

COMPLIANCE OF CORPORATE GOVERNANCE IN BANGLADESH

A Dissertation

By

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MAGD Program**

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October 29, 2009

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Approved as to Style and Content by

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**Institute of Governance Studies (IGS)
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October 29, 2009

Statement of the Candidate

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October 29, 2009
Prof. Dr. Iftekhar Ghani Chowdhury
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Subject: Letter of Transmittal.

Dear Sir:

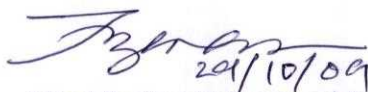
Here is the Thesis Paper on "Compliance of Corporate Governance in Bangladesh" that is a partial requirement of Master's of Arts in Governance and Development (MAGD) Program in BRAC University.

The Code of Corporate Governance for Bangladesh was first prepared and published in March, 2004 by the Taskforce on Corporate Governance with the support from BEI and Department for International Development (DFID). Later on, Securities and Exchange Commission (SEC), Bangladesh issued corporate governance notification on February, 2006. The Code and notification are organized into sections by specific topics (Role of Shareholders, Board Issues, etc.). Within each section, a number of Principles and Guidelines has been set out. Each Principle explains the underlying value of corporate governance practices. This paper tries to reveal the overall levels of compliance of Principles and Guidelines of Corporate Governance prescribed in the Code by the Public Limited Companies, Financial Institutions, and Banks.

I have had practical exposure on different components of corporate governance while working on the thesis paper. Writing this paper has been extremely helpful for me in blending academic knowledge with the existing practices of corporate governance.

I sincerely appreciate the wonderful opportunity given to me to work under your supervision. I will certainly be delighted in meeting your queries if there are any regarding the paper.

Thanking you'



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Abstract

Corporate Governance (CG) is a growing and newer concept in the context of Bangladesh Economy. It is important to know the levels of compliance of the Code of Corporate Governance regarding the Principles and Guidelines in Bangladesh. This paper tries to reveal the existing level of compliance of corporate governance in three sectors i.e., Public Limited Companies (PLCs), Financial Institutions (FIs), and Banks of Bangladesh. This study focused on five specific aspects of corporate governance e.g., ownership and control structure of the company, shareholders' right and disclosure of information, public disclosure and transparency, effectiveness of the board and performance of various committees. These aspects and sub-categories reveal the basic information regarding the current status of the compliance of the Code of Corporate Governance, SEC notification, Bangladesh Bank circulars. In the case of disclosure and transparency banks and Financial Institutions (FIs) are doing better than the PLCs. The latter should develop and promote the culture of disclosure to public in more effective manners. Chief Executive Officers (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, FIs and banks are doing better than the PLCs. In case of banks depositors' directors have significant influence in the decision making process of the board. It is therefore concluded that the spirit of appointing independent and depositors' directors should be taken seriously and individual with expertise and reputation should be appointed as independent directors. Except audit committee other committees like compensation committee, and nomination committee rarely exists or effectively operates in Bangladesh's PLCs. In some FIs and banks all the three committees are in existence. Although audit committees were present in all three sectors, their effectiveness is questionable, especially in PLCs.

It can be logically deduce that corporate culture in Bangladesh is still in a growing stage. While legal requirements for good corporate governance have been created, rushing to institutionalize the culture of governance through legal and regulatory requirements or through external pressures may raise problem rather than any good to the culture. Corporate Governance is a journey, not a destination and the Code and notification have provided guidance for beginning that journey for Bangladesh.

List of Abbreviations used

BB	: Bangladesh Bank
BEI	: Bangladesh Enterprise Institute
CEO	: Chief Executive Officer
CFO	: Chief Financial Officer
CG	: Corporate Governance
CSE	: Chittagong Stock Exchange
DCCI	: Dhaka Chamber of Commerce and Industries
DFID	: Department For International Development
DSE	: Dhaka Stock Exchange
FI	: Financial Institutions
NGO	: Non-Government Organization
OECD	: Organization for Economic Co-operation and Development
PLC	: Public Limited Companies
SEC	: Securities and Exchange Commission
SOE	: State-Owned Enterprise

COMPLIANCE OF CORPORATE GOVERNANCE IN BANGLADESH

1.0 INTRODUCTION

1.1. Introduction

Corporate Governance (CG) is a growing and newer concept in the context of Bangladesh Economy. Corporate governance refers to the business practices of corporate houses which make them more transparent and accountable to their stakeholders. There are different stakeholders of a business entity e.g. shareholders, board of directors, management, staffs and workers, and consumer groups. Each of these stakeholders has different point of view and interest toward the objectives, missions and visions of the business. Moreover, government regulatory bodies have industry specific rules and regulations which businesses have to comply with.

A lack of practice of good governance in companies and business organizations may lead to poor accountability, lack of transparency which ultimately limits the trustworthiness of companies. World has recently observed various corporate scandals like Enron, Daewoo, WorldCom etc. which seriously compels the different stakeholders to think about the practice of corporate governance. These corporate scandals can be observed not only in western countries, it can also be found here in Bangladesh. Recently, a Bangladeshi financial institution named 'Al – Baraka Bank' went into bankruptcy which caused thousands of depositors' loss of valuable deposits.

"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.¹"

¹ (Cadbury, 2000)

Though the concept of corporate governance is nothing new in the western countries, it is comparatively newer in Bangladesh as it may be a good way to create good image for the business entity. In August 2003, Bangladesh Enterprise Institute (BEI) invited a number of prominent individuals from the private sector, the government, NGOs, and other relevant bodies to begin the process of formulating a Code of Corporate Governance for Bangladesh. Convening this Taskforce on Corporate Governance was an outcome of BEI's ongoing research and advocacy work on strengthening corporate governance in Bangladesh. Finally, the Code of Corporate Governance for Bangladesh was prepared and published in March, 2004 by the Taskforce on Corporate Governance with the support from BEI and Department for International Development (DFID).

The Code of Corporate Governance prescribes the principles, procedures and process through which better corporate governance practices may gradually be introduced in the private sector, financial institutions, State Owned Enterprises (SOEs) and Non – Governmental Organizations (NGOs). As such, the Code is organized into Principles and Guidelines. Organizations can start on the path to better corporate governance first by acknowledging the Principles of Corporate Governance and then by incorporating them through initial implementation strategies, which they must justify and explain. The next step would be to comply fully with the Guidelines for implementation, as set out in the Code, which represent an appropriate synthesis of international and indigenous best practices that are wholly applicable to the Bangladeshi context.

Finally, Securities and Exchange Commission (SEC), Bangladesh published a notification which requires all the Banks, Financial Institutions (FIs), and Public Limited Companies (PLCs) comply with the conditions stated in the notification on January 9, 2006. However, these conditions are imposed on 'comply or explain' basis. The companies listed with any stock exchange in Bangladesh should comply with these conditions or explain the reasons for non-compliance in accordance with the condition No.5². There is direction setup by Bangladesh Bank for all Banks and FIs to comply with some certain conditions.³

² See Appendix C for conditions stated in the notification.

³ See Appendix C for conditions stated in the notification.

1.2 Statement of the Problem

It is important to know the levels of compliance of Corporate Governance regarding the Principles and Guidelines in Bangladesh. The specific question pertinent to diagnosis the practices of Corporate Governance may be:

- Whether the existing practices of corporate governance are satisfactory enough to comply with the Principles and Guidelines prescribed in the Code of Corporate Governance, notification of SEC and directions of Bangladesh Bank.

1.3 Objectives of the Study

The study tries to reveal the levels of compliance of Corporate Governance in Public Limited Companies, Financial Institutions (FIs) and Banks in Bangladesh. So, the objectives of the study are:

1. To identify the levels of accountability to the stakeholders i.e., Shareholders, Boards, Managements by complying with the Principles and Guidelines prescribed in different circulars and orders.
2. To identify the levels of transparency in disseminating information to the stakeholders by complying with the Principles and Guidelines.
3. To measure the overall level of compliance of the Principles and Guidelines.

1.4 Significance of the Study

There are numerous potential benefits and rewards for Bangladesh by improving corporate governance practices. The primary and most important benefit from implementing guidelines of corporate governance may be in achieving and sustaining development goals. Strengthening corporate governance can lead to a process of revitalization of the Bangladesh economy. If the code can be fully implemented in Public Limited Companies (PLCs), Financial Institutions (FIs), public corporations, joint stock companies, state-owned enterprise (SOEs), and Non-Governmental Organizations (NGOs), the reputation of Bangladesh for investment and aid will be greatly enhanced. Preparing and complying with a Code of Corporate Governance in national level sends a message to investors and observers that Bangladesh has recognized the importance of it and is taking definite steps to improve its governance performance. As such, implementation of a program of corporate governance can make significant contributions to economic growth.

1.5 Definition of the Concepts

Statement of the Problem:

- The existing practices of corporate governance are satisfactory enough to comply with the Principles and Guidelines prescribed in the Code of Corporate Governance, notification of SEC and directions of Bangladesh Bank.

The particular concepts or issues of the problem statement can be defined as follows:

Existing practices: means the current practices of Corporate Governance (CG) adopted by the PLCs, FIs, and banks in Bangladesh in the Year 2009.

Corporate Governance: The definition of the CG that is pertinent has been taken from the definition given by Organization for Economic Co-operation and Development (OECD) in April 1999 (1992, page 15)

Corporate governance is the system by which business corporations are directed and controlled. The corporate governance structure specifies the distribution of rights and responsibilities among different participants in the corporation, such as, the board, managers, shareholders and other stakeholders, and spells out the rules and procedures for making decisions on corporate affairs. By doing this, it also provides the structure through which the company objectives are set, and the means of attaining those objectives and monitoring performance.

Satisfactory enough: means whether the practices of CG in organizations meet the requirement prescribed in the Code, SEC notification and BB directions for Corporate Governance.

Comply with the Principles and Guidelines: whether the practices of CG in organizations act in accordance with the Principles and Guidelines prescribed in the Code, SEC notification and BB directions for corporate governance.

Principles and Guidelines: Principles and Guidelines prescribed in the Code of Corporate Governance for Bangladesh, March 2004.

Code of Corporate Governance: Code of Corporate Governance for Bangladesh published in March, 2004 by the Taskforce on Corporate Governance with the support from BEI and Department for International Development (DFID).

SEC Notification: Notification on corporate governance by Securities and Exchange Commission (SEC), Bangladesh, February 20, 2006.

Bangladesh Bank Directions: Different Bangladesh Bank circular on Corporate Governance like: BRPD Circular No. 16 dated July 24, 2003.

Financial Institution: According to the Financial Institutions Act, 1993 it means such non-banking financial institutions, which-

- make loans and advances for industries, commerce, agriculture or building construction; or
- carry out the business of underwriting, receiving, investing and reinvesting shares, stocks, bonds, debentures issued by the Government or any statutory organization or stocks or securities or other marketable securities; or
- carry out installment transactions including the lease of machinery and equipments; or
- finance venture capital; and
- shall include merchant banks, investment companies, mutual associations, mutual companies, leasing companies or building societies;

Banking Company⁴: means any company transacting the business of banking in Bangladesh, and includes all new banks and special banks;

Explanation: Any company which is mainly engaged in the manufacture of goods or carries on any trade and which accepts deposits of money from the public merely for the purpose of financing its business as such manufacturer or trader shall not be deemed to transact the business of banking within the meaning of this clause.

Banking: means the accepting, for the purpose of lending or investment, of deposits of money from the public, repayable on demand or otherwise, and withdrawable by cheque, draft, order or otherwise;

⁴ According to the Banking Companies Act, 1991

2.0 LITERATURE REVIEW

The major function of the Code of Corporate Governance for Bangladesh is to improve the general quality of corporate governance practices. The Code does this by defining best practices of corporate governance and specific steps that organizations can take to improve corporate governance. The Code focuses more stringent practices than is required by Bangladeshi law such as Banking Companies Act, 1991 and Financial Institutions Act, 1993 in some areas to raise the quality and level of corporate governance because these additional requirements are in line with the international best practices. Even if small organizations do not feel they can meet all the requirements immediately, the Code provides a standard that can be used to measure progress towards the goal of best practices.

Many of the best organizations in Bangladesh already have practices and procedures in keeping with the provisions of the corporate governance. However, the Code/Notification is also a mechanism to disseminate these best practices to all organizations nationwide. Moreover, the best corporate governance practices, as suggested in the Code/Notification, can improve overall accountability and performance throughout the private sector as well as the NGO and SOE sectors. The spirit of these requirements seeks to enable organizations to grow and attract greater investment, rather than being a hindrance to growth.

It may take a number of years for the full compliance of the Code/Notification and will require the cooperation of a vast number of relevant stakeholders. Some of the Code's Principles, Guidelines, and provisions can be incorporated into the decision-making process of key institutions and in framing new policies immediately. Companies that demonstrate sound corporate governance practices should be given incentives and rewards by the government, Securities and Exchange Commission (SEC), and Bangladesh Bank.

The Code is organized into sections on specific topics (Role of Shareholders, Board Issues, etc.). Within each section, the Code sets out a number of Principles and Guidelines. Each Principle explains the underlying value or tenant of corporate governance practices. These Principles of Corporate Governance may be applied in different organizations by different methods. Thus, while the Guidelines suggest

specific methods for application, the Code as a whole allows for each organization to apply the Principles in their own way. Organizations solely implementing the Corporate Governance Principles by their own method, nevertheless, should provide explanations to shareholders and the public as to how exactly these are applied in their practices, policies, regulations and procedures. To fully comply with the Code, however, organizations should implement both the Principles and Guidelines.

2.1 Definition of Corporate Governance

The study now discusses literature written by different authors. This paper starts by discussing definitions of Corporate Governance as per the views of the different authors. The report further tackles the relationship or partnership between a public and a private sector.

Sir Adrian Cadbury (1992) defined Corporate Governance as

It is the system by which companies are directed and controlled. Boards of directors are responsible for the governance of their companies. The shareholders' role in governance is to appoint the directors and the auditors and to satisfy themselves that an appropriate governance structure is in place. The responsibilities of the board include setting the company's strategic aims, providing the leadership to put them into effect, supervising the management of the business and reporting to shareholders on their stewardship. The board's actions are subject to laws, regulations and the shareholders in general meeting.

Organization for Economic Co-operation and Development (OECD) in April 1999 defined Corporate Governance which was consistent with the one presented by Cadbury (1992, page 15)

Corporate governance is the system by which business corporations are directed and controlled. The corporate governance structure specifies the distribution of rights and responsibilities among different participants in the corporation, such as, the board, managers, shareholders and other stakeholders, and spells out the rules and procedures for making decisions on corporate affairs. By doing this, it also provides the structure through which the company objectives are set, and the means of attaining those objectives and monitoring performance.

Strengthening corporate governance practices can not only benefit individual organizations but also the specific sectors as well as the nation as a whole. Improving corporate governance will improve the overall reputation of Bangladesh as a place to do business. Good corporate governance practices will lead to well-governed, more profitable companies that can attract both foreign and domestic investment.

Corporate governance can lead to higher levels of efficiency, quality, and competitiveness throughout the national economy, which in turn will enable Bangladesh to reach its goals for poverty alleviation.

According to Thomas & Hunger (2004)- Strategic Management and Business Policy: "Corporate Governance refers to exactly to how the company is run and managed". It also deals with the relationship that exists between the shareholders, Board of Directors and top Management in determining the direction and performance of the corporation. This also exists to ensure survival of the corporation and meet its set objectives. The primary objective is to maximize shareholders wealth. It deals with how each of the three (3) groups (shareholders, Board of Directors and top management) can work at its best and harmoniously.

Tricker (1984) states that "if management is about running business, corporate governance is about seeing that it is run properly. All companies need governing as well as managing. Ira Millstein also states that "an effective system of corporate governance must strive to channel the self interest of managers, directors and the advisors upon whom they rely into alignment with the corporate, shareholder and public interest".

King Code 2002 states that: Corporate governance advocate an integrated approach to good practice in the interest of a wide range of stake holders and fundamental principles of good financial, social, ethical and environmental imperatives.

Yet distinction has to be made between accountability and responsibility. One is liable to render an account when one is accountable and one liable be called to account when one is responsible. In governance terms one is accountable at

common law and by statute to the company if one is a director and one is responsible to the stake holders identified as relevant to the business of the company'

The stakeholders' concept of being accountable to all must be rejected for the simple reason that to ask boards to be accountable to everyone would result in being accountable to no one. The modern approach is for the board to identify the company's stakeholders, including its shareholders and to agree as to how the relationship with other stake holders should advance and managed in the interest of the company.

In decades past if people had gathered in order to establish a company to produce goods they would have applied to a regulation for a license , hired premises ,bought plants and proceeded to manufacture without much regard to the impact on the environmental , social or the interests of other stakeholders. The permission from the regulators to manufacture goods would have been the license to operate.

The done, the license to operate a company is much more complex. Boards have to consider not to online the regulatory aspect, but also industry and market standards, industry reputation, the media and the attitudes of customers, suppliers, consumers, employees, investors and communities (local), national and international ethical pressure groups, public opinion, public confidence, political opinion etc.

The inclusive approach recognizes that stakeholders such as the community in which the company operates, its customers, its employees and its suppliers need to be considered when developing the strategy of a company. This relationship between a company and its stakeholders is either contractual or non-contractual.

The inclusive approach requires that the purpose of the company should be defined , and the values by which the company will carry its daily life should be identified and communicated to all its stakeholders .The stakeholders relevant to like company business should also be identified .This three factors must be combined in developing strategies to achieve the company goals. The relationship between the company and its stakeholders must be mutual beneficial. A wealth of evidence has established that

this inclusive approach is the way to create sustained business success and steady, long term growth in the shareholder's value.

The key challenge for good corporate citizenship is to seek an appropriate balance between the enterprise (performance) and the consultants (conformable) which takes into account the expectations of the share owners for reasonable capital growth and the responsibility concerning the company . This is probably best encapsulated in the statement attributed to the president of the World Bank , Jim Wolfensohn , in which he stated that "the proper governance of company's will become as crucial to the world economy as the proper governing of countries" . Proper governance embraces both conformance and performance. Conforming to corporate governance standards results in constraints on management. Boards have to balance this with performance for financial success and the sustainability of the company business. Tomorrow's company's, the world have developed a concept of three corporate sins namely;

According to King (2002), Good Governance is regarded as constituting the seven characteristics outlined below:

- **Discipline** - Corporate discipline is a commitment by a company's senior management to adhere to behavior that is universally recognized and accepted to be correct and proper. This encompasses a company's awareness of and commitment to, the underlying principles of good governance, particularly at senior management level.
- **Transparency** - Transparency is the ease with which outsider is able to make meaningful analysis of a company's actions, its economic fundamentals and the non financial aspects pertinent to that business. This is a measure of how good management is at making necessary information available in a candid, accurate and timely manner – not only the audit data but also general reports and press releases. It reflects whether or not investors obtain a true picture of what is happening inside the company.

- **Independence** – Independence is the extent to which mechanisms have been put in place to minimize or avoid potential conflicts of interest that may exist, such as dominance by a strong chief executive or large shareowner. These mechanisms range from the composition of the board, to appointments to committees of the board and external parties such as the auditors. The decisions made, and internal processes established, should be objective and not allow for undue influences.
- **Accountability** – Individuals or groups in a company, who make decisions and take actions on specific issues, need to be accountable for their decisions and actions. Mechanisms must exist and be effective to allow accountability. These provide investors with the means to query and assess the actions of the board and committees.
- **Responsibility** – with regard to management, responsibility pertains to behavior that allows for corrective action and for penalizing mismanagement. Responsible management would, when necessary, put in place what it would take to set the company on the right path. While the board is accountable to the company, it must act responsively to and with responsibility towards all stakeholders of the company.
- **Fairness** – the systems that exist within the company must be balanced in taking into account all those that have an interest in the company and its future. The rights of various groups have to be acknowledged and respected. For example, minority shareowner interests must receive equal consideration to those of the dominant shareowners.
- **Social Responsibility** - a well-managed company will be aware of and respond to social issues, placing a high priority on ethical standards. A good governance citizen is increasingly seen as one that is non-disciplinary, non-exploitative and responsible with regard to environmental and human rights issues. A company is likely to experience indirect economic benefits such as improved productivity and corporate reputation by taking those factors into consideration.

If there is lack of good corporate governance in a market, capital will leave that market with the click of a mouse. As Arthur Levitt, the former chairperson of the US Securities and Exchange Commission has said "If a country does not have a reputation for strong corporate governance practices, capital will flow elsewhere. If investors are not confident with the level of disclosure, capital will flow elsewhere. If a country opts for lax accounting and reporting standards, capital will flow elsewhere. All enterprises in that country – regardless of how steadfast a particular company's practices may be – suffer the consequences. Markets must now honor what they perhaps, too often, have failed to recognize. Markets exist by the grace of investors. And it is today's more empowered investors that will determine which companies and which markets will stand the test of time and endure the weight of greater competition. It serves us well to remember that no market has a divine right to investor's capital.

There is a move from the single to the triple-bottom line, which embraces the economic, environmental and social aspects of a company's activities:

- ❖ Shareowners obtain their power from the democratic process of voting by which means they can elect or dismiss directors, who carry out the objectives of the company.
- ❖ The relationship between the company and the shareowners arises out of the articles of association, which are nothing more than a contract between them. This is the only means of shareowner protection, which is quite ineffective in practice. Because the shareowners have little or no protection, the quality of governance is of absolute importance to them.

Also corporate governance is essentially about leadership:

- Leadership for efficiency in order for companies to compete effectively in the global economy and thereby create jobs
- Leadership for probity because investors require confidence and assurance that the management of a company will behave honestly and with integrity in regard to their shareowners.

- Leadership with responsibility as companies are increasingly called upon to address legitimate social concerns relating to their activities and
- Leadership that is both transparent and accountable because otherwise business leaders cannot be trusted and this will lead to the decline of companies and the ultimate demise of a country's economy.

2.1.1 Ethics and Corporate Governance

A company's ethics refer to the principles, norms and standards that it promotes for the guidance and conduct of its activities internal relations and interactions with external stakeholders, in accordance with its corporate values. King Code (2002) states that each company should demonstrate its commitment to organizational integrity by codifying its standards of ethical behavior in a code of ethics. Commitment to the code of ethics will be demonstrated by:

- Creating systems and procedures to introduce, monitor and enforce its code of ethics
- Assigning high-level individuals to oversee compliance with the code of ethics
- Assessing the integrity of new appointees in selection and promotion procedures
- Exercising due care in delegating discretionary authority
- Communicating with and auditing safe systems for reporting of unethical or risky behavior
- Enforcing appropriate discipline with consistency and
- Responding to offences and preventing re-occurrence

Iskander (2000) defines corporate governance as a means of ensuring that a business is run well and that investors receive a fair return. It is about giving overall direction to management and ensuring accountability to shareholders, other external providers of funds and stakeholders. Corporate Governance should not be confused with management, which is concerned with day to day running of business (production, procurement, marketing, finance and personnel).

In a proprietary firm the owner-managers efforts are directed at maximizing the firm's value because this maximizes the owner-managers income as well. The relationship becomes complicated when corporations are owned by multiple

shareholders (principals) but run by managers (agents). The need for corporate governance arises from the potential divergence of interests between those who have control over a firm and those who provide its external financing. This divergence can be described as a principal agent problem (commonly known as agency costs) it is a function of the separation of ownership and control over the corporation will find it risky and costly to protect themselves from opportunistic behavior by managers or controlling shareholders.

In a broad sense the need for corporate governance arises when public and private sectors returns diverge. Unless meaningful protections are in place for external capital providers, those who control the corporation can use their position to misappropriate economic benefits, often at the expense of the long term performance and value of the enterprise. Where poor corporate governance is the norm, the repercussions extend beyond underperformance in a single corporation to include the corporate sector and they extend the great vulnerability in the financial system since it is hard for local capital providers (banks and institutional providers) to assess risk adequately. Lack of meaningful protection for capital providers is likely to reduce the availability of finance on favorable terms and affect the overall efficiency of the economy. As such Madgi. I. Iskander combination of laws, procedures, regulations, voluntary practices and implicit rules that enable the corporation to attract financial and human capital, perform efficiently and maximize long term value for shareholders while respecting the interests of stakeholders and society.

Just what constitutes corporate governance is still a topic of debate.

2.1.2 Corporate Governance from a private and public sector Perspective –

- From a corporation's perspective, the emerging consensus is that corporate governance is about maximizing the values, in the long run subject to meeting financial and other legal and contractual obligations. This broader and more inclusive definition stresses that achieving long-term sustained value to shareholders requires balancing the interests of shareholders and financiers with

those of other stakeholders – employees, customers, suppliers, investors and communities.

- From a public policy perspectives, corporate governance is about nurturing enterprises while ensuring accountability in the exercise of power and patronage by firms. The central role of public policy is to provide the firm with the incentives and discipline to minimize the divergence between private and social ventures and to protect the interest of stakeholders.

2.2 Corporate Governance of PLCs in Bangladesh

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 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 the 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.⁵

The board size should be optimal with diverse expertise and experience to ensure a well functioning and involved board. BEI guidelines states 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. In order to enhance corporate governance in the interest of investors and the capital market, SEC imposes some further conditions to the companies listed with any stock exchange in Bangladesh.⁶ These conditions are imposed on '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 propose by SEC is not be less than 5 and not more than 20.

Cadbury report, Sarbanes-Oxely Act, BEI, SEC and other major works on CG also emphasizes on the importance of independent directors in the board. All companies should encourage effective representation of independent directors on their Board of

⁵ The Code of Corporate Governance for Bangladesh, March 2004, BEI

⁶ SEC notification, dated 20th February 2006

Directors so that the Board, as a group, includes participation 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.

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

- The position of the Chairman of the Board and the CEO should be distinct and 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 subcommittee 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.

2.3 Corporate Governance of Banks and FIs in Bangladesh

Financial Institutions (FIs) especially, Banks pose unique corporate governance requirement 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 executives can 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 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 is the depositors' savings that the banks 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 (Shleifer 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 sum up depositors as well as shareholders. 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 sufficient motivation to monitor the banks as they do not have much at stake in case of bank failures (Macey and Garrett, 1988).

2.4 Corporate Governance Directions of Bangladesh Bank (BB)

Liquidity and solvency problems caused by poor governance in banks can have harmful systemic consequences in the broader economy reliant on banks for credit and payment services. High priority is therefore accorded to ensure corporate governance in banks, putting in place checks and balances comprising a mix of legal, regulatory and institutional provisions specifying the roles and accountabilities of the board, the executive management, external and internal audit, disclosure and transparency prescriptions. Corporate governance is a sine-qua-non for a sound financial system in private commercial banks. Good corporate governance can contribute substantially to a shared working environment between banks and its supervisors. It supports not only a well managed banking system but also necessary to protect depositors' interest. BB has taken several measures in recent times to put in place good corporate governance in banks. These include-regulation limiting the tenure of directors not more than six years at a stretch; reduction in the size of bank boards to a maximum of thirteen directors; appointment of two independent directors by BB; fit and proper test for appointment of board members and chief executive officers of Private Commercial Banks (PCBs); constitution of audit committee of board and enhanced disclosure requirements etc.⁷ In continuation of the above reforms, the roles and functions of the Board and Management were redefined and clarified with a view to specifying the powers of the management and restricting the intervention of directors in day to day management of the bank.

2.4.1 Corporate Governance in Banks and Financial Institutions (FIs)

Corporate Governance is the system of internal controls and procedures used to define and protect the rights and responsibilities of various stakeholders. In recent years, with the increase of failure of large corporations due to poor corporate governance the issue has come to the front and many organizations pronounce the guidelines intended to protect the rights of various stakeholders that will reduce the conflict of interests among them. Banks and FIs are "special" as they do not only accept and deploy large amount of uncollateralized public funds in fiduciary capacity, but also leverage such funds through credit creation. The depositors, particularly retail depositors, cannot effectively protect themselves as they do not have adequate information, nor are they in a position to coordinate with each other. It is believed

⁷ Bangladesh Bank Annual Report, 2008.

that there could be a contagion effect resulting from the instability of one bank, which would affect a class of banks or even the entire financial system and the economy. As one bank becomes unstable, there may be a heightened perception of risk among depositors for the entire class of such banks, resulting in a run on the deposits and putting the entire financial system in jeopardy.

The crisis of an individual bank may cause to create problem for entire financial system as well as the monetary management of the country. So, there should have clear and defined duties and responsibilities for the management and the board that act as the fiduciary for shareholders and the depositors. In view of the above, Bangladesh Bank is deploying continuous effort by inserting appropriate provisions in the Banking Companies Act, 1991 and Financial Institutions Act, 1993, supplemented by prudential regulations/guidelines in line with international best practices. The existing legal framework and significant current practices in particular cover the following aspects:

2.4.1.1 The Board of Directors Composition, Terms, Qualification: The maximum number of the Directors of the Board of banks and Financial Institutions (FIs) would be 13 and 11 respectively. Tenure of a Director of a bank would be 3 years extendable to another one term i.e. a Director can continue his/her office for six years at a stretch. A recess of one term is required after completion of six years as a Director. For FIs the tenure of a Director is 3 years and is renewable. Not more than 10 percent of the shares of a bank will be held by the members of a family. Not more than two member of a family will become Director of a bank in case of holding of more than 5 percent share of the Bank by that family and one member in case of holding of up to 5 percent share. Maximum voting right of any shareholder is restricted to 5 percent of total voting rights of all shareholders of the bank. On the other hand, maximum limit of holding shares of an FI by a single person/family/institution is 20 percent for domestic shareholders and 25 percent for joint venture. To be appointed a Director of a Bank or FI one requires to pass the 'fit and proper test' criteria: s/he has to hold qualifying amount of shares and not to be a minor or undercharged insolvent or mentally unsound with no record of criminal conviction or adverse judicial comment in any civil or criminal proceeding, no record of penalization by any authority for regulatory breach and, no loan default. In addition, the Director of a Bank requires having at least ten years of business or

professional experience. No employee/executive, except CEO, would be appointed as the Director of any Bank/FI.

2.4.1.2 Appointment of Directors from Depositors: For ensuring good governance in Banks, Banks are required to appoint 2 Directors from the depositors who will be in addition to 13 (thirteen) directors mentioned in the sub-clause 15(6) of Banking Companies Act, 1991. "Fit and proper test" criteria stated above, are applicable for appointing Directors from depositors. In addition, such Director should be a depositor of the bank company must at least have a bachelor degree from any recognized university, shall not be a director, officer/staff or advisor of any bank company, financial institution, insurance company or stock exchange, he, including his family members shall not hold more than 1% shares of the paid up capital of the bank, shall not be a salaried staff of the bank, shall not be involved with any political party, shall not be a loan/tax/bill defaulter. Removal of Directors and Vacation of Office: A Bank/FI by extra ordinary resolution can remove any Director. Failure to attend in the three consecutive Board meetings without approval of leave of absence, become default of loan of any bank or FI and failure to repay the entire defaulted loan within two months of receiving the notice, submission of false declaration at the time of appointment and loss of qualification will cause to vacate the office of a Director.

2.4.1.3 Responsibilities and Authorities of the Board of Directors: The major responsibilities and authorities of the Board of Directors are described in brief⁸:

- (a) Work-planning and Strategic Management
- (b) Lending and Risk Management
- (c) Internal Control Management
- (d) Human Resources Management and Development
- (e) Financial Management
- (f) Formation of Supporting Committees
- (g) Appointment of CEO

2.4.1.5 Responsibilities of the Chairman of the Board of Directors: As the Chairman of the Board of Directors (or Chairman of any Committee formed by the Board or any Director) does not personally possess the jurisdiction to apply

⁸ See Appendix D for detailed discussion.

policymaking or executive authority, he shall not participate in or interfere into the administrative or operational and routine affairs of the bank. The Chairman may conduct on-site inspection of any bank-branch or financing activities under the purview of the oversight responsibilities of the Board. He may call for any information relating to bank's operation or ask for investigation into any such affairs; he may submit such information or investigation report to the meeting of the Board or the Executive Committee and if deemed necessary, with the approval of the Board, s/he shall effect necessary action thereon in accordance with the set rules through the CEO. However, any complaint against the CEO shall have to be apprised to Bangladesh Bank through the Board along with the statement of the CEO.

2.4.1.6 Role of the Audit Committee: The Audit Committee of Board of Directors will assist the Board in fulfilling its oversight responsibilities including implementation of the objectives, strategies and overall business plans set by the Board for effective functioning of the bank. The Committee will review the financial reporting process, the system of internal control and management of financial risks, the audit process, and the bank's process for monitoring compliance with laws and regulations and its own code of business conduct.

2.4.1.7 The Chief Executive Officer (CEO) Appointment : To be appointed as chief executive of a banking company, an individual must possess at least 15 years of banking experience with at least 2 years in the level next below the chief executive and must meet the other stipulations mentioned above for Directors, except qualifying shares. The minimum experience of the CEO in the case of FI is 12 years and experience of 2 years in the post of next below the CEO is not required. Maximum age limit of CEO of Banks is 65 years.

2.4.1.8 Disclosure Requirements: Banks/FIs are required to prepare their financial statements comprising of balance sheet, profit and loss account, cash flow statement, statement of changes in equity, liquidity statement and other explanatory notes in accordance with International Accounting Standard (IAS). Copies of financial statements should be preserved in each of the bank branches, so that the customers of the bank may readily use those on request. Besides, balance sheet should be affixed in a visible place of each bank branch. The financial statements should be published in widely circulated one Bengali and one English daily newspaper within

one week of submission of the statements to Bangladesh Bank so that the stakeholders of the bank including its depositors, shareholders and regulatory bodies can get information about the bank easily. These should also be disclosed in the bank's website.

2.4.1.9 Other Issues: Lending to the Director of own bank/FI is restricted up to 50 percent of the paid-up capital of such Director. Banks are not allowed to appoint Consultants for routine works that can be performed by the regular staff. The Consultants should have specific terms of references (ToR). No past Chairman, Director, Adviser, Chief Executive would be appointed as the Consultant of the same bank. No Consultant or Advisor shall participate in decision making process or exercise power regarding the financial, administrative or operational and routine affairs of the bank. With the view to save the interest of the Depositors, Banks are to appoint two Directors from the depositors who will be in addition to 13 Directors from the shareholders. Issuance of comprehensive guideline on maintenance of risk based capital in accordance with the Basel II is under process which would strengthen long term sustainability of banks.

3.0 METHODOLOGY

The study has been conducted on three sectors i.e., Public Limited Companies (PLCs), Financial Institutions (FIs), and Banks to measure the levels of compliance of corporate governance. There are 305 companies which are enlisted in the Securities and Exchange Commission, Bangladesh. Among these companies there are 47 Banks, 39 Insurances, 8 Cement manufacturing companies, 5 Ceramics, 24 Engineering, 33 Food and Allied, 10 Fuel and Power, 26 Pharmaceuticals and some other industries.

The population for measuring the levels of compliance of the Banks and financial institution is 86. And other than the financial institutions there are 219 PLCs that constitute the population for these industries.

3.1 Data Source

The study mainly focused on primary sources for collecting data with extensive literature review and industry specific guidelines and regulations suggested by the SEC, Dhaka Stock Exchange (DSE), Chittagong Stock Exchange (CSE), and Bangladesh Bank.

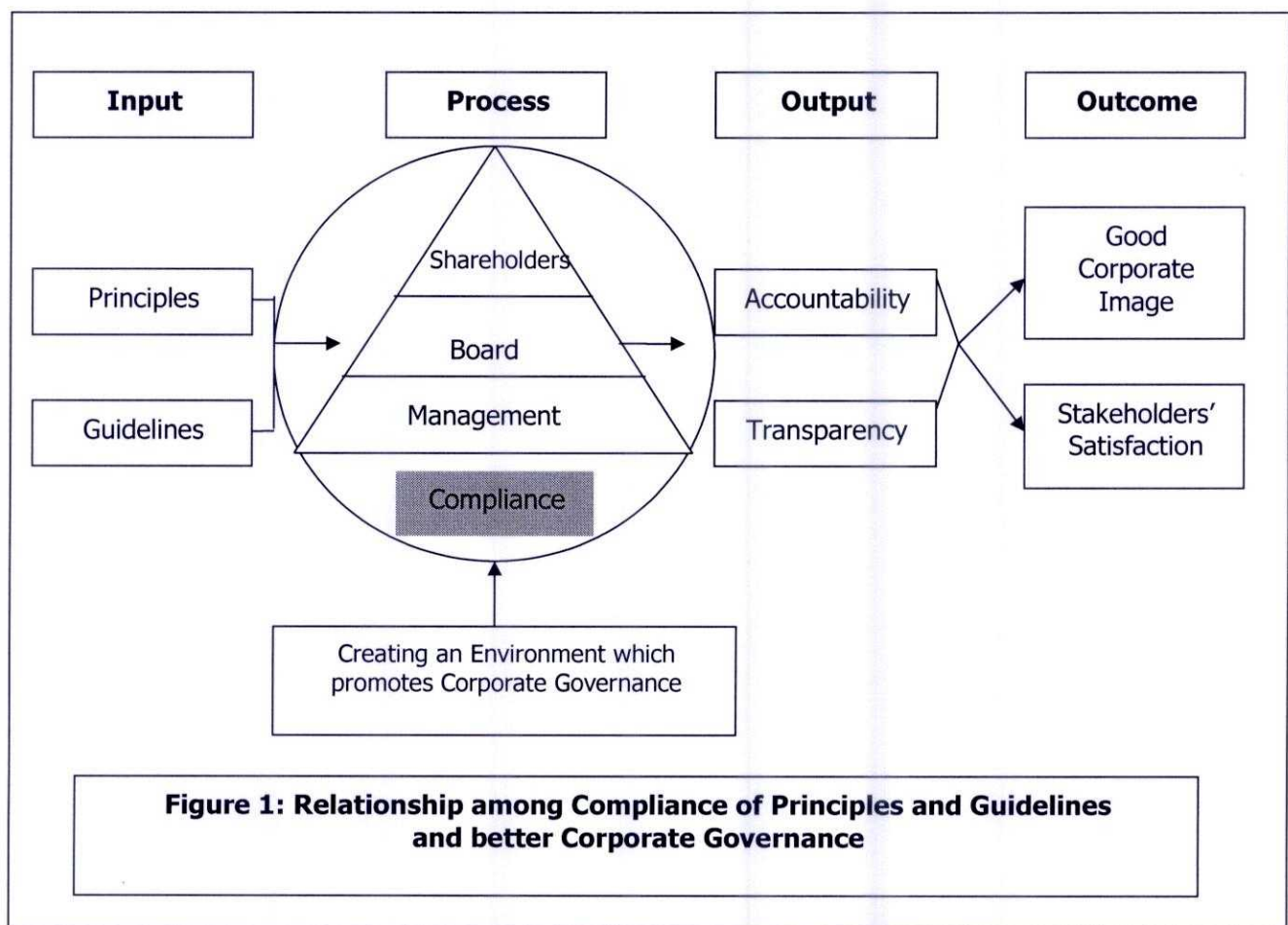
3.2 Study Design

The Code is organized into sections on specific topics i.e., Role of Shareholders, Board Issues, Financial Reporting, Auditing and Non-Financial Disclosure etc. There are a number of Principles and Guidelines within each section which explains the value of corporate governance practices.

Most of the companies in Bangladesh are guided and regulated by the Company Act 1994, government circulars, rules and regulations thorough Ministry of Commerce and Ministry of Industries, SEC, DSE, CSE, Bangladesh Bank. 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 this study, it is supposed that if the Principles and Guidelines are followed properly in corporate houses it will ensure accountability and transparency which will ultimately enhance corporate image and stakeholders' satisfaction. Figure 1 shows the relationship among Compliance of Principles and Guidelines and better Corporate Governance.



3.3 Sample Design

Since there were a few studies conducted in measuring the levels of compliance, it is very difficult to follow a standard sampling technique. Moreover, due to the time constraint the study followed convenience sampling method.

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: Public Limited Companies (PLCs), Financial Institutions (FIs), Banks. 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:

- Transparency to all stakeholders,
- Accountability of the management and the board,
- Fairness in the decision making, and
- 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.

3.4 Sample Size and Instruments

The study has been conducted on 10 PLCs, 5 FIs, and 5 Banks which were selected on Simple Random Sampling method. 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.

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) and SEC also provided assistance through its members so that the companies cooperate with the study. However, even after repetitive assurance some organizations were reluctant to answer all the questions in writing. As a result, information remained incomplete. This has limited the ability of the study to analyze the results using quantitative techniques.

3.5 Data Management and Analysis

Collected data were analyzed by using statistical software i.e., SPSS and Microsoft Excel which deemed appropriate in analyzing such findings.

3.6 Scopes and Limitations

As the study was conducted by following convenience sampling method, it may not truly representative to the whole population. Due to the time constraints it was not be possible to conduct a pilot survey. If a pilot survey were conducted it might have revealed a way to find an appropriate sample.

4.0 FINDINGS OF THE STUDY

The state and nature of corporate governance has been studied under five general headings. Three types of companies were studied:

- Financial institutions (FIs) like insurance companies and leasing firms which are listed in the Dhaka Stock Exchange (DSE), and
- Banks that are listed in the DSE
- Public Limited Companies (PLCs) listed in the DSE but without any government share.

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

4.1 Ownership and Control Structure of the Company

To understand the overall ownership pattern and control structure of the companies, this paper investigated on the following key issues:

- a) Significant voting rights of the largest shareholder,
- b) Control of ownership by large shareholders,
- c) Family control over the business,
- d) Share of the government or foreigners,
- e) Relationship between the CEO and the largest shareholder,

Bangladesh Bank direction for ownership of a company tries to ensure corporate governance in banks and FIs. As per BB regulation not more than 10 per cent of the shares of a bank can be held by the members of a family. Not more than 2 members of a family can become Director of a bank in case of holding of more than 5 per cent share of the Bank by that family and 1 member in case of holding of less than 5 per cent share.⁹

It was found that in almost 90 per cent of the companies, the largest shareholder has significant voting rights and the largest shareholder has an effective and visible control over the company. In 75 per cent cases, the company is controlled by two or more large shareholders. In 40 per cent cases, the respondents believe that there is some family control over business. In 20 per cent cases, government or foreigners

⁹ Bangladesh Bank Annual Report, 2008.

have shares in the ownership of the company. There is no relationship between the CEO and the largest shareholder in more than 80 per cent cases.

4.2 Shareholder Rights and Disclosure of Information

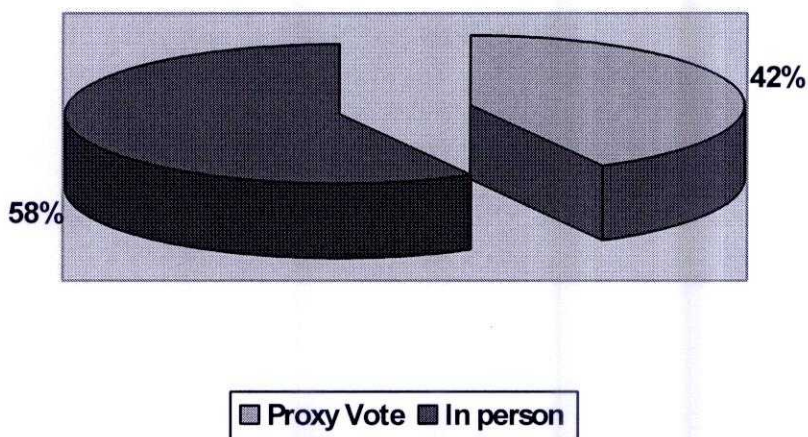
On the issue of shareholders' rights and disclosure, the study investigated several key issues:

- a) Practice of voting in the Annual General Meeting of the companies,
- b) Disclosure of information in terms of knowing the agenda,
- c) Lead time to analyze information,
- d) Information on equity of major shareholders,
- e) Practice of nomination and disclosure of director candidates in the meeting,
- f) Rights of the minority shareholders in nominating candidates, and
- g) Rights of the shareholders in terms of opposing candidates nominated by the management.

4.2.1 Ease of Participation in Voting by Shareholders

Figure 2 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. 42 per cent of the shareholders participated through proxy vote, 58 per cent in person.

Figure 2: Participation in Voting by Shareholders



4.2.2 Knowledge on AGM Agenda, Discussion 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 3 shows that participants realize that knowledge on AGM agenda, discussion and Equity of Shareholders are matters of concern in Bangladesh.

Figure 3: Right to know Agenda, Discussion and Equity of Major Shareholders

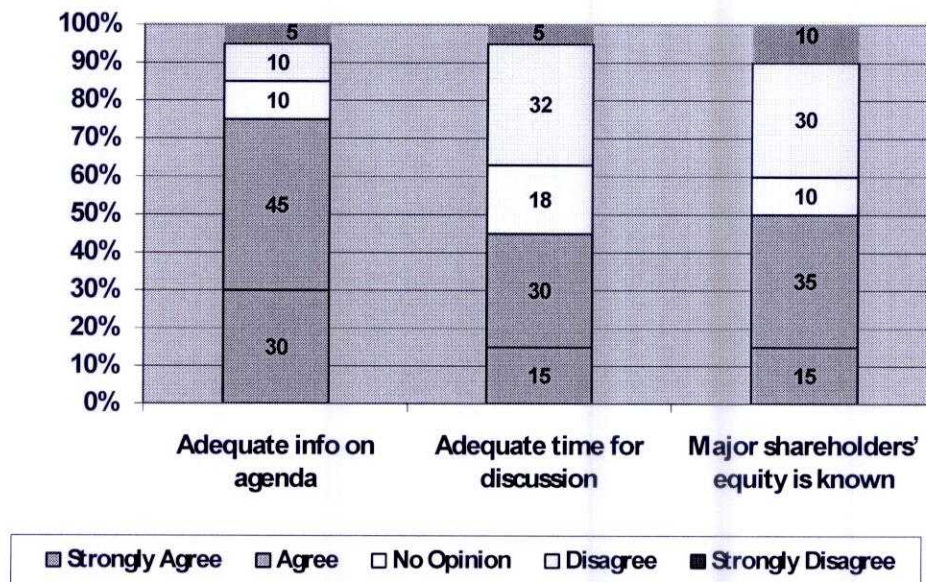


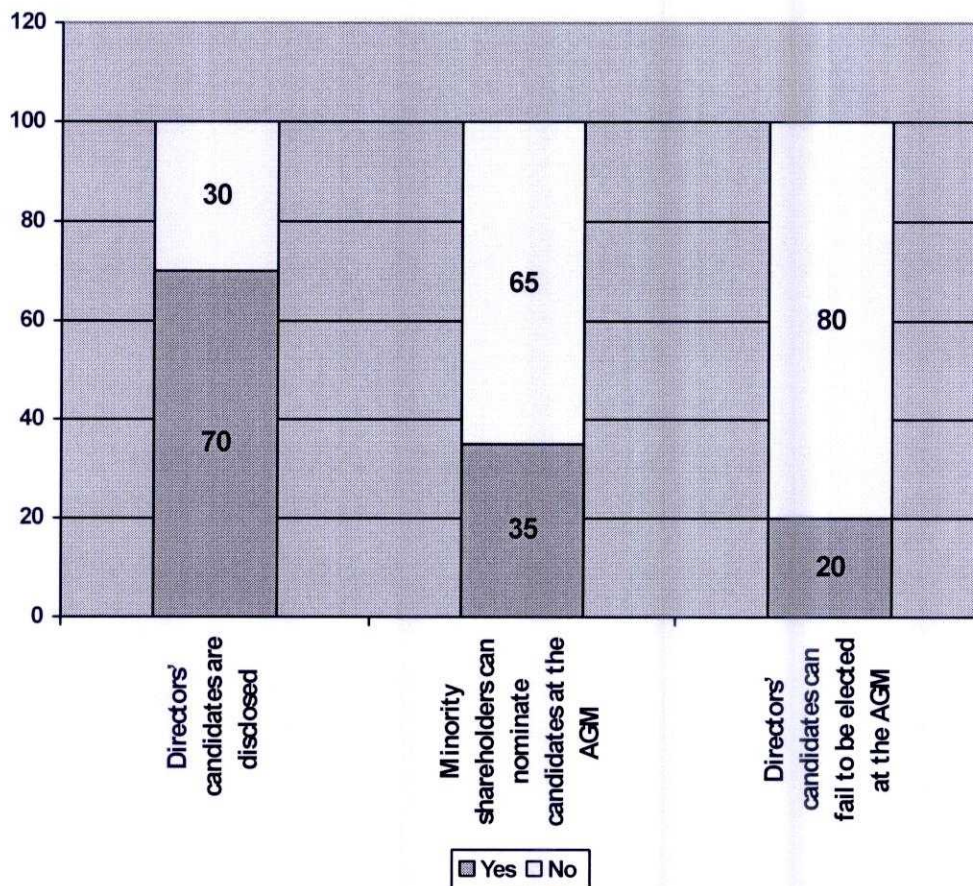
Figure 3 shows that 75 per cent of the respondents mentioned that adequate information on agenda is given before the AGM. The study revealed that only 45 per cent of the respondents told that adequate time is given for discussion in the AGM. It is found that in 40 per cent cases the equity of the major shareholders can be known.

The study revealed that though adequate information is given beforehand the shareholders are not given enough time for discussion which can be a matter of concern.

4.2.3 Nomination of Director's Candidate

Nomination of candidates in the meeting is an important element to ensure transparency in governing the company. Figure 4 show that while a majority of the shareholders knew about the Director's candidate prior to the AGM, however, some 30 per cent 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 35 per cent of the shareholders mentioned that minority shareholders could nominate their candidates. The opportunity for the minority shareholders to be nominated should be increased and it will certainly increase the confidence of the minority shareholders. Only 20 per cent of the respondents described that directors' candidates may fail to be elected at the AGM.

Figure 4: Nominating and Electing Candidates at the AGM



4.2.4 Summary by Three Types of Companies

In terms of three sectors, this study found that FIs and banking companies are more open to their shareholders compared to PLCs. This illustrates that regulatory structure imposed upon FIs and banking companies are more effective than on public limited companies. In other words, regulatory agencies are rather relaxed in implementing such requirements on non – financial public limited companies. The main reason may be the additional stringent and rigorous rules and regulations imposed on the financial institutions by the Bangladesh Bank in addition to those imposed by the SEC and DSE.

4.3 Public Disclosures and Transparency

Public disclosure is an important element of governance in the corporate world because it builds trust, helps bringing 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.

Usually companies disseminate information through the following means which were studied:

WWW	: Company's Website
AR	: Annual Report
RR	: Report to Regulatory Agencies
Media	: Print or Electronic Media
No	: Non Disclosure

Some of the companies use more than one means to disclose information regarding the corporate governance practices. 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 external auditors and consultants,
- v. Policies on risk management,
- vi. Significant changes in the ownership, and
- vii. Corporate governance rules and vision.

Figure 5: Public Disclosures and Transparency

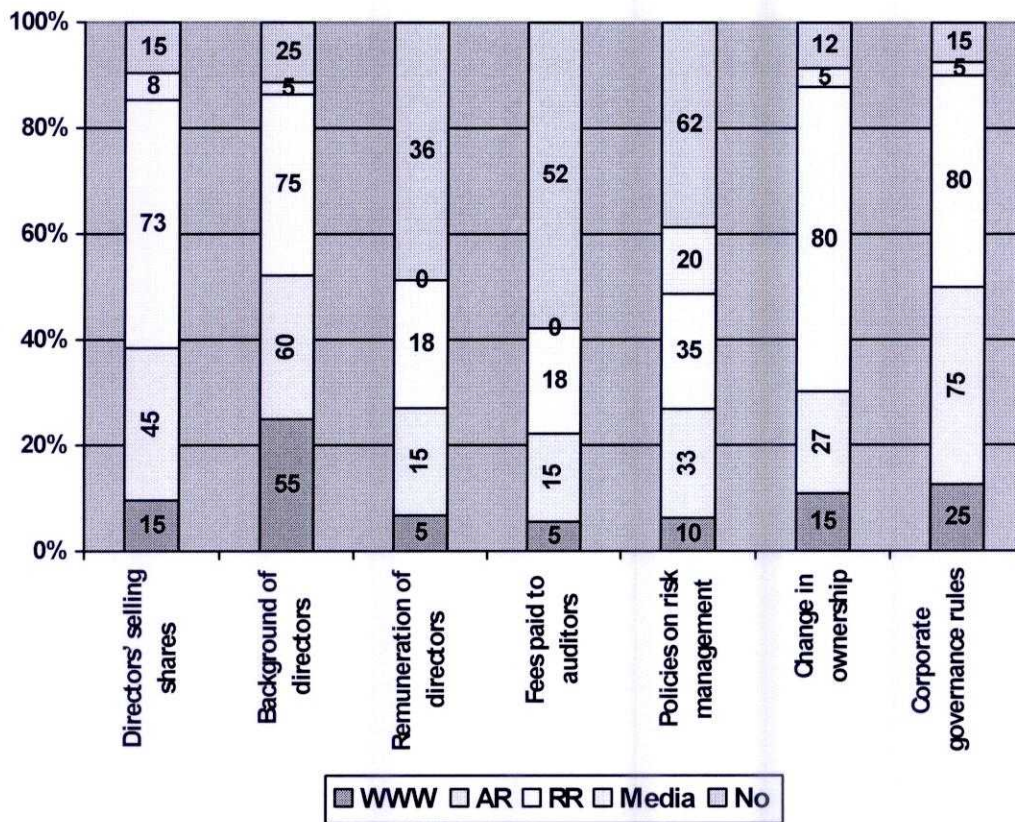


Figure 5 shows Annual Reports, and Reports to Regulatory Agencies consist the bulk of the disclosure tool for these companies. In other words, companies used 'box checking' method to provide information to the regulatory agencies rather than understanding the essence of public disclosure as a whole. On two of the aspects i.e, remuneration/ compensation paid to directors and fees paid to external auditors and consultants, some companies had zero disclosure. The study found that 15 per cent of the companies did not disclose director's selling or buying of shares, 25 per cent did not disclose background or profile of the directors, 36 per cent did not disclose remuneration paid to the directors, 52 per cent did not disclose fees paid to the external auditors or consultants, 62 per cent did not disclose company policies of risk management, 12 per cent did not disclose significant changes in the ownership and 15 per cent did not disclose corporate governance rules and vision of the company. These are contrary to the principles adopted in the best practice of CG.

4.4 Effectiveness of the 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
- (4) Performance evaluation of the CEO by the board.

4.4.1 Board Composition

According to the SEC notification on corporate governance: "The number of the board members of the company should not be less than 5 (five) and more than 20 (twenty):

Provided, however, that in the case of banks and non-bank financial institutions, insurance companies and statutory bodies for which separate primary regulators like Bangladesh Bank, Department of Insurance etc. exist, the Board of those companies should be constituted as may be prescribed by such primary regulators in so far as those prescriptions are not inconsistent with the aforesaid condition".¹⁰

And according to the Bangladesh Bank circular on corporate governance states that: "The maximum number of the Directors of the Board of banks and Financial Institutions (FIs) would be 13 and 11 respectively. Tenure of a Director of a bank would be 3 years extendable to another one term i.e. a Director can continue his/her office for six years at a stretch. A recess of one term is required after completion of six years as a Director. For FIs the tenure of a Director is 3 years and is renewable".¹¹

Because of the strict regulatory requirements of the Bangladesh Bank, it was found that 100 per cent of the FIs and banks comply with the corporate governance practices regarding the number of directors in the board. It was also found that all the PLCs which were studied have the prescribed number of directors in their board.

¹⁰ SEC notification, dated 20th February 2006.

¹¹ Bangladesh Bank Annual Report, 2008.

4.4.2 Presence and Effectiveness of the Independent Directors

SEC notification requires that:

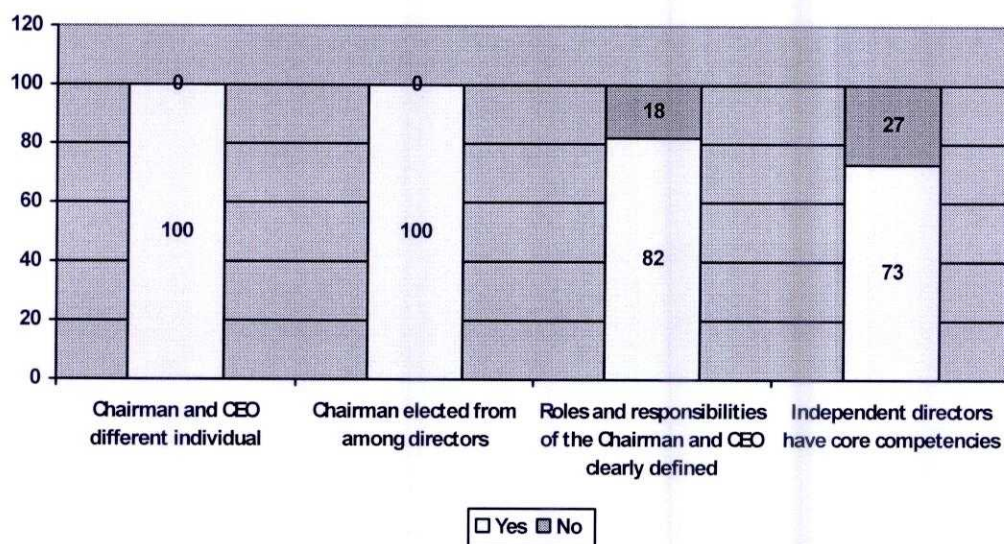
- (i) At least one tenth (1/10) of the total number of the company's board of directors, subject to a minimum of one, should be independent directors.
- (ii) The independent director(s) should be appointed by the elected directors.¹²

82 per cent of the PLCs have the provision for independent directors and others are trying to incorporate the requirements within this year. Bangladesh Bank (BB) circular on corporate governance requires that: For ensuring good governance in Banks, Banks are required to appoint 2 Directors from the depositors who will be in addition to 13 (thirteen) directors mentioned in the sub-clause 15(6) of Banking Companies Act, 1991. The study found that all of the FIs and banks were adherent to the requirements of the BB.

4.4.3 Information regarding Chairman, CEO and Independent Directors

Board size and number of independent directors were found to be within the statutory requirement stated by SEC in all three types of companies. Study found that CEOs and the Chairman of the Board are always separate individuals in all cases.

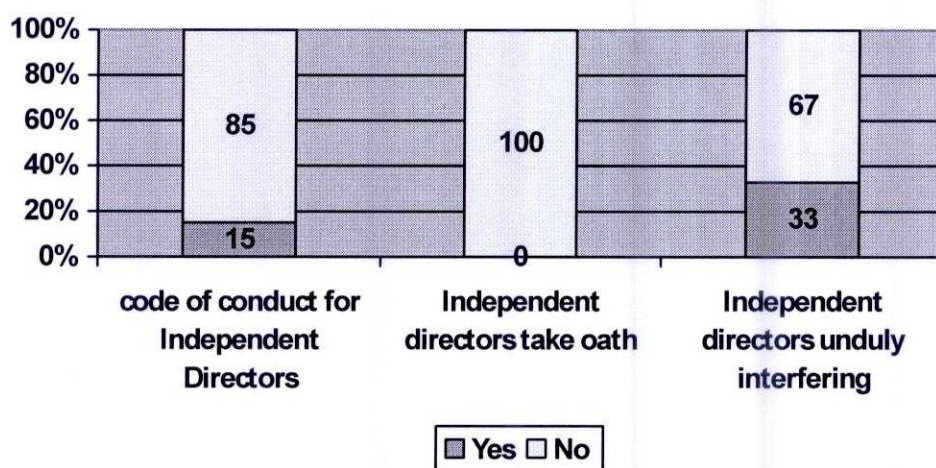
Figure 6: Information regarding Chairman, CEO and Independent Directors



¹² See appendix D for further discussion

It was found that, Chairman of the board of directors were elected from among directors in all cases. In 82 per cent cases roles and responsibilities of the Chairman and CEO were clearly defined. For ensuring good corporate governance it is necessary to define the roles and responsibilities of the chairman and CEO of the company. But one thing is of serious concern that in 27 per cent cases independent directors do not have core competencies.

Figure 7: Information regarding Independent Directors



Independent directors usually come from outside the organization. So it is important to know that whether they are well acquainted with the organization culture, norms and values. Figure 7 shows that, in 85 per cent situation, there is no specific code of conduct for the independent directors. There is no practice of oath taking for the independent directors which the CEOs think necessary to keep the company secret. During the interview session, a couple of CEOs mentioned that some of the independent directors often unduly interfere or intervene into the companies operation. About 67 per cent respondents mentioned that independent directors are unduly interfering into the company matter which is a good sign for the effective corporate governance.

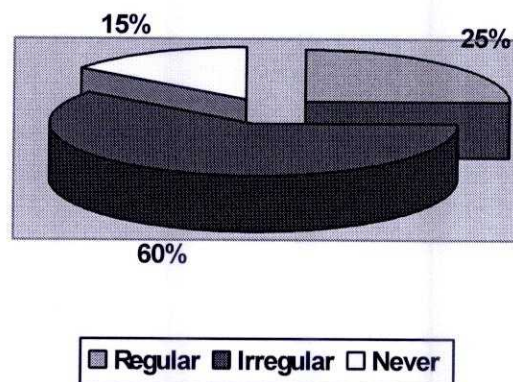
4.4.4 Evaluation and Compensation of CEOs

Study further indicates that both banks and FIs routinely evaluate and review the performance of the CEOs and compensation packages. However, in the public limited companies this procedure is rarely practiced.

4.4.4.1 Performance evaluation of CEO:

For effective corporate governance, it is necessary to evaluate and monitor the performance of the CEOs regularly. This supervision ensures a checks and balance between the board and the CEO. Figure 8 show that only 25 per cent organizations regularly evaluate the performance of the CEOs and 15 per cent organizations never evaluate the performance of the CEOs.

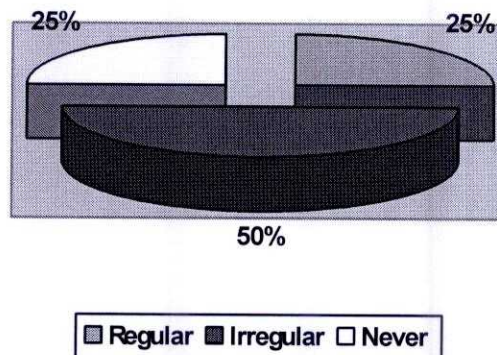
Figure 8: Performance Evaluation of the CEOs



4.4.4.2 Evaluation of CEOs compensation package:

Regular evaluation of compensation package serves as an incentive for CEOs. If the reward is commensurate with the performance, CEOs are more inclined to give their very best for the companies. Figure 9 show the study found that 50 per cent companies do not regularly evaluate the compensation packages of the CEOs. This is against the practice of good corporate governance.

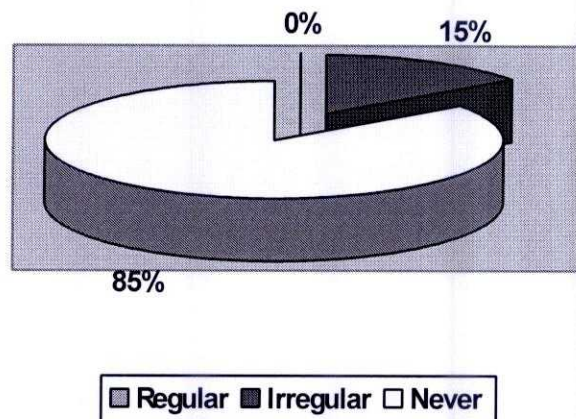
Figure 9: Evaluation of CEOs compensation package



4.4.4.3 Stock option for CEO:

Though the provision of stock for the CEOs work as an incentive, only 15 per cent companies irregularly provide stocks for the CEOs.

Figure 10: Stock Option for CEO



4.4.5 Role of the Independent Directors

On the issue of active participations of the independent directors in the board meetings, banks and FIs had a better rating than other PLCs. This is possibly due to the fact that BB requires all banks to have appointment of depositors as directors at banks. In the PLCs the role of independent directors is intermediate in nature.

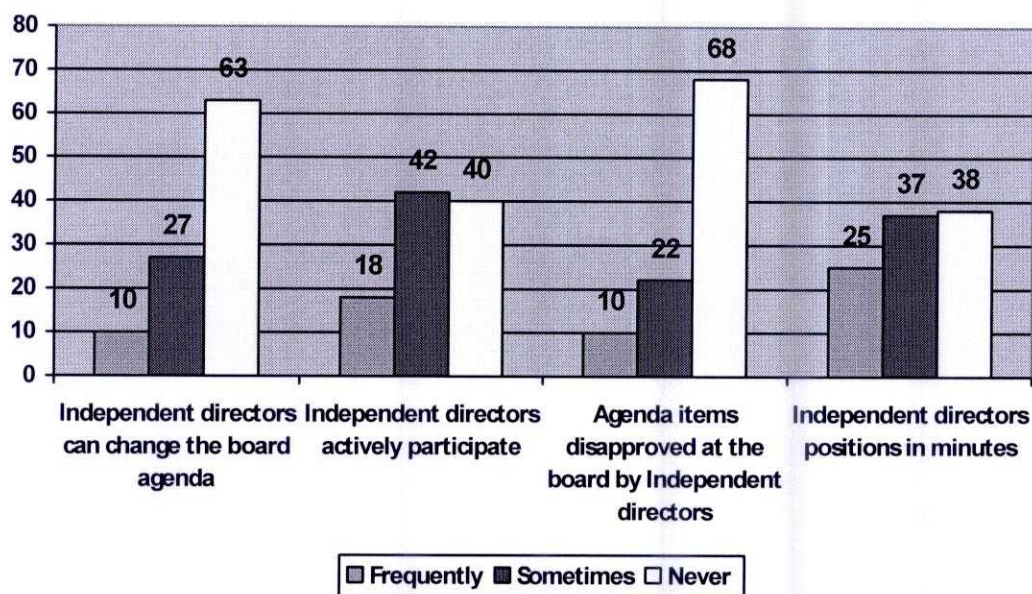
Factors that were investigated to measure the role of independent directors in the board meeting in:

- (i) Whether independent directors can add or change the board meeting agenda set by the CEO,
- (ii) Whether independent directors actively participate in board discussions,
- (iii) Whether agenda items disapproved at the board meetings by independent directors, and
- (iv) Whether independent directors' positions are recorded in minutes in the board meeting.

Figure 11 shows that in 40 per cent of the cases, independent directors were never active in the meetings of the board whereas in only 18 per cent cases they

frequently participate. The role of the independent directors is to actively participate in the board meeting so that they can provide some unbiased and neutral inputs in the company policy and strategy formulation. Thus, for ensuring effective corporate governance it is essential that companies empower their independent directors and make such a provision that will ensure their active participation.

Figure 11: Role of Independent Directors in the AGM



In another 63% of the cases, independent directors rarely intervened to alter the agenda of the meetings and in 68% of the cases; they rarely disapproved the agenda placed in the board. Independent directors rarely participated in the meeting of the private companies. This explains the weakness of the system to use independent directors to safeguard the interests of the small investors.

Figure 11 shows that, independent directors' positions are not recorded in minutes in the board meeting in 38 per cent case. The main reason is that independent directors usually do not participate in the discussion of the board meeting.

Among the three types of companies, the participation of independent or depositors directors' role is more visible in FIs and banks than PLCs.

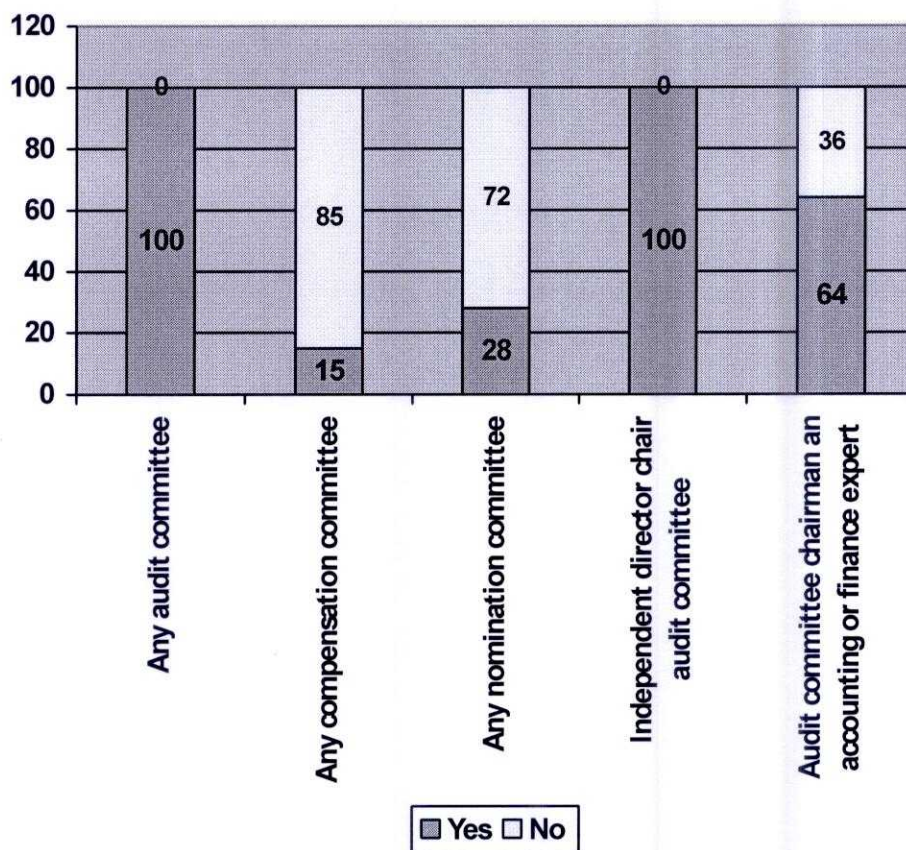
4.5 Performance of Committees

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.

4.5.1 Existence of Committees

All the companies that were studied have audit committee and independent directors chair in all the audit committee. But figure 12 shows that the compensation committee was missing in 85 per cent cases and nomination committee was missing in 72 per cent cases.

Figure 12: Existence of Committees



Existence of the audit committee in all companies is a statutory requirement. This is, rather, a poor show for the corporate sectors in Bangladesh.

According to the SEC notification, every company should have an audit committee as a sub-committee of the board of directors. The audit committee should assist the board of directors in ensuring that the financial statements reflect true and fair view of the state of affairs of the company and in ensuring a good monitoring system within the business. The audit committee shall be responsible to the board of directors. The duties of the audit committee should be clearly set forth in writing.

Figure 11 further shows that in only 64 per cent cases appointed audit committee chairman is an accounting expert, a requirement for good corporate governance according to the SEC notification. According to the condition 3.2 (ii) of the SEC notification:

The Chairman of the audit committee should have a professional qualification or knowledge, understanding and experience in accounting or finance.¹³

To measure the effectiveness and independence of the audit committee following variables were used:

- (i) Presence of expert domain knowledge
- (ii) Chairing by the independent directors
- (iii) Recording of the minutes of each meeting
- (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.

Besides the above mentioned variables, the following variables were used to measure the effectiveness of the independence committee:

- i. Whether there are any written rules for conducting audit
- ii. Whether new audit committee member is given appointment within 1 month if an existing member passes away or expires

¹³ SEC notification, dated 20th February 2006.

- iii. Whether there are any formal procedure for selecting the external auditor
- iv. Whether the company reviews the performance of the external auditor

Figure 13: Effectiveness and Independence of the Audit Committee

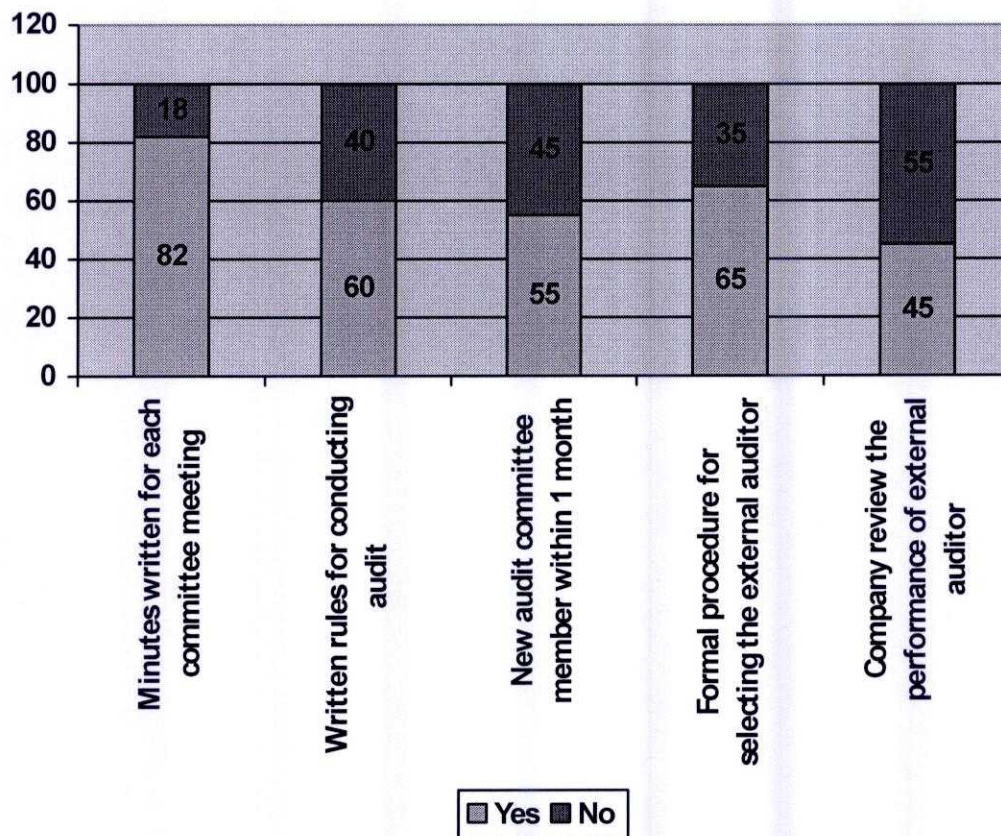


Figure 13 shows that in 82 per cent cases minutes were written for each audit committee meeting, a good practice observed mostly in FIs and banks. But in only 60 per cent cases the existence of written rules conducting audit was found, a poor show of corporate governance practice in Bangladesh. In 45 per cent cases companies failed to appoint new audit committee member to fill up the vacancies immediately or not later than 1 (one) month from the date of vacancies.

Figure 13 further shows that, there were no formal procedure for selecting external auditors in 35 per cent cases and there were no company review of the performance of the external auditor in 55 per cent cases which were a poor show of the corporate governance practices in Bangladesh.

While interviewing with some of the CEOs and top level executives, it was revealed that most of the organizations do not discuss about the remuneration of the members of the audit committee in the AGM. Among the three types of companies, in most of the PLCs there were no written audit rules and no regular review of the external and internal auditors. This shows a severe weakness in the function of the auditing system in PLCs.

4.5.2 External/ Statutory Auditors

The SEC notification states that: the issuer company should not engage its external/statutory auditors to perform the following services of the company; namely:-

- (i) Appraisal or valuation services or fairness opinions;
- (ii) Financial information systems design and implementation;
- (iii) Book-keeping or other services related to the accounting records or financial statements;
- (iv) Broker-dealer services;
- (v) Actuarial services;
- (vi) Internal audit services; and
- (vii) Any other service that the Audit Committee determines.

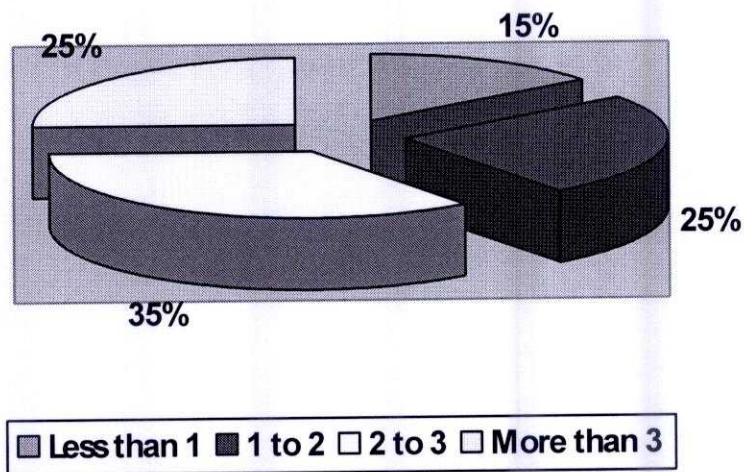
From the survey it was found that no company engaged external/ statutory auditors to perform the above mentioned services.

4.5.3 Board Meetings

To understand shareholders' rights the study used several variables like: (i) length of the meeting, and (ii) 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.

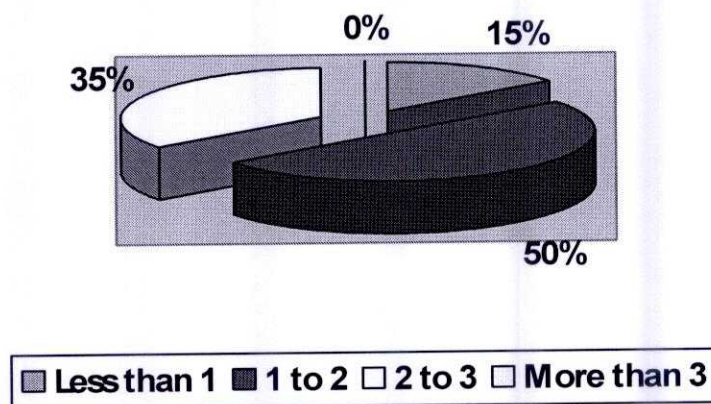
Figure 14 shows that the about 40 per cent AGM ended within 2 hours and 60 per cent AGM took more than 2 hours.

Figure 14: Duration of the last year's AGM



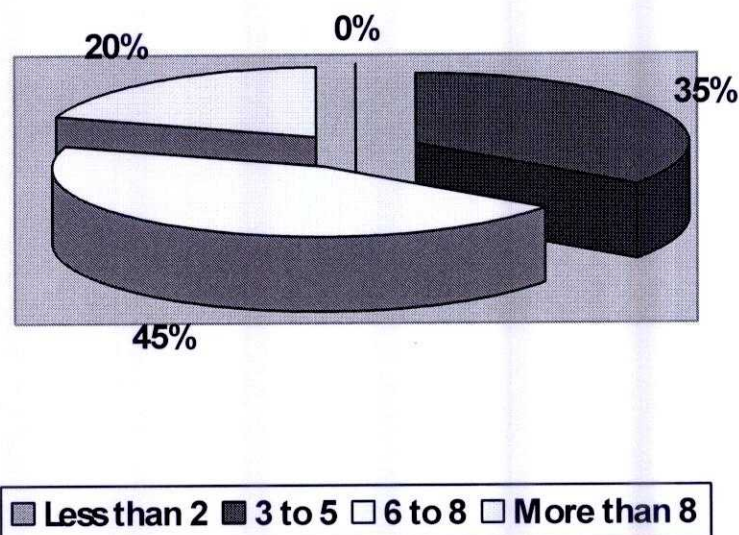
Meetings of the board were held quite frequently and in terms of average attendance, and time spent the survey found that average time spent for each meeting is between 1 and 3 hours whereas between 70% and 100% of the members attended these meetings.

Figure 15: Duration of a General Board Meeting



It was interesting to find that there was a sharp increase in the number of board meetings held last year by the companies. Figure 16 shows that about 65 per cent companies held at least 6 meetings in the last year. If the companies arrange more meetings, more discussion can be held about the policies and strategies of the business.

Figure 16: Number of board meetings held last year



5.0 FINDINGS AND CONCLUSION

This study focused on the state of corporate governance in three sectors of the economy: the PLCs, the FIs, and banks. To understand the state of corporate governance, five broad aspects of governance and management issues were studied. These are: a) ownership and control structure of the company b) shareholders' rights and disclosure of information, c) public disclosure and transparency, d) effectiveness of the Board, and e) performance of committees. Within each of these issues many sub-categories were studied as discussed above. These sub-categories reveal the basic information regarding the current status of the compliance with reference to the Code of Corporate Governance, SEC notification and BB circular for corporate governance in Bangladesh. The study used interviews with key stakeholders, experts and executives, of these types of companies through a questionnaire survey and also group discussions to know whether the existing practices of accountability and transparency comply with the Principles and Guidelines prescribed in the Code. The overall level of compliance of the Principles and Guidelines are discussed below:

5.1 Ownership Pattern and Control Structure of the Company

To understand the overall ownership pattern and control structure of the companies, this paper investigated on the following key issues:

- a) Significant voting rights of the largest shareholder,
- b) Control of ownership by large shareholders,
- c) Family control over the business,
- d) Share of the government or foreigners,
- e) Relationship between the CEO and the largest shareholder,

It was found that in almost 90 per cent of the companies, the largest shareholder had significant voting rights and the largest shareholder had effective and visible control over the company. In 75 per cent cases, the company is controlled by two or more large shareholders. In 40 per cent cases, the respondents believe that there is some family control over business. In 20 per cent cases, government or foreigners have shares in the ownership of the company. There is no relationship between the CEO and the largest shareholder in more than 80 per cent cases.

5.2 Shareholders Rights and Disclosures of Information

On the issue of shareholders' rights and disclosure, the study investigated several key issues:

- a) Practice of voting in the Annual General Meeting of the companies,
- b) Disclosure of information in terms of knowing the agenda,
- c) Lead time to analyze information,
- d) Information on equity of major shareholders,
- e) Practice of nomination and disclosure of director candidates in the meeting,
- f) Rights of the minority shareholders in nominating candidates, and
- g) Rights of the shareholders in terms of opposing candidates nominated by the management.

In terms of three sectors, this study found that banks and FIs are more open to their shareholders compared to PLCs. This means that except for PLCs, shareholders of the companies do receive information to protect their interests in the company. Non-financial public limited companies need to improve the practice of disclosure of information to all shareholders, so that other shareholders feel that they are treated equitably. The PLCs 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.

5.3 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 Bank, 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 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 banks and FIs are doing better than the PLCs. The latter should develop and promote the culture of disclosure to public in more effective manners.

5.4 Effectiveness of the Board of Directors

Four separate issues were studied to understand the effectiveness of the board:

- (1) Size of Board and structure
- (2) Presence and effectiveness of the independent directors
- (3) Separation of chairman and CEO
- (4) Performance evaluation of the CEO by the board.

An effective board is a sign of healthy corporate culture. 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, FIs and banks are doing better than the PLCs. Non-financial public limited organizations rarely evaluate their CEOs, this could be because in many cases CEOs are directly linked 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 banks and FIs depositors' directors have significant influence in the decision making

process of the board. It is therefore concluded that the spirit of appointing independent directors should be taken seriously and individual with expertise and reputation should be appointed as independent directors.

5.5 Performance of Committees

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 few but 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). Some of the FIs and banks are the only organizations where all the three committees are in existence. Although audit committees were present in all three sectors, their effectiveness is questionable, especially in non-financial institutions.

5.6 Final Remarks

Given the above discussion and findings, it is fair to conclude that corporate culture in Bangladesh is still in a growing stage. While legal requirements for good corporate governance have been created, rushing to institutionalize the culture of governance through legal and regulatory requirements or through external pressures may raise problem rather than any 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.

Corporate Governance is a journey, not a destination and the Code, SEC notification, and BB directions have provided guidance for beginning that journey for Bangladesh. However, as the corporate environment develops in Bangladesh, the Code of Corporate Governance will need to be adapted to address new developments.

6.0 RECOMMENDATIONS

The overall recommendations are suggested after examining the study results and findings:

6.1 For Public Limited Companies (PLCs)

- Board should regularly evaluate the performance of CEO which is rarely practiced
- Independent directors should play vital role in intervening in the decision making process of the board
- Individual with expertise and reputation should be appointed as independent directors
- Compensation Committee, Nomination Committee should be incorporated which are rarely in existence
- Companies should disclose director's selling or buying of shares
- Companies should disclose background or profile of the directors
- Companies should disclose remuneration paid to the directors
- Companies should disclose significant changes in the ownership of the company
- Companies should have written audit rules and should regularly review functions of the external and internal auditors
- Remuneration of the members of the audit committee should be approved in the AGM
- Shareholders should have been informed about the director's candidate prior to the AGM

6.2 For Financial Institutions (FIs)

- Individual with expertise and reputation should be appointed as independent directors
- Compensation Committee, Nomination Committee, and Risk Management Committee should be incorporated which are rarely in existence
- Companies should disclose director's selling or buying of shares
- Companies should disclose background or profile of the directors
- Companies should disclose remuneration paid to the directors

- Companies should disclose significant changes in the ownership of the company
- Audit committee should be chaired by the independent directors
- Remuneration of the members of the audit committee should be approved in the AGM

6.3 For Banks

- Depositors' directors should play vital role in intervening in the decision making process of the board
- Individual with expertise and reputation should be appointed as independent directors
- Compensation Committee, Nomination Committee, and Risk Management Committee should be incorporated which are rarely in existence
- Companies should disclose director's selling or buying of shares
- Companies should disclose background or profile of the directors
- Companies should disclose remuneration paid to the directors
- Companies should disclose significant changes in the ownership of the company
- Audit committee should be chaired by the independent directors
- Remuneration of the members of the audit committee should be approved in the AGM

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Appendix-A

QUESTIONNAIRE SURVEY ON COMPLIANCE OF CORPORATE GOVERNANCE IN BANGLADESH

Dear Respondent,

Thank you very much for your participation in this survey. This research survey is being conducted as per the partial requirement of writing a thesis paper in Master's of Arts in Governance and Development (MAGD) Program of Institute of Governance Studies (IGS), BRAC University. The objective of this research is to examine the levels of compliance of Corporate Governance in Bangladesh. This objective of the study is to understand corporate governance practices in Public Limited Companies (PLCs), and Banking and Financial Institutions (FIs) in Bangladesh. Your response regarding the corporate governance issues will be valuable in evaluating the status and nature of the practices on this particular issue. The results will be used only for the academic purpose and presented without revealing the identity of individuals or organizations.

General Information of the Company/Institution and Respondent:

Respondent's Name:.....

Sex: [1=Male, 2=Female]

Age:

Position: [1=Director, 2=CEO, 3=Manager, 4=Executive, 5=Other]

Company Name:.....

1. The ownership and control structure of the company:

Please put (✓) mark

Particulars	Yes	No
Does the largest shareholder have significant voting rights?		
Is the company controlled by two or more large shareholders?		
Is the company ownership fairly distributed?		
Is the company mainly owned and controlled by families?		
Is the company partially owned by government?		
Is the company partially owned by foreigners?		
Is there any relationship between the CEO and the largest shareholder?		

2. Shareholders participation in voting at the Annual General Meeting (AGM):

Please put (✓) mark

Particulars	Yes	No
Does your company allow proxy vote?		
Is presence required in voting at the AGM?		

3. Do you agree with the following statements for your company? Express the extent to which you agree or disagree on the given statement by choosing (✓) mark:

(Scale: 5= Strongly Agree, 4= Agree, 3= No Opinion, 2= Disagree, 1= Strongly Disagree)

Particulars	5	4	3	2	1
Adequate information are provided to the shareholders on the agendas of the AGM					
Adequate time is given for asking questions and raising issues at the AGM					
It is difficult to know how much equity ownership the major shareholders control					

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

Please put (✓) mark

Particulars	Yes	No
Directors' candidates are disclosed before the AGM		
Minority shareholders can nominate candidates at the AGM		
Directors' candidates can fail to be elected at the AGM		

5. Disclosure of Information through:

WWW	: Company's Website
AR	: Annual Report
RR	: Report to Regulatory Agencies
Media	: Print or Electronic Media
No	: Non Disclosure

Please put (√) mark in the box (Answer can be more than one):

Particulars	WWW	AR	RR	Media	No
Directors' selling or buying shares in the company					
Resume/Background of directors					
Remuneration/Compensation of directors					
Fees paid to external auditors or others					
Policies on risk management					
Significant change in ownership					
Corporate governance rules and vision					

6. Board composition:

Particulars	Number
Total number of directors in the board	
Number of outside directors	
Number of independent directors	
Foreign Nationals in the board	
Number of Shareholders attended the last year's AGM	

7. Information regarding Chairman of the Board, CEO and Independent Directors:

Please put (√) mark

Particulars	Yes	No
Are the Chairman and CEO different individual?		
Is the Chairman elected from among directors of the company?		
Are Roles and responsibilities of the Chairman and CEO clearly defined?		
Do the Independent directors have core competencies relevant in the context of the company?		
Is there any code of conduct for Independent Directors?		
Do the Independent directors take oath not to disclose information to others?		

8. CEOs Evaluation and Compensation:

Please put (√) mark

Particulars	Regular	Irregular	Never
Performance evaluation of CEO			
Evaluation of CEOs compensation package			
Stock option for CEO			

9. Representation of Independent directors:

Please put (√) mark

Particulars	Frequently	Sometimes	Never
Independent directors can add or change the board meeting agenda set by the CEO			
Independent directors actively participate in board discussions			
Agenda items disapproved at the board meetings by Independent directors			
Independent directors positions at the board meeting recorded in minutes			

10. Functions of Committees:

Please put (√) mark

Particulars	Yes	No
Is there any audit committee?		
Is there any compensation committee?		
Is there any nomination committee?		
Does the independent director chair audit committee?		
Is the audit committee chairman an accounting or finance expert?		
Are minutes written for each committee meeting?		
Are there any prescribed or written rules for conducting audit?		
Is it possible to appoint new audit committee member within 1 (one) month if any existing member expires or become unable to hold office?		
Is there any formal procedure for selecting the external auditor?		
Does the company review the performance of external auditor?		

11. Does the company engage its external/ statutory auditors to perform the following services?

Please put (√) mark

Particulars	Yes	No
Appraisal or valuation services of fairness opinions		
Financial information systems design and implementation		
Book-keeping or accounting records or financial statements		
Broker-dealer services		
Actuarial services		
Internal audit services		
Any other services that the audit committee determines		

12. Amount of time and effort directors pay to board meetings: (In hours)

Particulars	Less than 1	2-3	4-5	More than 5
Duration of the last year's AGM				
Duration of a general board meeting				

13. Number of board meetings held last year:

Please put (√) mark

Particulars	Less than 2	3-5	6-8	More than 8
Board meeting held last year				

14. Did the company face any following regulatory action for any non-compliance from the regulatory agencies like Securities Exchange Commission (SEC), Bangladesh Bank etc.? (Please put √ mark)

☐ Warning ☐ Hearing ☐ Fine ☐ Postpone share selling

15. How frequently the AGM is being held in the company? (Please put √ mark)

☐ Regular ☐ Irregular

16. Has the company ever been a bank defaulter? (Please put √ mark)

☐ Yes ☐ No

17. Does the company have any bank defaulter director? (Please put √ mark)

☐ Yes ☐ No (If yes, then how many)

Thank you very much for your kind cooperation

Appendix-B

Table-XXIII : List of Scheduled Banks
(As on 30 June 2008)

State owned/government controlled banks (4+5=9)

State owned commercial banks (4)

Agrani Bank Limited
Janata Bank Limited
Rupali Bank Limited*
Sonali Bank Limited

Specialised banks (5)

Bangladesh Krishi Bank
Bangladesh Shilpa Bank
Bangladesh Shilpa Rin Sangstha
Bangladesh Small Industries and Commerce (BASIC) Bank Limited
Rajshahi Krishi Unnayan Bank

Private commercial banks (30)

Al-Arafah Islami Bank Limited
AB Bank Limited
Bangladesh Commerce Bank Limited
Bank Asia Limited
BRAC Bank Limited
Dhaka Bank Limited
Dutch Bangla Bank Limited
Eastern Bank Limited
Export Import Bank of Bangladesh Limited
First Security Bank Limited
International Finance Investment and Commerce Bank Limited
Islami Bank Bangladesh Limited
Jamuna Bank Limited
Mercantile Bank Limited
Mutual Trust Bank Limited
National Bank Limited
National Credit and Commerce Bank Limited

One Bank Limited
Prime Bank Limited
Pubali Bank Limited

* In December 1986, it was decided to transform Rupali Bank into a Public Limited Company, keeping 51 percent ownership in the Government Sector. As of December 2007, the Government share in the paid up capital of the bank was at 93.2 percent.

Shahjalal Islami Bank Limited
Social Investment Bank Limited
Southeast Bank Limited
Standard Bank Limited
The City Bank Limited
ICB Islamic Bank Limited
The Premier Bank Limited
Trust Bank Limited
United Commercial Bank Limited
Uttara Bank Limited

Foreign commercial banks (9)

Bank Alfalah Limited
Citibank N.A.
Commercial Bank of Ceylon Limited*
Habib Bank Limited
National Bank of Pakistan
Standard Chartered Bank
State Bank of India
The Hongkong and Shanghai Banking Corporation Limited
Woori Bank

* The name has been changed to Commercial Bank of Ceylon PLC Limited in July 2008.

Table-XXIV : List of Financial Institutions*
(As on 30 June 2008)

Ahsania-Malaysia Hajj Investment & Finance Company Limited
 Bangladesh Finance and Investment Limited
 Bangladesh Industrial Finance Company Limited
 Bay Leasing and Investment Limited
 Delta Brac Housing Finance Corporation Limited
 Fareast Finance and Investment Limited
 Fidelity Assets and Securities Company Limited
 First Lease International Limited
 GSP Finance Company (Bangladesh) Limited
 IDLC Finance Limited
 Industrial and Infrastructure Development Finance Company Limited
 Industrial Promotion and Development Company of Bangladesh Limited (IPDC)
 Infrastructure Development Company Limited (IDCOL)
 International Leasing and Financial Services Limited
 Islamic Finance and Investment Limited
 LankaBangla Finance Limited
 Midas Financing Limited
 National Housing Finance and Investment Limited
 Oman Bangladesh Leasing and Finance Limited
 Peoples Leasing and Financial Services Limited
 Phoenix Finance and Investments Limited
 Premier Leasing & Finance Limited**
 Prime Finance and Investment Limited
 Saudi Bangladesh Industrial and Agricultural Investment Company Limited
 Self Employment Finance Limited
 The UAE-Bangladesh Investment Company Limited
 Union Capital Limited
 United Leasing Company Limited
 Uttara Finance and Investment Limited

* Licensed by the Bangladesh Bank under Financial Institutions Act, 1993.

** The name has been changed to Premier Leasing & Finance Limited as on 5/8/2007.

Appendix-C

SEC NOTIFICATION

Dated the 20th February, 2006

No. SEC/CMRRCD/2006-158/Admin/02-08: Whereas, the Securities and Exchange Commission (herein after referred to as the 'Commission') deems it fit that the consent already accorded by the Commission, or deemed to have been accorded by it, or to be accorded by it in future, to the issue of capital by the companies listed with any stock exchange in Bangladesh, should be subject to certain further conditions, on 'comply or explain' basis, in order to enhance corporate governance in the interest of investors and the capital market;

Now, therefore, in exercise of the power conferred by section 2CC of the Securities and Exchange Ordinance, 1969 (XVII of 1969), the Commission hereby supersedes its earlier Order No.SEC/CMRRCD/2006-158/Admin/02-06 dated the 9th January, 2006 and imposes the following further conditions to the consent already accorded by it, or deemed to have been accorded by it, or to be accorded by it in future, to the issue of capital by the companies listed with any stock exchange in Bangladesh:

Provided, however, that these conditions are imposed on '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 in accordance with the condition No.5.

The Conditions:

1.00 BOARD OF DIRECTORS:

1.1 Board's Size

The number of the board members of the company should not be less than 5 (five) and more than 20 (twenty):

Provided, however, that in the case of banks and non-bank financial institutions, insurance companies and statutory bodies for which separate primary regulators like Bangladesh Bank, Department of Insurance etc. exist, the Board of those companies should be constituted as may be prescribed by such primary regulators in so far as those prescriptions are not inconsistent with the aforesaid condition.

1.2 Independent Directors

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 the following:-

(i) 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.

Explanation: For the purpose of this clause "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.

- (ii) The independent director(s) should be appointed by the elected directors.

1.3 Chairman of the Board and Chief Executive

The positions of the Chairman of the Board and the Chief Executive Officer of the companies should preferably be filled by different individuals. The Chairman of the company should be elected from among the directors of the company. The Board of Directors should clearly define respective roles and responsibilities of the Chairman and the Chief Executive Officer.

1.4 The Directors' Report to Shareholders

The directors of the companies should include following additional statements in the Directors' Report prepared under section 184 of the Companies Act, 1994:-

- (a) The financial statements prepared by the management of the issuer company present fairly its state of affairs, the result of its operations, cash flows and changes in equity.
- (b) Proper books of account of the issuer company have been maintained.
- (c) Appropriate accounting policies have been consistently applied in preparation of the financial statements and that the accounting estimates are based on reasonable and prudent judgment.
- (d) International Accounting Standards, as applicable in Bangladesh, have been followed in preparation of the financial statements and any departure there from has been adequately disclosed.
- (e) The system of internal control is sound in design and has been effectively implemented and monitored.
- (f) There are no significant doubts upon the issuer company's ability to continue as a going concern. If the issuer company is not considered to be a going concern, the fact along with reasons thereof should be disclosed.
- (g) Significant deviations from last year in operating results of the issuer company should be highlighted and reasons thereof should be explained.

- (h) Key operating and financial data of at least preceding three years should be summarized.
- (i) If the issuer company has not declared dividend (cash or stock) for the year, the reasons thereof should be given.
- (j) The number of Board meetings held during the year and attendance by each director should be disclosed.
- (k) The pattern of shareholding should be reported to disclose the aggregate number of shares (along with name wise details where stated below) held by:-
 - (i) Parent/Subsidiary/Associated companies and other related parties (name wise details);
 - (ii) Directors, Chief Executive Officer, Company Secretary, Chief Financial Officer, Head of Internal Audit and their spouses and minor children (name wise details);
 - (iii) Executives; and
 - (iv) Shareholders holding ten percent (10%) or more voting interest in the company (name wise details).

Explanation: For the purpose of this clause, the expression “executive” means top five salaried employees of the company, other than the Directors, Chief Executive Officer, Company Secretary, Chief Financial Officer and Head of Internal Audit.

2.00 CHIEF FINANCIAL OFFICER (CFO), HEAD OF INTERNAL AUDIT AND COMPANY SECRETARY:

2.1 Appointment

The company should appoint a Chief Financial Officer (CFO), a Head of Internal Audit and a Company Secretary. The Board of Directors should clearly define respective roles, responsibilities and duties of the CFO, the Head of Internal Audit and the Company Secretary.

2.2 Requirement to Attend Board Meetings

The CFO and the Company Secretary of the companies should attend meetings of the Board of Directors, provided that the CFO and/or the Company Secretary should not attend such part of a meeting of the Board of Directors which involves consideration of an agenda item relating to the CFO and/or the Company Secretary.

3.00 AUDIT COMMITTEE:

The company should have an Audit Committee as a sub-committee of the Board of Directors.

The Audit Committee should assist the Board of Directors in ensuring that the financial statements reflect true and fair view of the state of affairs of the company and in ensuring a good monitoring system within the business.

The Audit Committee shall be responsible to the Board of Directors. The duties of the Audit Committee should be clearly set forth in writing.

3.1 Constitution of Audit Committee

- (i) The Audit Committee should be composed of at least 3 (three) members.
- (ii) The Board of Directors should appoint members of the Audit Committee who should be directors of the company and should include at least one independent director.
- (iii) When the term of service of the Committee members expires or there is any circumstance causing any Committee member to be unable to hold office until expiration of the term of service, thus making the number of the Committee members to be lower than the prescribed number of 3 (three) persons, the Board of Directors should appoint the new Committee member(s) to fill up the vacancy(ies) immediately or not later than 1 (one) month from the date of vacancy(ies) in the Committee to ensure continuity of the performance of work of the Audit Committee.

3.2 Chairman of the Audit Committee

- (i) The Board of Directors should select 1 (one) member of the Audit Committee to be Chairman of the Audit Committee.
- (ii) The Chairman of the audit committee should have a professional qualification or knowledge, understanding and experience in accounting or finance.

3.3 Reporting of the Audit Committee

3.3.1 Reporting to the Board of Directors

- (i) The Audit Committee should report on its activities to the Board of Directors.
- (ii) The Audit Committee should immediately report to the Board of Directors on the following findings, if any:-
 - (a) Report on conflicts of interests;
 - (b) Suspected or presumed fraud or irregularity or material defect in the internal control system;
 - (c) Suspected infringement of laws, including securities related laws, rules and regulations; and
 - (d) Any other matter which should be disclosed to the Board of Directors immediately.

3.3.2 Reporting to the Authorities

If the Audit Committee has reported to the Board of Directors about anything which has material impact on the financial condition and results of operation and has discussed with the Board of Directors and the management that any rectification is

necessary and if the Audit Committee finds that such rectification has been unreasonably ignored, the Audit Committee should report such finding to the Commission, upon reporting of such matters to the Board of

Directors for three times or completion of a period of 9 (nine) months from the date of first reporting to the Board of Directors, whichever is earlier.

3.4 Reporting to the Shareholders and General Investors

Report on activities carried out by the Audit Committee, including any report made to the Board of Directors under condition 3.3.1 (ii) above during the year, should be signed by the Chairman of the Audit Committee and disclosed in the annual report of the issuer company.

4.00 EXTERNAL/STATUTORY AUDITORS

The issuer company should not engage its external/statutory auditors to perform the following services of the company; namely:-

- (i) Appraisal or valuation services or fairness opinions;
- (ii) Financial information systems design and implementation;
- (iii) Book-keeping or other services related to the accounting records or financial statements;
- (iv) Broker-dealer services;
- (v) Actuarial services;
- (vi) Internal audit services; and
- (vii) Any other service that the Audit Committee determines.

5.00 REPORTING THE COMPLIANCE IN THE DIRECTOR'S REPORT

The directors of the company shall state, in accordance with the annexure attached, in the directors' report whether the company has complied with these conditions.

Annexure

Status of compliance with the conditions imposed by the Commission's Notification No. EC/CMRRCD/2006-158/Admin/02-08 dated 20th February, 2006 issued under section 2CC of the Securities and Exchange Ordinance, 1969:

(Report under Condition No. 5.00)

Condition No.	Title	Compliance status (Put ? in the appropriate column)		Explanation for non-compliance with the condition
		Complied	Not complied	
1.1				
1.2 (i)				
1.2 (ii)				
1.3				
1.4 (a)				
1.4 (b)				
1.4 (c)				
1.4 (d)				
1.4 (e)				
1.4 (f)				
1.4 (g)				
1.4 (h)				
1.4 (i)				
1.4 (j)				
1.4 (k)				
2.1				
2.2				
3.00				
3.1 (i)				
3.1 (ii)				
3.1 (iii)				
3.2 (i)				
3.2 (ii)				
3.3.1 (i)				
3.3.1 (ii) (a)				
3.3.1 (ii) (b)				
3.3.1 (ii) (c)				
3.3.1 (ii) (d)				
3.3.2				
3.4				
4.00 (i)				
4.00 (ii)				
4.00 (iii)				
4.00 (iv)				
4.00 (v)				
4.00 (vi)				
4.00 (vii)				

By order of the Securities and Exchange Commission

Dr. Mirza Azizul Islam
Chairman

Appendix-D

Corporate Governance Directions of Bangladesh Bank

Corporate Governance in Banks

Liquidity and solvency problems caused by poor governance in banks can have harmful systematic consequences in the broader economy reliant on banks for credit and payment services. High priority is therefore accorded to ensure corporate governance in banks, putting in place checks and balances comprising a mix of legal, regulatory and institutional provisions specifying the roles and accountabilities of the board, the executive management, external and internal audit, disclosure and transparency prescriptions. Corporate governance is a sine-qua-non for a sound financial system in private commercial banks. Good corporate governance can contribute substantially to a shared working environment between banks and its supervisors. It supports not only a well managed banking system but also necessary to protect depositors' interest. BB has taken several measures in recent times to put in place good corporate governance in banks. These include-regulation limiting the tenure of directors not more than six years at a stretch; reduction in the size of bank boards to a maximum of thirteen directors; appointment of two independent directors by BB; fit and proper test for appointment of board members and chief executive officers of PCBs; constitution of audit committee of board and enhanced disclosure requirements etc. In continuation of the above reforms, the roles and functions of the Board and Management were redefined and clarified with a view to specifying the powers of the management and restricting the intervention of directors in day to day management of the bank (Box 5.2).

Corporate Governance in Banks and Financial Institutions:

Corporate Governance is the system of internal controls and procedures used to define and protect the rights and responsibilities of various stakeholders. In recent year, with the increase of failure of large corporations due to poor corporate governance the issue comes to front and many organizations pronounce the guidelines those are intended to protect the rights of various stakeholders and reduce the conflict of interests among them. Banks and Financial Institutions (FIs) are "special" as they do not only accept and deploy large amount of uncollateralized public funds in fiduciary capacity, but also leverage such funds through credit creation. The depositors, particularly retail depositors, cannot effectively protect

themselves as they do not have adequate information, nor are they in a position to coordinate with each other. It is believed that there could be a contagion effect resulting from the instability of one bank, which would affect a class of banks or even the entire financial system and the economy. As one bank becomes unstable, there may be a heightened perception of risk among depositors for the entire class of such banks, resulting in a run on the deposits and putting the entire financial system in jeopardy.

The crisis of an individual bank may cause to create problem for entire financial system as well as the monetary management of the country. So, there should have clear and defined duties and responsibilities for the Management and the Board that act as the fiduciary for shareholders and the depositors. In view of the above, Bangladesh Bank is deploying continuous effort by inserting appropriate provisions in the Banking Companies Act, 1991 and Financial Institutions Act, 1993, supplemented by prudential regulations/guidelines in line with international best practices. The existing legal framework and significant current practices in particular cover the following aspects:

The Board of Directors Composition, Terms, Qualification etc.:

The maximum number of the Directors of the Board of banks and Financial Institutions (FIs) would be 13 and 11 respectively. Tenure of a Director of a bank would be 3 years extendable to another one term i.e. a Director can continue his/her office for six years at a stretch. A recess of one term is required after completion of six years as a Director. For FIs the tenure of a Director is 3 years and is renewable. Not more than 10 percent of the shares of a bank will be held by the members of a family. Not more than two member of a family will become Director of a bank in case of holding of more than 5 percent share of the Bank by that family and one member in case of holding of up to 5 percent share. Maximum voting right of any shareholder is restricted to 5 percent of total voting rights of all shareholders of the bank. On the other hand, maximum limit of holding shares of an FI by a single person/family/institution is 20 percent for domestic shareholders and 25 percent for joint venture. To be appointed a Director of a Bank or FI one requires to pass the 'fit and proper test' criteria: s/he has to hold qualifying amount of shares and not to be a minor or undercharged insolvent or mentally unsound with no record of criminal conviction or adverse judicial comment in any civil or criminal proceeding, no record

of penalization by any authority for regulatory breach and, no loan default. In addition, the Director of a Bank requires having at least ten years of business or professional experience. No employee/executive, except CEO, would be appointed as the Director of any Bank/FI.

Appointment of Directors from Depositors:

For ensuring good governance in Banks, Banks are required to appoint 2 Directors from the depositors who will be in addition to 13 (thirteen) directors mentioned in the sub-clause 15(6) of Banking Companies Act, 1991. "Fit and proper test" criteria stated above, are applicable for appointing Directors from depositors. In addition, such Director should be a depositor of the bank company must at least have a bachelor degree from any recognized university, shall not be a director, officer/staff or advisor of any bank company, financial institution, insurance company or stock exchange, he, including his family members shall not hold more than 1% shares of the paid up capital of the bank, shall not be a salaried staff of the bank, shall not be involved with any political party, shall not be a loan/tax/bill defaulter. Removal of Directors and Vacation of Office: A Bank/FI by extra ordinary resolution can remove any Director. Failure to attend in the three consecutive Board meetings without approval of leave of absence, become default of loan of any bank or FI and failure to repay the entire defaulted loan within two months of receiving the notice, submission of false declaration at the time of appointment and loss of qualification will cause to vacate the office of a Director.

Responsibilities and Authorities of the Board of Directors

(a) Work-planning and Strategic Management: The Board shall determine the objectives and goals and to this end shall chalk out strategies and work-plans on annual basis. The Board shall have its analytical review incorporated in the Annual Report as regard the success/failure in achieving the business and other targets as set out in its annual work-plan and shall apprise the shareholders of its opinions/recommendations on future plans and strategies. It shall set the Key Performance Indicators (KPIs) for the CEO and other senior executives and have it evaluated at times.

(b) Lending and Risk Management: The policies, strategies, procedures etc. in respect of appraisal of loan/investment proposal, sanctioning, disbursement,

recovery, rescheduling and writing-off thereof shall be made with the Board's approval under the purview of the existing laws, rules and regulations. The Board shall specifically distribute the power of sanction of loan/investment and such distribution should desirably be made among the CEO and his subordinate executives as much as possible. No Director, however, shall interfere, directly or indirectly, into the process of loan approval. The Board shall frame policies for risk management and get them complied with and shall monitor the compliance thereof quarterly.

(c) Internal Control Management: The Board shall be vigilant on the internal control system of the bank and Financial Institutions in order to attain and maintain satisfactory qualitative standard of its loan/investment portfolio. It shall review the reports submitted by its audit committee regarding compliance of recommendations made in internal and external audit reports and the Bangladesh Bank inspection reports.

(d) Human Resources Management and Development: Policies relating to recruitment, promotion, transfer, disciplinary and punitive measures, human resources development etc. and service rules shall be framed and approved by the Board. The Chairman or the Directors shall in no way involve themselves or interfere into or influence over any administrative affairs including recruitment, promotion, transfer and disciplinary measures as executed under the set service rules. No member of the Board of Directors shall be included in the selection committees for recruitment and promotion to different levels. Recruitment and promotion to the immediate two tiers below the CEO shall, however, rest upon the Board. Such recruitment and promotion shall have to be carried out complying with the service rules i.e., policies for recruitment and promotion.

(e) Financial Management: The annual budget and the statutory financial statements shall finally be prepared with the approval of the Board. It shall quarterly review/monitor the positions in respect of bank's income, expenditure, liquidity, non-performing asset, capital base and adequacy, maintenance of loan loss provision and steps taken for recovery of defaulted loans including legal measures. The Board shall frame the policies and procedures for bank's purchase and procurement activities and shall accordingly approve the distribution of power for making such expenditures. The maximum possible delegation of such power shall rest on the CEO and his subordinates. Decisions on matters relating to infrastructure development

and purchase of land, building, vehicles etc. for the purpose of bank's business shall, however, be adopted with the approval of the Board.

(f) Formation of Supporting Committees: For decision on urgent matters an Executive Committee, whatever name called, may be formed with the Directors. There shall be no committee or sub-committee of the Board other than the Executive Committee and the audit committee. No Alternate Director shall be included in these committees.

(g) Appointment of CEO: The Board shall appoint a competent CEO, whatever name called, for the Bank/FI with the approval of the Bangladesh Bank. The CEO for banking companies should be appointed for tenure of at least 3 years.

Responsibilities of the Chairman of the Board of Directors: As the Chairman of the Board of Directors (or Chairman of any Committee formed by the Board or any Director) does not personally possess the jurisdiction to apply policymaking or executive authority, he shall not participate in or interfere into the administrative or operational and routine affairs of the bank. The Chairman may conduct on-site inspection of any bank-branch or financing activities under the purview of the oversight responsibilities of the Board. He may call for any information relating to bank's operation or ask for investigation into any such affairs; he may submit such information or investigation report to the meeting of the Board or the Executive Committee and if deemed necessary, with the approval of the Board, s/he shall effect necessary action thereon in accordance with the set rules through the CEO. However, any complaint against the CEO shall have to be apprised to Bangladesh Bank through the Board along with the statement of the CEO.

Role of the Audit Committee: The Audit Committee of Board of Directors will assist the Board in fulfilling its oversight responsibilities including implementation of the objectives, strategies and overall business plans set by the Board for effective functioning of the bank. The Committee will review the financial reporting process, the system of internal control and management of financial risks, the audit process, and the bank's process for monitoring compliance with laws and regulations and its own code of business conduct.

The Chief Executive Officer (CEO) Appointment : To be appointed as chief executive of a banking company, an individual must possess at least 15 years of banking experience with at least 2 years in the level next below the chief executive and must meet the other stipulations mentioned above for Directors, except qualifying shares. The minimum experience of the CEO in the case of FI is 12 years and experience of 2 years in the post of next below the CEO is not required. Maximum age limit of CEO of Banks is 65 years.

Responsibilities: The CEO of the bank shall discharge the responsibilities and hold the authorities as follows:

(a) In terms of the financial, business and administrative authorities vested upon him by the Board, the CEO shall discharge his own responsibilities. S/he shall remain accountable for achievement of financial and other business targets by means of business plan, efficient implementation thereof and prudent administrative and financial management.

(b) The CEO shall ensure compliance of the Banking Companies Act, 1991 or Financial Institutions Act, 1993 as the case may be and/or other relevant laws and regulations in discharge of routine functions of the bank.

(c) The recruitment and promotion of all staff of the bank/FI except those in the two tiers below him shall rest on the CEO. S/he shall act in such cases in accordance with the approved service rules on the basis of the human resources policy and sanctioned strength of employees as approved by the Board. The authority relating to transfer of and disciplinary measures against the staff, shall rest on him, which S/he shall apply in accordance with the approved service rules. Besides, under the purview of the human resources policy as approved by the Board, he shall nominate officers for training etc.

Disclosure Requirements

Banks/FIs are required to prepare their financial statements comprising of balance sheet, profit and loss account, cash flow statement, statement of changes in equity, liquidity statement and other explanatory notes in accordance with International Accounting Standard (IAS). Copies of financial statements should be preserved in each of the bank branches, so that the customers of the bank may readily use those

on request. Besides, balance sheet should be affixed in a visible place of each bank branch. The financial statements should be published in widely circulated one Bangla and one English daily newspaper within one week of submission of the statements to Bangladesh Bank so that the stakeholders of the bank including its depositors, shareholders and regulatory bodies can get information about the bank easily. These should also be disclosed in the bank's website.

Other Issues

Lending to the Director of own bank/FI is restricted up to 50 percent of the paid-up capital of such Director. Banks are not allowed to appoint Consultants for routine works that can be performed by the regular staff. The Consultants should have specific terms of references (ToR). No past Chairman, Director, Adviser, Chief Executive would be appointed as the Consultant of the same bank. No Consultant or Advisor shall participate in decision making process or exercise power regarding the financial, administrative or operational and routine affairs of the bank. With the view to save the interest of the Depositors, Banks are to appoint two Directors from the depositors who will be in addition to 13 Directors from the shareholders. Issuance of comprehensive guideline on maintenance of risk based capital in accordance with the Basel II is under process which would strengthen long term sustainability of banks.