stock Exchange and c) non-financial public limited companies also listed in the stock exchanges in the country but without any government share.

Five specific aspects of good corporate governance practices that are examined are briefly explained in the following sections.

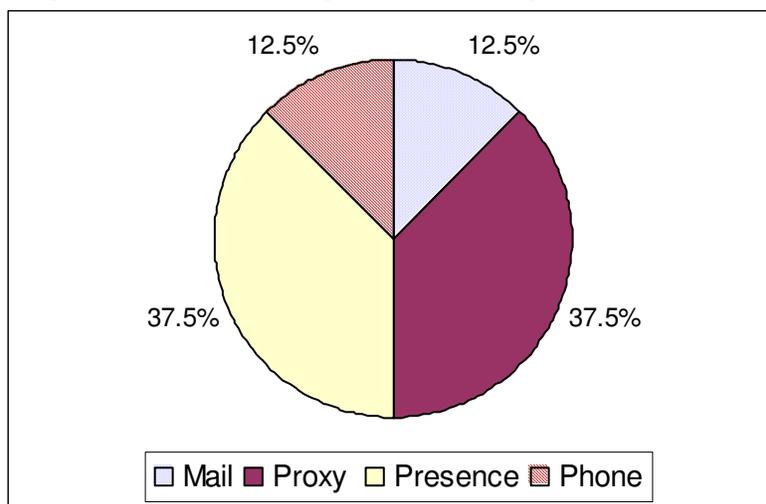
Shareholder Rights and Disclosure of Information

On the issue of shareholders' rights and disclosure, the study investigated several key issues: i) the practice of voting in the Annual General Meeting of the companies, ii) disclosure of information in terms of knowing the agenda, iii) lead time to analyze information, iv) information on equity of major shareholders, v) practice of nomination and disclosure of director candidates in the meeting, vi) rights of the minority shareholders in nominating candidates, and vii) rights of the shareholders in terms of opposing candidates nominated by the management. To understand shareholders' rights the study used several proxy variables like a) length of the meeting, and b) attendance in the meetings. Duration of the meetings indicates whether shareholders' are given opportunities to debate on issues related to their interest or not. Similarly, higher attendance of the meeting indicates presence of a pluralistic environment in the decision making process. It was found that duration of the AGMs in these companies were mostly between 2-3 hours. For public limited companies number of shareholders attended the last AGM are between 300 and 6000.

Ease of participation in voting by shareholders

Figure 1 illustrates that in terms of ease of participating in the meetings, shareholders used several options to express their opinion. Most of the shareholders either participate in person or nominate an individual to vote.

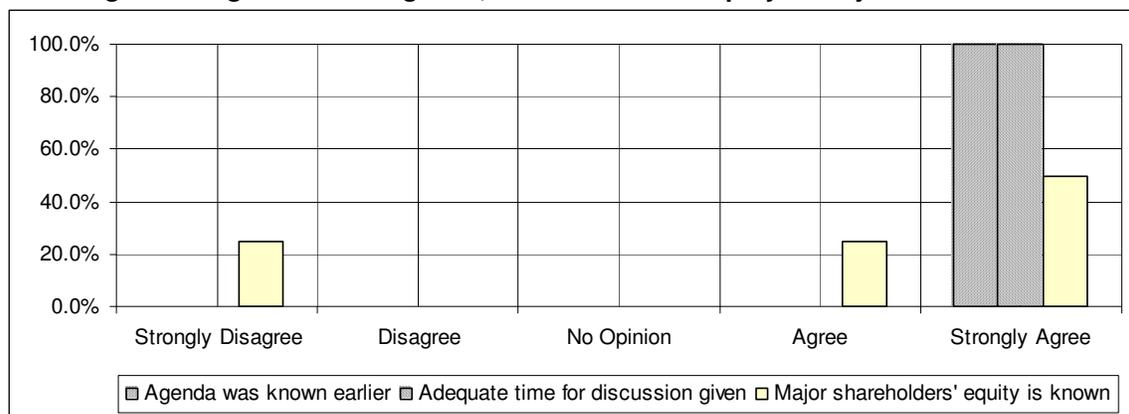
Figure 1: Ease of Participation in AGM by the Shareholders



Knowledge on AGM Agenda and Equity of Major Shareholders

It is important that shareholders' know the agenda of the meeting well in advance, can discuss their views in the meeting and have knowledge about the equity position of the major shareholders. These are important elements for ensuring good governance at the corporate level to safeguard rights of the smaller investors in the company. Figure 2 shows that except for equity of the major shareholders, this is not of a matter of concern in Bangladesh.

Figure 2: Right to know Agenda, Discussion and Equity of Major Shareholders



Nomination of Director's Candidate

Nomination of candidates in the meeting is an important element to ensure transparency in the governing the company. Study result (Table 1) shows that while a majority of the shareholders knew about the Director's candidate prior to the AGM, however, some had no idea about it. This information should have been known to all. A failure implies lack of transparency in the corporate governance.

Similarly, only 50% of the shareholders mentioned that minority shareholders could nominate their candidates.

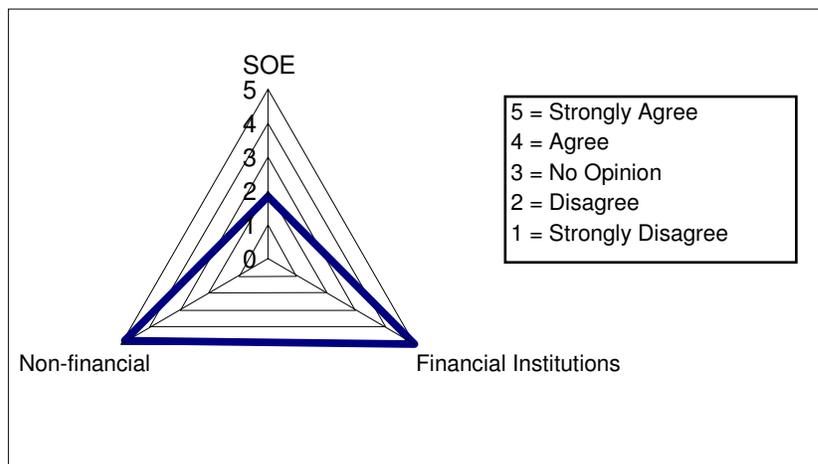
Table 1: Disclosure and Rights of the Shareholders - nomination of candidates

	Prior disclosure of Director's candidate	Nomination of Candidates by minority shareholders
Yes	75.0%	50.0%
No	25.0%	50.0%

Summary by three types of companies

In terms of three sectors, this study found that financial and non-financial public limited companies are more open to their shareholders compared to SOEs (Figure 3). This illustrates that regulatory structure imposed upon public limited companies - financial and non-financial enterprises are more effective than on state-owned enterprises. In other words, regulatory agencies are rather relaxed in implementing such requirements on government corporations.

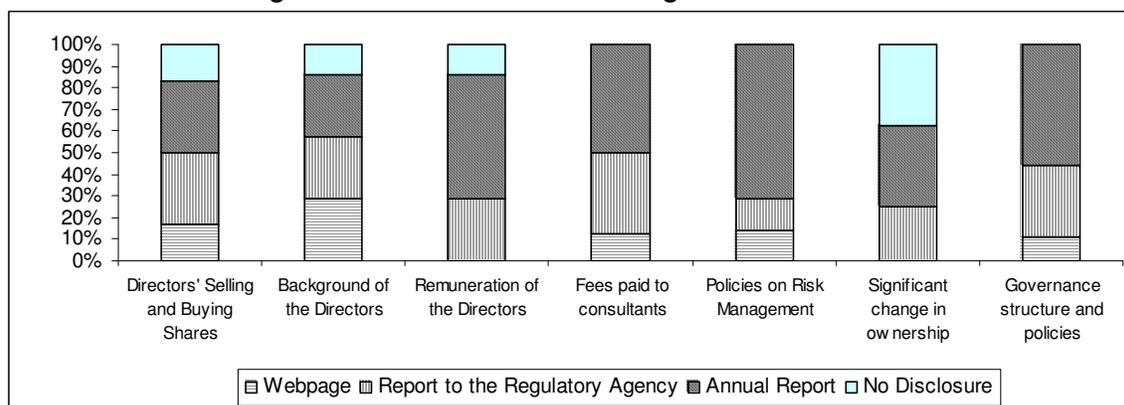
Figure 3: Opinion of the Management on the Rights to Disclose Information to the Shareholders



Public disclosures and transparency

Public disclosure is an important element of governance in the corporate world because it builds trust, helps bring new investors and ensures smooth functioning of the capital markets and excels the company growth. It is, therefore, a requirement in our SEC's code of conduct.

Figure 4: Public Disclosure through different modes



Seven different aspects of corporate governance with respect to public disclosure were studied. These are: i) directors' selling and/or buying shares of the company, ii) background of the directors, iii) remuneration of the directors, iv) fees paid to consultants, v) policies on risk management, vi) significant changes in the ownership, and vii) governance structure and policies.

Figure 4 shows Annual Reports, and Reports to Regulatory Agencies consist the bulk of the disclosure tool for these companies. In other words, companies used 'box checking' method to provide information to the regulatory agencies rather than understanding the essence of public disclosure as a whole. On four of the aspects (stated above), some companies had zero disclosure. The study found that 17% of the companies did not disclose director's selling or buying of shares, 14% did not disclose background or profile of the directors, 14% did not disclose remuneration paid to the directors and 37% did not disclose significant changes in the ownership of the company. These are contrary to the principles adopted in the best practice of CG.

Effectiveness of Board

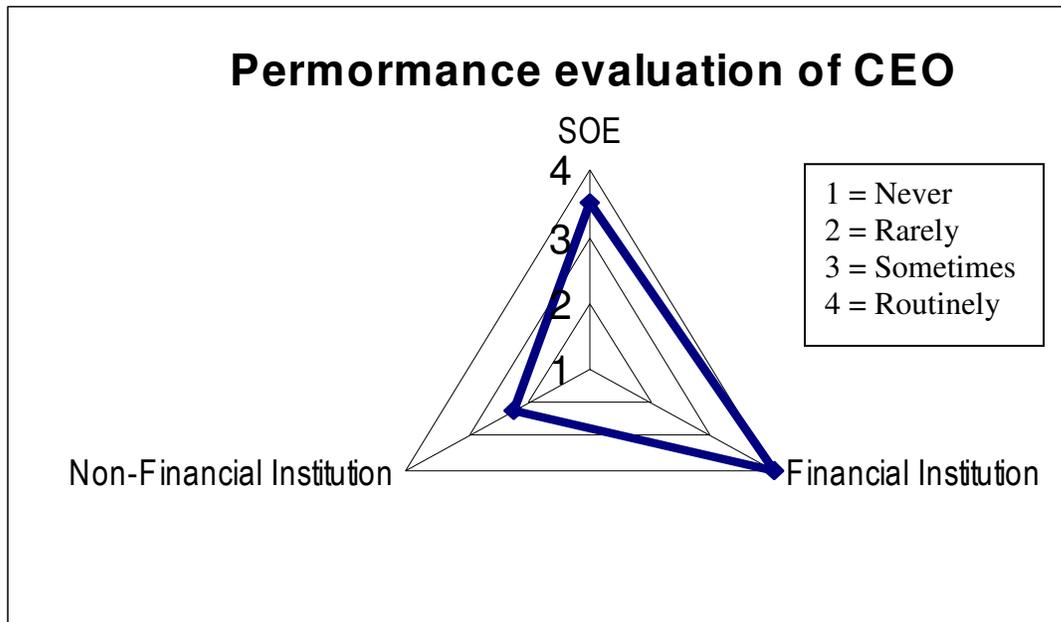
On this issue, to determine the effectiveness of the board several factors were examined: (1) size of Board and structure (2) presence and effectiveness of the independent directors (3) separation of chairman and CEO (3) performance evaluation of the CEO by the board. In the SOEs, on an average eight out of nine directors are independent directors, in public limited companies – financial and non-financial institutions, board size and number of independent directors were found to be within the statutory requirement stated by SEC.

Study found that CEOs and the Chair of the Board are always separate individuals in all cases.

Evaluation of CEOs

Study further indicates that both SOEs and Financial institutions routinely evaluate and review the performance of the CEOs and compensation packages. However, in the

Figure 5: Performance Evaluation of the CEOs



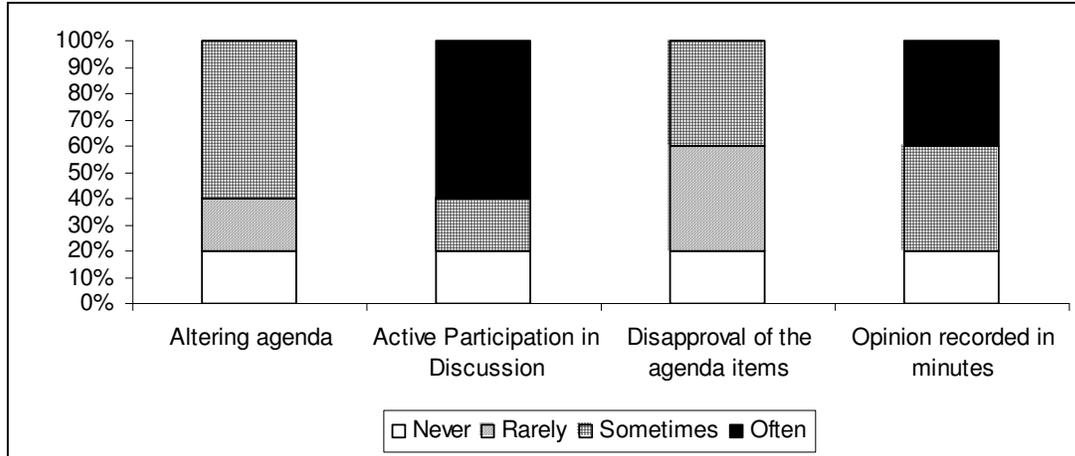
private sectors this procedure is rarely practiced (Figure 5).

Role of the Independent Directors

On the issue of active participations of the independent directors in the board meetings, State Owned Enterprises had a better rating than others. This is possibly due to the fact that at SOEs the Board mostly consists of independent directors. In the financial sectors, the study did not find a significant role of independent directors whereas in the non-financial public limited enterprises the role of independent directors is intermediate in nature. Factors that were investigated to measure the role of independent directors in the board meeting in (i) altering the agenda set by CEO, (ii) participating discussions, (iii) disapproving the agenda, and (iv) recording opinions in the minutes. Figure 6 shows that in 20% of the cases, cases, independent directors were never active in the meetings of the board. In another 20% of the cases, independent directors rarely intervened to alter the

agenda of the meetings and in 40% of the cases, they rarely disapproved the agenda placed in the board. Independent directors rarely participated in the meeting of the private companies

Figure 6: Role of Independent Directors in the AGM

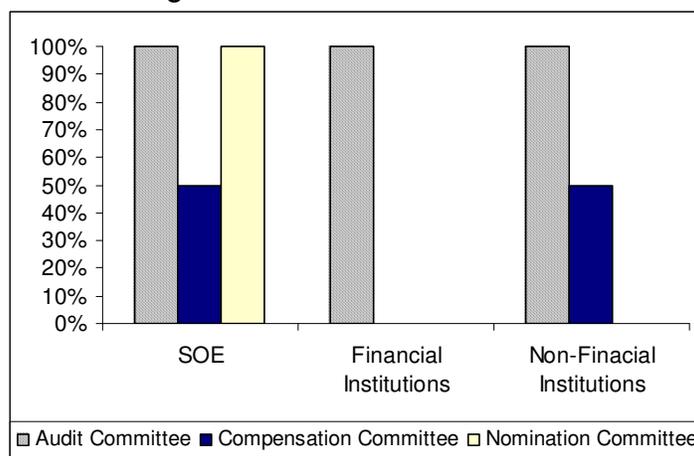


These illustrate the weakness of the system to use independent directors to safeguard the interests of the small investors.

Committees

Interests of the investors and other stakeholders in the company are safeguarded through various committees. In the best practice guideline, three major committees are recommended. These are: a) audit committee, b) compensation committee and c) nomination committee. In the SOEs, all three committees are found to be present whereas in public limited (non-financial institution) the nomination committee was missing and in the financial institutions only the audit committee existed. Existence of the audit committee in all companies is the effect of the statutory requirement. This is, rather, a poor show for the corporate sectors in Bangladesh.

Figure 7: Presence of Committees



To measure the effectiveness and independence of the audit committee several variables like (i) presence of expert domain knowledge (ii) chairing by the independent directors (iii) recording of the minutes (iv) approval of remuneration by the shareholders, and (v) presence of an audit rule of companies, (vi) use of external auditor were investigated, and (vii) use of internal auditors by the company, were used.

Figure 8: Effectiveness and independence of the Audit Committee

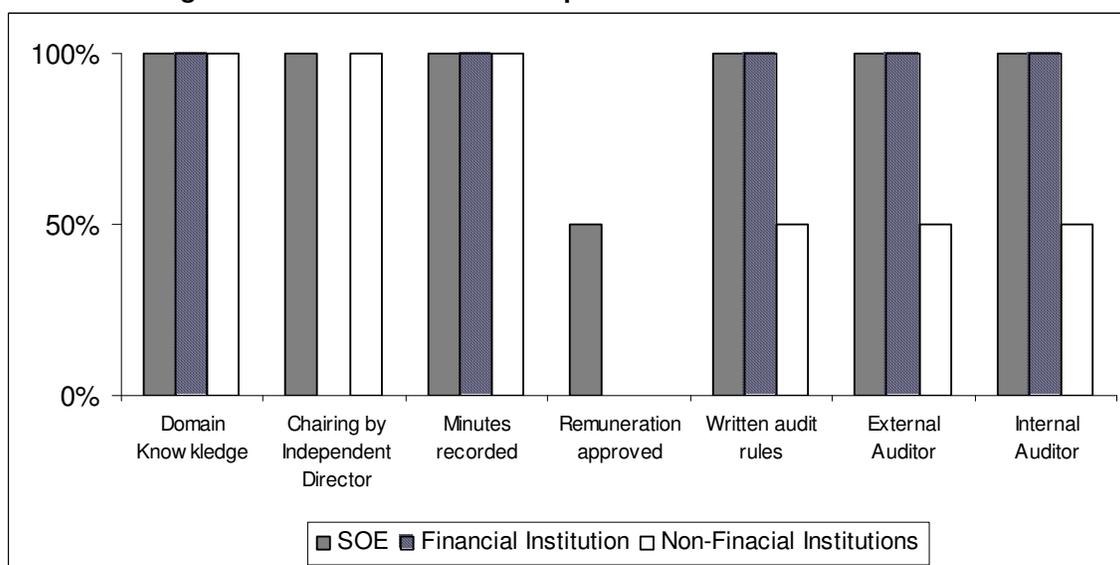


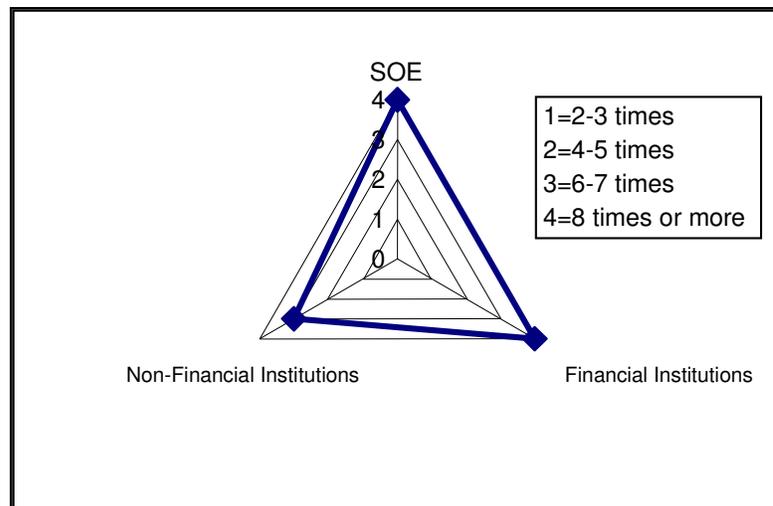
Figure 8 shows that in the audit committee, members have requisite knowledge to work in the committee and it is valid for all types of enterprises. It has been observed that in SOEs and in Public limited non-financial institutions, audit committees are sometimes chaired by the independent directors while in financial enterprises it is not the case. Interestingly, on the remuneration of the members of the audit committee, SOEs

discussed the matter in the AGMs separately while for others there was no separate discussion on the remuneration issue. This is perhaps due to the fact that remuneration for members of committees in SOEs are usually nominal and so they might have discussed remuneration of the audit committee members separately to increase their allowances. What is more interesting is that all non-financial enterprises (listed companies) did not have written audit rules; neither had they regularly reviewed functions of the external and the internal auditors. This shows a weakness in the function of the audit system in non-financial enterprises public limited companies.

Board Meetings

Figure 9 shows that the meetings of the board were held quite frequently and in terms of average attendance, and time spent the survey found that average time spent for each meeting is between 1 and 3 hours whereas between 70% and 100% of the members attended these meetings.

Figure 9: Number of Board Meetings in a Year



VI. Findings and Conclusions

This study focused on the state of Corporate Governance (CG) in three sectors of the economy: the Non-financial Institutions (public-listed company), the financial enterprises, and the State Owned Enterprises (SOEs). To understand the state of CG, three broad aspects of governance and management issues were studied. These are: a)

shareholders' rights, b) public disclosure of information, c) effectiveness of the Board. Within each of these many sub-categories were studied which were discussed above.

The study used interviews with key stakeholders, experts and executive, of these types of companies, a questionnaire survey and also group discussions to arrive at the following conclusions.

Shareholders Rights and Disclosures of Information

In terms of three sectors, this study found that financial and non-financial public limited companies are more open to their shareholders compared to SOEs. This means that except for SOEs, shareholders of the companies do receive information to protect their interests in the company. In the SOEs, the dominant player, the state, is more powerful and do not adequately share information with minority shareholders. As a dominant shareholder, the state is capable of abusing the rights of minority shareholders. State Owned Enterprises need to improve the practice of disclosure of information to all shareholders, so that other shareholders feel that they are treated equitably. The state's track record in terms of respecting rights of all the stakeholders has a significant impact on the value of shares in the market and it is important for the company's future growth. As more and more SOEs are considering floating shares in the market (as a means of privatization) respecting the rights of minority shareholders' and disclosure of information to them will play an important role for the SOEs' success.

Public Disclosures and Transparencies

Most of the codes and principles that have been introduced throughout the world are based on some common pillars, whether it is RAFT (responsibility, accountability, fairness, and transparency) or FAT (fairness, accountability, and transparency), transparency issue is a major factor common to all. Laws have been enacted to protect this issue. Even in Bangladesh, SEC, Bangladesh banks, and other regulatory bodies made it mandatory for the organizations to report crucial information such as information with regards to

1. Directors' selling and buying shares in their company
2. Background of directors
3. Remuneration of directors

4. Fees paid to external auditors, advisors
5. Policies on risk management to stakeholders.

The principle objective of this disclosure of information is to ensure transparency. Organizations in all the three sectors need to improve their procedures of disclosures. At present most of the above issues are reported in Annual Reports (AR) and/or in the Reports to the Regulatory (RR) agencies. However rather than using a box checking methods (i.e. carrying out minimum requirements that ensures that the organization is complying with the regulations) organizations should focus more on the spirit of the disclosure. Some issues like directors selling or buying are not disclosed at all. This is crucial for the potential future investors of the enterprise. Directors remuneration are also rarely disclosed, this needs further improvement.

In the case of disclosure and transparency to the public State Owned Enterprises are doing better than the public limited companies both financial and non-financial institutions. The latter should develop and promote the culture of disclosure to public in more effective manners.

Effectiveness of the Board of Directors

Four separate issues were studied to understand the effectiveness of the board. An effective board is a sign of healthy corporate culture. These are discussed below.

CEOs are expected to carry out the vision of the board, take decisions and report to the boards the status of the organization on a regular basis. Board is expected to evaluate the performance of CEO in order to ensure good practice of corporate governance. In this particular case financial institutions and State Owned Enterprises are doing better than the non-financial public limited enterprises. Non-financial public limited organizations rarely evaluate their CEOs, this could be because in many cases CEOs are directly linked and/or have more shares than the other members of the board. This practice will not create a healthy and effective board culture.

Independent directors are appointed in board by law to protect the interest of the numerous small shareholders of the organization. Although most financial institutions have independent directors (following the legal compliance) they rarely or never

intervene in the decision making process of the board; where as independent directors in non-financial public limited organization play nominal role. In case of SOE independent directors have significant influence in the decision making process of the board. It is therefore concluded that the spirit of appointing independent directors taken seriously and individual with expertise and reputation should be appointed as independent directors.

Board of the directors appoints statutory committees to ensure accountability, transparencies, and fairness. OECD Principles, Basel corporate governance guidance and others have stressed the importance of specialized committees of the board. Audit Committee, Compensation Committee, Nomination Committee, and Risk management committee (for the financial institution) are but few such specialized committees which are functioning effectively in the organizations where sound corporate governance practice is found. Except Audit Committee other committees like Compensation Committee, and Nomination Committee rarely exists or effectively operates in Bangladesh's Public limited companies (financial and non-financial institutions). State Owned Enterprises are only organizations where we find existence of all the three committees. Although audit committees were present in all three sectors, their effectiveness is questionable, especially in private and in financial institutions.

Given the above discussion and findings, it is fare to conclude that corporate culture in Bangladesh is still in a state of infancy. While we have created legal requirements for good corporate governance, rushing to institutionalize the culture of governance through legal and regulatory requirements or through external pressures will do more harm than good to the culture. Under such circumstances, the spirit of the good governance will be lost and rather perfunctory structure will take place. The objective of practicing good governance is to help the corporation as well as the society and the nation. It promotes a mechanism to use the capital market to enhance the growth of the corporations and for this it is important that corporate sector are educated to understand the benefits from good corporate governance. It is under such a scenario, the state of governance in our corporations will mature.

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Annexure-A

Questionnaire Survey on Corporate Governance Practices at State Owned Enterprises, Public limited Financial and Non-Financial Institution in Bangladesh

Dear *Respondent*

Thank you very much for your willingness to this survey. The Dhaka Chamber of Commerce and Industry (DCCI) has given us the opportunity to do this research survey to understand corporate governance practices at State Owned Enterprises, Public limited Financial and Non-Financial institution in Bangladesh.

The survey is asking question on the practices in your company/institution regardless of the law and regulations. Your accurate and frank response is the key.

The results will be used only for the research purposes and be presented only in aggregate manner without revealing the identity of individual company/institution.

Please Mark (✓) the appropriate answer by filling the box or express the extent to which you agree or disagree on the given statement by choosing (circle) one of the following:

5= Strongly agree

4= Agree

3=No opinion

2=Disagree

1= Strongly disagree

I. General Information on the Company/Institution and Respondent

- 1. Respondent's Name:
- 2. Sex: [1=Male, 2=Female]
- 3. Age:
- 4. Position: [1=Director, 2=Manager, 3=Executive, 4=Other]
- 5. Company Name:

Please fill in the box from the following answers: **(Q6-Q12)**

- 6. How do you describe the ownership and control structure of the company?

1=The largest shareholder has a substantial voting right and effectively controls the company. (You can express share percentage if you want) or (say over 30%-40% including that of companies he/she control.

2=Two or more large shareholders collectively control the company

3=Ownership is fairly disseminated with no controlling shareholder, and shareholder does not directly control the management

4=Others (Please Explain:

- 7. Is the company stand-alone company or a subsidiary of a business group or holding company?

1= Stand-alone company

2= Subsidiary of a family based business group.

3=Subsidiary of a business group not control by families.

4=Others (Please Explain:

- 8. Is the company wholly or partially owned and control by the government?

1= Yes, substantially owned and controlled by the government.

2= Partially owned, but not much controlled by the government.

3=Others [Please explain:

- 9. Is the firm wholly or partially owned and controlled by foreigners (foreign companies)?

1= Little owned by foreign investors

2=Yes, substantially owned and controlled by foreigners (foreign companies).

3= Substantially owned, but not controlled, by foreign investors.

4=Others [Please explain:.....

10. What relation does the CEO have with the founder or the largest shareholder?

- 1= Founder himself/herself
- 2= Founder's family member.
- 3= Professional manager.
- 4= Others: [Please explain:.....]

11. What is the ownership/control structure of the biggest creditor bank of your company?

- 1= Mainly government-owned .
- 2= Belong to the same business group as the firm
- 3=Belong to a business group not related with the firm
- 4= Mainly owned and controlled by a foreign financial institution(s).

12. Does your company have a labor union(s)?

- 1= Yes
- 2= No

II. Shareholder Rights and Disclosure of Information:

13. How easy is it for your shareholders to participate in voting at the shareholders' meeting?[May be more than One Answers]

- 1= Is voting by mail allowed?
- 2= Can anybody serve as a proxy?
- 3= Presence Requires
- 4=Others [Explain.....]

Express the extent to which you agree or disagree on the given statement by choosing (circle) one of the following:

14. Do you agree with the following statements for your company?

14.a. Shareholders are provided with adequate information on the agenda items of the shareholders' meeting ... [(5),(4), (3), (2),(1)].

14.b. Adequate time is given for asking questions and placing issues at the shareholders' meeting: [(5),(4), (3), (2),(1)]

14.c .It is not difficult to know how much equity ownership the major shareholders control (including the equity shares of companies they control)?

----- [(5),(4), (3), (2),(1)]

15. Role of shareholders in practice in nominating candidates and electing outside directors of your company:

Please Mark (✓) the appropriate answer by filling the box from **(Q15a-Q15c)**

15a. Are director candidates disclosed before the shareholders' meeting?

1=Yes

2= No

15b. Can minority shareholders (holding more than a certain level of shares) nominate candidates at the shareholders' meeting or prior to the meeting (to have the company disseminate relevant information)?

1=Yes

2= No

15c. Would it be possible for the director candidates proposed by the management of your company to fail to be elected at the shareholders' meeting?

1=Sometimes

2= Rarely

3= Unthinkable

iii. Information about the latest annual shareholders' meeting:

16. How long did the meeting last?

1= Less than 30 minutes

2= (30-60 minutes)

3=(2-3 hours)

4= Over 3 hours

17. How many shareholders attended the meeting? persons

iv. Disclosure and Transparency

13. Does your company disclose the following information? If yes, then by what means?

Web: company's web page **AR:** annual report

RR: report to regulatory agencies **No:** no disclosure

Please Fill in the box from the appropriate answers: Questions (13a-13g)(May be More than One Answers):

13a. Directors' selling or buying shares in their company:

1=Web

2= RR

3=AR

4=No

<input type="checkbox"/>	<input type="checkbox"/>
--------------------------	--------------------------

13b. Resume/background of directors:

1= Web

2= RR

3=AR

4= No

--	--

13c. Remuneration of directors:

1= Web

2= RR

3=AR

4= No

--	--

13d. Fees paid to external auditors, advisors, and other related parties:

1= Web

2= RR

3=AR

4= No

--	--

13e. Policies on risk management:

1= Web

2= RR

3=AR

4= No

--	--

13f. Significant changes in ownership:

1= Web

2= RR

3=AR

4= No

--	--

13g. Governance structures and policies (explicit corporate governance rules and vision)

1=Web

2= RR

3=AR

4= No

--	--

14. How timely and informative are the disclosures?

14a. Does your company disclose semi-annual reports?

1= Yes

2=No

--

14b. Does your company disclose quarterly financial statements?

1=Yes

2=No

--

14c. Does your company have a web-site? Is it also in English?

1= Yes

2=No

14d. Available and very informative both in local language and English:

1= Yes

2=No

3= No web-site yet

.V. Effectiveness of the Board of Directors

15. Board Size and Structure

1. How many directors does your (supervisory) board have in total? []

2. How many outside directors does your board have? ----- []

3. How many independent directors does your board have? ----- []

16. Are there any foreign nationals on your board?

1= Yes

2=No

17. Does the CEO of your firm also serve as board Chairman?

1= Yes

2=No

18. How is the CEO evaluated and compensated? Please Mark the answer by filling the following box:

18a. Does your board or compensation committee formally evaluate the CEO's performance?

1=Yes, as a routine

2= Sometimes

3= Rarely

4=Never

18b. How about the review of CEO compensation?

1=Yes, as a routine

2= Sometimes

3= Rarely

4= Never

18c. Is the CEO given a stock option?

1= Substantially

2= Some

3= None

19. How prevalent are the following practices? Please Mark the appropriate answer by filling the following box:

19a. Independent directors altering or adding the board meeting agenda set by the CEO:

- 1=Often
- 2=Sometimes
- 3=Rarely
- 4=Never

19b. Independent directors participating actively in board discussions

- 1=Often
- 2= Sometimes
- 3=Rarely
- 4=Never

19c. Agenda items disapproved at the board meetings by independent directors

- 1=Often
- 2=Sometimes
- 3=Rarely
- 4=Never

19d. Independent directors' positions on board meeting agendas recorded in minutes

- 1=Often
- 2= Sometimes
- 3= Rarely
- 4=Never

VI. Functions of the Board and Board Committees

20. Does your board have the following committees? What proportion of the Committee members are independent directors [50%, 2 out of 3, etc.]? [] Please check Mark the appropriate answer by filling the following box:

20a. Audit Committee:

- 1= Yes
- 2=No
- 3=Other Explain.....

20b. Compensation Committee:

- 1= Yes
- 2=No
- 3=Other Explain.....

20c. Nomination Committee:

1= Yes

2=No

3=Other Explain.....

21. (If you have an audit committee) How effective and independent are your audit committee?

21a. Does it have someone with accounting/finance expertise?

1= Yes

2=No

21b. Does a genuine independent director chair the committee?

1= Yes

2=No

21c. Are minutes written for each audit committee meeting?

1= Yes

2=No

21d. Is each member's remuneration approved separately at the shareholders' meeting?

1= Yes

2=No

21e Are there written rules governing overall audit function in your company?

1= Yes

2=No

21f. Does your company select/recommend the external auditor and conduct a proper review of his work?

1=Very much so

2= To some extent

3= Hardly

21g. Does it approve the appointment of the internal auditor and supervise him to routinely review risk exposure and accounting procedures?

1=Very much so

2= To some extent

3= Hardly

22. General Support for Directors

22a. Does the company provides any education or training opportunities for directors beyond what is mandatory?

1=Actively

2= Occasionally

3= Never

VI. Board Meeting Frequency, Attendance, Etc.

23. How much time and effort did directors devote to board meetings last year?

23a .How many board meetings were held last year?

1=(2-3 times)

2= (4-5 times)

3= (6-7 times)

4=(8 times or more).

23b. On average, how many hours did a board meeting last? Not more than:

1=(1)

2=(1-2)

3=(2-3)

4=(3-4)

5= Above 4

23c. What was the average attendance rate for board meetings?

1=(90-100%)

2=(80-90%)

3=(70-80%)

4=(60-70%)

5=(50-60%)

Thank you very much.

Now we would like to get some factual information on your company's human resources.

Please feel free to ask your secretary or whomever you deem appropriate to fill out the remainder of the survey.

VI. Human Resources

22. How many employees does your firm have? ----- [] persons

22a. Full Time.....[]

22b.Part Time.....[]

23. Roughly what percent of your employees belong to the following groups?

1. Managerial and supervisory employees ----- [] %

2. Employees working for more than 10 years at your firm ----- [] %

3. Employees graduated from a 4-year college or university ----- [] %

4. In the past three years, by what percent has the size of your firm's workforce changed?

1=(%Increased by).....

2=(%, Decreased by).....

3=(% Almost the same).....

24. Does your firm have the following employment practices/policies? Answer by Managerial/supervisory employees (MS) and other employees (Non-MS)

24a. Self-directed teams (which have some degree of responsibility and discretion over such decisions as methods of work, task schedules, assignment of members to different tasks, and feedback about group performance):

For MS:

- 1=Yes
- 2= No

For Non-MS:

- 1=Yes
- 2=No

24b. Problem-solving groups or quality circles (quality programs where employees are involved in problem solving)

For MS:

- 1=Yes
- 2= No

For Non-MS:

- 1=Yes
- 2=No

24c. Job rotation and cross training:

For MS:

- 1=Yes
- 2= No

For Non-MS:

- 1=Yes
- 2=No

24d. Employee stock ownership plans:

For MS:

- 1=Yes
- 2= No

For Non-MS:

- 1=Yes
- 2=No

24e. Stock option plans:

For MS:

- 1=Yes
- 2= No

For Non-MS:

- 1=Yes
- 2=No

24f. Profit sharing or performance-based group incentive pay:

For MS:

- 1=Yes
- 2= No

For Non-MS:

- 1=Yes
- 2=No

Thank You

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