

# **Corporate Governance in the Stock Market of Bangladesh: Justification for a Viable Legal Framework**

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## **1. Introduction**

The corporate governance in the stock market of Bangladesh denotes a general understanding how the corporate governance is regulated in the listed companies/corporations issuing shares publicly in the secondary market of trading. Generally, the way the companies behave, act, run and carry out their functions, affairs, trade, and business, falls under the corporate governance. This also includes the behavior of the stock exchanges and the securities management institutions, how they control, practice, manage and regulate the trading of shares in stock market and the corporate affairs of the listed companies. It ensures the stability and constant development of the stock market. It is also very essential to maintain the balance between super-fall and super-rise of share price in the stock market. However, the stock market of Bangladesh which is the biggest investment market of our country, remains mostly unregulated and unsecured for the general people since it lacks an effective corporate governance guideline.

The lacking is felt because for a long period of time the stock market has remained uncared by the people, indifferently and arbitrarily handled by the stakeholders, unattended by the corporations, unregulated by the regulatory authorities, ignored by the Government and lawless by the Legislature. This leads to the failure to ensure the transparency, accountability, and integrity of companies. For this reason, the existing poor corporate governance is often held to blame for the collapse of the financial market in Bangladesh.<sup>1</sup> To fix the bugs, framing compact and effective corporate regulations in the stock market appears to be fundamental embracing deep issues, core instincts, major contributory, collaborative factors and other supplementary essentials of all the branches relating to corporate governance of the stock market and its listed companies; so is also greater awareness among the law-makers, regulatory institutions, corporations, and among the general people also.

The importance of having viable corporate governance guidelines has recently become visible in the stock market of Bangladesh when the

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<sup>1</sup> Md Gulam Saroar Hossain Khan et al, 'Current Status of the Corporate Governance Guidelines in Bangladesh: A Critical Evaluation with Legal Aspect' (2009) 3 *Bangladesh Research Publications Journal* 971.

Bangladesh Securities and Exchange Commission (BSEC) has held several factors responsible for non-effectiveness of the stock market. Of them, legal vacuums as regards the governance of companies are mostly identified. To fill up the vacuums, numerous attempts have already been taken and plans are designed by the regulatory authorities of the stock market. Amongst the attempts, the Corporate Governance Guidelines for Listed Companies of Bangladesh can be appreciated as the most noteworthy. This Guideline appears only for and confined to the companies listed with the stock exchanges of Bangladesh - Dhaka Stock Exchange (DSE) and Chittagong Stock Exchange (CSE).<sup>2</sup> This attire of boundary is made since only listed companies can issue share in stock/share market for raising capital from the public at large. However, this alone could not fix the bug in the sector. Having said this at the background, this article intends to justify a viable legal framework of corporate governance in the stock market.

## **2. Importance of Corporate Governance Guidelines in the Stock Market**

Since corporate governance emphasizes that the owners of the corporation (namely, the shareholders) need to have the most effective means at their disposal to ensure that the corporation they own brings in a reasonable return for their investment, it requires the management and the board of directors to ensure that all business decisions are taken in the best interests of the company having due consideration of the risks and rewards. At the same time, proper corporate governance expects that the directors and management of the company will put the interests of the company before their own personal interests. By this way contemporary corporate governance creates a direct relationship between the shareholders (ultimate owners) of the company and the board of directors and managers of the company. One of its purposes is to maintain check and balance between the two converse interest-holders i.e. the shareholders and board of directors/managerial authorities of the company. It also aims to put the existence and interest of the company above all (e.g. above the board of directors, managers, investors and sometime above the shareholders) upholding the original principle of distinctive personality of company.

Applying the said principle of distinctive personality of corporation, the board of directors, company secretary and managers are primarily entrusted with the duties to run and control the affairs and functions of

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<sup>2</sup> There are two stock exchanges of Bangladesh. One is Dhaka Stock Exchange (DSE) and other is Chittagong Stock Exchange (CSE). Section 2(m) of *Bangladesh Securities and Exchange Commission (Research Analyst) Rules, 2013* reads out "stock exchange means any person who maintains or provides a market place or facilities for bringing together buyers and sellers of securities or for otherwise performing with respect to securities the functions commonly performed by a Stock Exchange, as that term is generally understood, and includes such market place and facilities".

the company. They do so for and on behalf of the company, shareholders and other investors of the company and also for themselves. They can also be compared to trustee. It is felt that the function of corporate governance is not only to oversee/monitor how the corporations are functioning but also to ensure, protect and save the rights of the shareholders and other investors in the company by cutting some power from the board of directors, imposing some restrictions and responsibilities upon them and also by giving some protective device to the shareholders. One of those is to ensure effective participation of the shareholders in the company. To this effect corporate governance sincerely stresses to enable the shareholders. Full, fair and proper supply of information about the regular affairs of the company also enables the shareholders to take part in the function and management of the company. Shareholders also equip themselves with the necessary knowledge to hold management to account. In corporations where there are majority shareholders, the majority that is able to influence the appointment of directors takes particular care to ensure that their own interests do not conflict with the interests of the company. For protection of their rights the majority shareholders can stand against the arbitrary, prejudicial, illegal and adverse decisions and actions of the board of directors and corporate governance considers these issues carefully. In addition, the interests of minority and bare shareholders are not left anymore ignored by the corporate governance. Most commendably, contemporary corporate governance is taken to be highly concerned protecting the rights and interests of minority shareholders and also the bare shareholders<sup>3</sup> of the company. For these reasons the scope of corporate governance is widening and its necessity is also proving inevitable.

Furthermore, ensuring fair, proper, sound and healthy corporate practice is very fundamental to build and develop strong, competitive, productive and profitable stock market which has become one of the vital contributories of the contemporary capital market all over the world. Good companies having consistent profit making background are given easy access to the stock markets and corporate guidelines provide a strong link of assurance to this effect. Corporate governance guideline is also necessary to examine the relationship between the management and shareholders of the company. Such guideline is very crucial to find out whether management of a corporation treats with its shareholders to a

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<sup>3</sup> Bare shareholders are those who possess less than qualifying shares of being counted as minority shareholder. Under section 233 read with section 195 of the *Companies Act, 1994* the minimum qualifying shares of being considered as minority shareholder is 10% in case of company having a share capital and 15% in case of company no having a share capital. Companies Act provides some sort of protection to them who are possessing at least 10% shares and above. But there is no such protection for those bare shareholders who possess less than 10% i.e. (.0.1% to 9.49%). Corporate governance is also concerned about those shareholders who have no qualifying shares to get the benefit and protection of minority shareholder under law.

good extent by giving them dividend from profit and also by allowing them taking part in the affairs and decision of the corporation. Corporate governance guideline ensuring healthy use of voting rights by the shareholders of the company is one of the key factors in this regard. The guideline aims to have the intent that having gone to market, the company runs the business for the benefit of its owners, namely the shareholders, and behaves responsibly in the markets. Proper corporate governance practices are therefore of great importance in the capital markets.

By now the corporate governance becomes an important issue in regulating the stock market in Bangladesh. Amongst others, one basic issue that necessitates the insertion of corporate governance in the stock market of Bangladesh is that there is no limit of hiking price against share in the stock market although there is a limit below which a share value cannot fall. The limit says that a share cannot fall below TK. 10 (face value). It means a share cannot be fixed at any price between TK 1 to TK 9.99. However, a share valuing TK 10 can be reached at a price valuing TK 500 and more (paper wealth). On the other hand, under the law face value may be of each share TK 100 maximum. It means company can fix the face value of each share at any sum between TK 10 to TK100. However, this is just face value and not the paper wealth against each share. To be noted that paper wealth is the price at which shares are sold / hiked in the market for trading and there is no bar under the law to what extent paper wealth can rise. A corporate governance guideline can therefore provide an effective protection here to keep harmony between the face value and paper wealth of share. This makes the stock market to sell shares in a much higher price than the face value of shares in our country.

Generally in private limited companies directors and all the shareholders are primary shareholders and can frequently control and manage the share of the private limited companies. However, the scenery is not the same in public limited companies. It becomes upsetting when shares of public limited companies are opened in the secondary market wherefrom the secondary shareholders purchases shares in a much higher price than the face value of shares. It causes difference in share pricing. One can possess two percent of company's share only by spending TK 20,000 and another can have two percent shares by spending TK 50, 000 and others can have the same by spending more or less price. It makes the share pricing scheme of the company in the stock market more complex and irony. To get rid of this complex, puzzle and irony condition the necessity to adopt a viable corporate governance guideline in the stock market seems to be inevitable.

It is generally accepted that companies live and die by their stock price, yet for the most part they do not actively participate in trading their stocks within the market. They receive money from the securities market only when they first sell a security to the public in the primary market, which is commonly referred to as an initial public offering (IPO). In the

subsequent trading of these shares in the secondary market (what most refer to as “the stock/share market”), it is the regular investors buying and selling the stock, who benefit from any appreciation in stock price. Fluctuating prices are translated into gains or losses for these investors as they shift ownership of stock. Individual traders receive the full capital gain or loss after transaction costs; none goes with the company. To control this there needs a comprehensive and compact corporate governance regulation in the stock market.

Further, investors of the secondary market do have less influence in share pricing in our country. The original company that issues the stock does not participate in any profits or losses resulting from these transactions because this company has no vested monetary interest. This is what confuses many people. Now, the question is why then a company, or more specifically its management, does care about a stock's performance in the secondary market when this company has already received its money in the IPO. This question demands multiple complex answers. One answer is that the secondary market ensures wide participation of all kind of investors from any corner irrespective of having any direct link between the company and the investor. It helps companies to raise equity finance. On the other hand, this market can be described as fraud and sham market as in fact, in the secondary market there is uncontrolled trading and transfer of share which basically creates no direct link between the company/enterprises and the 3<sup>rd</sup> graded/multi graded investors in genuine sense. The puzzle concept of limited liabilities of companies and the complex theory of corporate personality are dichotomous. Theory and practice is not transparent so far determining the liability of the actual perpetrator. A viable corporate governance guideline can help to minimize these complex problems. A study by Nikhil Chandra Shil<sup>4</sup> to an extent correctly highlights this puzzle situation.

He shows that there are many things that jointly function in the affairs of the company and share trading in the stock market. Co-existence, co-assistance and combined function of those things can assure consistent economic growth in a country. For assembling and ensuring harmonized/balanced function amongst all those things, effective and comprehensive corporate governance guideline is very much needful. It is also needful for sound and successful regulation of the stock market by ensuring transparency, cleanliness in share trading and also by protecting the rights of different kind of shareholders, investors, other stakeholders and the interest of directors also.

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<sup>4</sup> Nikhil Chandra Shil, 'Accounting for Good Corporate Governance' (2008) 70 *Journal of Administration and Governance (JOAAG)* 2.

### **3. Basic Features of the Stock Market of Bangladesh**

Share market being the largest investment market in our country has been the most area of concern for the last 10-20 years. We usually get to know about it when massive liquid trade takes place in the market and we become interested in investing by using our own projection about the share market. We also get to know about it when huge loss suffered by the general investors in secondary share market due to heavy fall down in share price. However, the investment relies on the apparent loss and gain in share market. Most emphatically, the general investors do possess very little idea about the myth and the reality of the share market. For that reason they cannot apply proper duty of care and do blind investment in the share market. There are also lack of transparency and lack of disclosure of information by the listing companies responsible for this. With its stock market's volatility, stock fever remains a national passion owing to limited investment choices in Bangladesh. Therefore, little knowledge of the general investors about share market and its finance projection can be identified as one of the most important features of the Bangladeshi stock market.

Another basic feature of the Bangladeshi stock market has been short-term trading. The liquidity created by market manipulation activities creates an illusion of perceived wealth, and in some cases, where shares are sold in time, real wealth. In a market based on short-term trading, policy signals or perceived policy signals also dictate market sentiment. The conventional wisdom holds that the stock market as a whole has always been a viable investment. However, no market can sustain a rapid pace of growth. As share prices raises, the return on equity falls, investors will start to look at other investment assets.

Another classic feature of the stock market is a speculative bubble. It is a situation in which temporary prices are sustained largely by investors' enthusiasm rather than by consistent estimation of real value. There is a view that banks finance only well-established and safe borrowers while stock markets can finance risky, productive and innovative projects. All firms initially acquire command over some resources. This is done by debt financing or equity financing. The corporation does so primarily by selling promises of future returns to those who provide financial capital in the form of interests for creditors, dividend and capital growth for shareholders. It is often believed that there is an interrelationship between growth rates across countries or different companies and the extent to which they are dependent on external finance and the development of financial systems in which they are operating.

It is also found that some securities markets are more developed than others and they can attract more customers. Reasons behind this are not remained unidentified. One of the factors is the degree of investor protection. This is achieved by providing the customers (share traders) with more protection and ensuring them a better secured and reliable place of share trading. This trend has now become the fundamental issue

of enlarging size and reputation of a security market. Providing the shareholders with larger protection and secured place for trading share is also one of the fundamental objectives of securities regulation and corporate regulation worldwide. However, the regulation in practice aims to protect interests of both the companies and their investors since a sound coexistence of these two participants is inevitable for a securities market to operate and flourish.

Further, the principal function of any stock market is to create balance in pricing goods or services. To do this, the specific market condition that regulators and exchanges attempt to create is called the transparency. With a sufficient degree of transparency, investors have a level playing field on which to make their investment decisions. Regrettably, for Bangladeshi companies, the markets do not play this function. It fails to maintain consistent balance between fall and rise of share price in stock market.

Another feature of the stock market worldwide is the reserve capital system but in our country there is no capital reserved system either by the stock exchanges or by the listed companies. The concept of depositing reserve capital of such amount is to ensure the protection of creditors and investors of bank or financial institution. It provides further and larger protection to the creditors and investors in future when bank or financial institution would face liquidation or insolvency. It is the common practice all over the world. It is to be kept in mind that authorized and paid up capital of public limited companies is completely different from the reserves capital concept that needs to be reserved first with specified superior governing body either by the listed companies or by the stock exchange or by both. It is worth mentioning that in almost all developed stock markets in the world, such as in China, United Kingdom, United States of America, and India there is mandatory provision for having reserve capital first of any company/firm/enterprise with the superior Management Authority before entering into/enlisting with the stock market.

However, the share market being the largest investment sector of Bangladesh suffers lack of having any reserve capital system either discretionary or mandatory under law. It is very surprising that there is no provision in the stock market binding the public limited companies and the stock exchanges to have reserve fund either with the BSEC or with the Bangladesh Bank or with any other Government body. On the contrary, under the banking laws of Bangladesh it is mandatory for the financial institutions and banks to have reserve capital with Bangladesh Bank of TK 100 crores to TK 200 crores. On considering that the share market is emerging and it is the largest investment sector of Bangladesh where all kinds of investors, small, medium, large and semi-large freely invest liquid money it needs a greater protection. However, the lack of provision of having reserve capital system can be identified as one of the major fallouts of Bangladeshi stock market.

#### **4. Laws of Bangladesh providing Corporate Governance in the Stock Market**

Good corporate governance basically depends on the domestic legislation, policy and conventional corporate practice. Domestic legislation determines the basic corporate practice in a country. Domestic legislation may take reference from foreign practice only for developing a good shape of corporate governance practice but it mostly always the internal factors those determine the basic format of corporate governance practice. There are a lot of important attributes in shaping the domestic legislation of corporate governance. It may include domestic corporate laws, corporate ownership structure, the state of the economy, demand-supply-price in corporate trading, number of investors, economic growth, national income, national reserve fund, national savings in central bank, percentage of people depending on commerce and business, gross domestic product, the overall legal system, government policies, culture and history, availability of investors, number of bank, financial institution, stakeholders, corporation and traders, government capability, political scenario, law and order situation in a country, interest of small, medium, bigger and foreign investors, etc. For these in numerous in numbers, it may not be always possible to lay down all provisions or guidelines for effective corporate governance in a single piece of legislation. Comprehensive corporate governance guidelines may be the combined effect of relevant laws, policies, conventional practices, court verdicts, etc.

In Bangladesh, corporate governance guidelines are rooted in several rooms and those are guided by several factors; such as, company laws, the BSEC guidelines and notifications, rules framed by stock exchanges, banking laws, pressure from the buyers and sellers, participation of all kind of investors, dominant role of large investors, institutional capacity, overall investment in stock market, domestic cash flow, money fluctuation, inflation & liquidation, international economic condition, investment in business sector, participation of large, profitable and prospective public limited companies in stock market, nature of account (omnibus account and real account), role of Government, political condition, role of shadow stakeholders, etc. The reflection of these conditions is found in several legislations, guidelines and notifications in our country. The Companies Act, 1994, the Bangladesh Bank Order, 1972, the Financial Institutions Act, 1993, the Bankruptcy Act, 1997 and the Banking Companies Act, 1991 provide comparatively a comprehensive outline of formation, constitution, incorporation, documentation of company/bank/financial institutions; their management, regulation, company affairs, governing systems, rights, liabilities, shareholders, directors and other functional matters. The Securities and Exchange Ordinance, 1969, Securities and Exchange Commission Act, 1993 and other rules, regulations, notifications framed by the BSEC are fundamentally governing the behavior, function and affairs of the stock exchanges, the public limited companies listed with any stock exchange of Bangladesh, central depository systems, etc. Bangladesh Bank also plays an important role



providing several regulatory guidelines to this effect. All these altogether constitute the code of corporate governance in Bangladesh. Along with these, the Corporate Governance Guidelines provided by the BSEC vide Notification Nos. SEC/CMRRCD/2006-158/Admin/02-08 dated 20.02.2006, SEC/CMRRCD/2006-158/134/Admin/44 dated 7.08.2012 and SEC/CMRRCD/2009-193/151/Admin dated 18.08.2013 are particularly relevant for the corporate governance of the listed companies with stock exchanges in Bangladesh.

To what extent these are comprehensive and effective in ensuring sound corporate practice in Bangladesh is still a question of controversy. However, it is felt that these legislations are not adequate to ensure competitive, strong business market for all kind of investors in Bangladesh. That is, for the stock market, the largest money market in Bangladesh repeatedly faces challenges with great fall down of share price and a large portion of liquid money just go missing from the market in a single moment. Up and down is the common feature of money market but there must have certain consistency and level of protection which is missing in Bangladesh. Only for that reason millions of small investors come back from stock market with no gain and losing all their hopes and capitals though initially some profit in terms of liquid money by short-term trading in stock market attracted them to invest more. Unfortunately, there was no single code of corporate governance in Bangladesh. In the year of 2004 the Taskforce on Corporate Governance, convened and supported by Bangladesh Enterprise Institute proposed 'The Code of Corporate Governance for Bangladesh (Principles & Guidelines for Best Practices in the Private Sector, Financial Institutions, State-Owned Enterprises & Non-Governmental Organizations)' and the same has been institutionally adopted in the year of 2006 by the BSEC and finally in 2012.

#### **4.1 Corporate Governance Guidelines Framed by the BSEC**

After a long legal inertia, much of controversies and under tremendous recommendations by corporate market analyzers and researchers, at last, in the mid of 2012 the BSEC published a Notification of Corporate Governance being No. SEC/CMRRCD/2006-158/134/Admin/44 dated 7.08.2012 setting out some conditions as to corporate governance for the listed companies with any stock exchanges of Bangladesh to be followed for issuing shares in stock market on 'comply' basis. Though earlier a Notification was issued by the BSEC for corporate governance in the year of 2006 vide Notification No. SEC/CMRRCD/2006-158/Admin/02-08 dated 20.02.2006 that lacked to provide a standard code. Subsequently, the Notification 134 came into effect repealing the said Notification dated 20.02.2006. Thereafter, giving an immediate effect the BSEC imposes further conditions to the consent already accorded by it, or to be accorded by it in future, to the issue of capital in Bangladesh, or to the public offer of securities for sale by the Notification No. SEC/CMRRCD/2009-193/151/Admin dated 18.08.2013 (Pre-Condition of Right Issue

(Compliances of Corporate Governance Guidelines)). The condition is that no issuer of a listed security shall issue right share, if the issuer of a listed security fails to comply with the Commission's Notification No. SEC/CMRRCD/2006-158/134/Admin/44 dated 7.08.2013 regarding Corporate Governance Guidelines (henceforth referred to as "Notification 134"). None of these Notifications makes it clear that if any listed company fails to do so, what the consequence would be and whether the company will be delisted from the stock exchange.

This Notification provides some specific guidelines for corporate governance and it supersedes its earlier Notification No. SEC/CMRRCD/2006-158/Admin/02-08 dated 20.02.2006. Initially, though this Notification was made to be followed on 'comply' basis, it had not that much strongly mandatory effect upon the issuer of shares since its date of enforcement to 18 August, 2013. Now, by virtue of the aforesaid Notification dated 18.08.2013 it becomes binding upon the issuer of shares. The purpose of this Notification is denoted as to 'enhance corporate governance in the interest of investors and the capital market' subject to certain further conditions, on 'comply' basis and this is applicable only for listed companies with any stock exchange of Bangladesh.

Let's draw a discussion in details examining the effectiveness and fallout of this Notification and also see whether listed corporations comply or value it. One of the first limitations of this Notification is that it is made on 'comply' basis only for the listed companies with any stock exchange in Bangladesh. It would create disharmony in corporate governance of public companies because all public companies are not listed.

However, with the existing domain provided by the said enactment i.e. the Notification 134 adds some important conditions for determining the standard of corporate governance of listed companies in the interest of investors and the capital market, which are discussed below: -

(A) Board's Size: The number of the board members of the company shall not be less than 5 (five) and more than 20 (twenty). However, in case of banks and non-banking financial institutions, insurance companies, and statutory bodies for which separate primary regulators like Bangladesh bank, Insurance Development and Regulatory authority, etc. exist, the Boards of those companies shall be constituted as may be prescribed by such primary regulators in so far as those prescriptions are not inconsistent with the aforesaid condition (underlines provided).

The underlined provision, if challenged, may be declared *ultra-vires* because it tends to supersede the primary legislations and this is beyond jurisdiction of the enacting authority of this Notification though the BSEC apparently has such jurisdiction under section 2CC of the Securities and Exchange Commission Ordinance, 1969. There is a huge legal gap (discussed later) and it requires to be marginalized.

(B) Independent Directors: This Notification emphasizes to have independent directors in every listed corporation and at least 1/5 of the total number of directors in the company's board shall be independent directors. Condition No. 1.2 of this Notification states that 'all companies shall 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'. The independent director(s) shall be appointed by the board of directors and approved by the shareholders in the Annual General Meeting (AGM). The post of independent director(s) cannot remain vacant for more than 90 days. The Board shall lay down a code of conduct of all Board members and annual compliance of the code to be recorded.

However, the vital issue of concern is that number of independent directors is 1:5 which is very less in proportion. There comes another question whether an outsider (as director) an exercise equal rights and raises a strong voice against four others (four joint entrepreneurs). Further, independent directors will be paid by the concerned company and they have no reporting obligation about the affairs of the company before any independent/autonomous/higher managing authority, such as, Ministry of Commerce, the BSEC, and the Registrar of Joint Stock of companies and Forms (RJSC) etc.

Again, there is a major issue of concern whether one person receiving interest (or capital of survival) from a particular corporation can disclose anything prejudicial to the interest of the Governors (directors' managerial authorities) of that corporation who give him that capital in the name of remuneration/salary. There is another fundamental question whether anyone can go against his own interest for the interest of others especially for the secondary market investors who are not known and not even connected in any way. This requires a holistic approach to answer. However, the holistic approach is not encouraged in business. Business Corporation cannot be modelled holistic. Moreover, the independent directors are under no strict legal obligation to scrutinize, examine the over-all affairs and functions of the companies. They are also under no strict obligation to prepare a neutral report, give neutral opinion, and submit honest report to any superior authority for securing the best interest of the investors and for ensuring fair dealing in the capital market. However, the preamble of this Notification emphasizes attention on this very issue. Under these circumstances it cannot reasonably be expected that independent directors would act independently, neutrally and value-free. This cannot protect the right of general investors in the secondary market of listed corporations. This again makes the corporations free of any liability if loss suffered by the investors/shareholders in the secondary stock market.

(C) Obligations upon directors: Condition No. 1.5 of the Notification 134 imposes some obligations upon the directors to include some additional statements in the Report sent to the shareholders of the company with the

earlier statements as provided under Section 184 of the Companies Act, 1994. Combined effect of Conditions No. 1.5 and Section 184 provides comparatively a satisfactory situation so far it imposes duties upon the directors to prepare and submit report to the shareholder containing the aforesaid statements. It enhances the disclosure obligation upon the directors and secures greater interest of the shareholders. By this shareholders come to know about more affairs of the companies and they can be cautious about their future steps. It is not clear here that whether this obligation of reporting to the shareholder extends to the secondary shareholders who held share in secondary stock market. It is also not clear from here whether this reporting obligation is a separate obligation of reporting apart from the obligation of providing Annual Report in the Annual General Meeting of the company. However, it can be submitted with Annual Report. This Notification does not make it clear what kind of obligation this reporting obligation to the shareholders is. It raises the question whether shareholders can compel the directors to provide them with a clear report containing all these statements. There is a question again whether it again depends upon the mercy of the directors. This reporting obligation is only to the designated shareholders as described under Clause 1.5 (xxi) which amongst others excludes those shareholders having 10% interest in the company.

Further, in the secondary share market most of the investors as shareholders hold less than 10% shares. According to this Condition the directors owe no obligation to disclose the aforesaid statements to the shareholders having less than 10% shares in total. This is again a deprivation of the shareholders/stockholders in the secondary/repeated share market. It fails to prevent the bad practice of the managerial bodies i.e. directors of the company. Another deficiency is that, it does not provide the consequence of intentionally error, misleading and wrongly/*malafide* contained statement. The extent of liability of directors in case intentionally misleading statement is not cleared-up by this Notification. It also fails to impose liability upon the directors if discrepancies are found in the statement showing much more assets of the company than the real assets of the company.

Furthermore, it also lacks the mechanism to resolve the very fundamental issue arising out of the fact that, the directors tend to show the company highly profitable and prospective for attracting more investment, in fact, the company is not. Having no scope of examination, the investors (including the existing shareholders) rely on the report invest in the company and suffer loss. And this loss meets with no compensation. Neither the company nor the directors and managers of the company cannot be hold responsible for this. Because, the law fails to identify that some duties and responsibilities need to be imposed upon the directors and managerial authorities of the company to this effect. The law also fails to assure fair disclosure of information and effective participation of shareholder in the management and affairs of the company because fair disclosure ensures effective participation. Additionally, it fails to ensure

transparency, accountability because transparency, accountability, fair disclosure of information and effective participation of shareholders assure fair trade and just business. As this area remains still unaddressed by our law, it hopelessly fails to identify it as an offence and illegal. And consequently the perpetrators cannot be not identified and left unpunished.

From very barbaric sense it is often acknowledged that the concept of public issuing of shares in the stock market through IPO is to make the directors of company privileged and benefit holders at the cost, capital and risk of the investors in the secondary stock market. Money from the share market may disappear/go missing for many reasons and the market crashes when huge fall in share price occurs in the stock market. One very fundamental reason can be the imbalance and continuous price rising for a considerable period of time. Because, continuous and unnatural rising of share price for a long period of time will lead to super fall in share price since it not only causes speculative share market bubble but also causes huge difference between the face value of share and paper wealth of share. Other reasons are huge difference between the face value and paper wealth of share, huge omnibus account, dominance of large investors and lack of reserve capital system in stock market, corruption, legal abortiveness, insider trading, actual turnover and income of the company, etc. Example, "A", a big company dominates the stock market capturing 40% investment of the investors. There are 3.5 lacs investors in secondary market. The face value of each share is TK 100 but in the secondary market each share is traded between TK 380 – TK 400. However, in fact, the turnover of "A" Company is very poor and the people do not know about it and the same has not been disclosed in the director's report or Annual Report of the Company.

Moreover, the Company faces huge loss in its actual investment in business, fails to retain the existing consumers or attract new consumers and consequently gets burdened with huge loan liability. In addition, the Company faces huge liquidation and becomes profit-less, asset-less, capital-less and income-less. Further, the share price will definitely fall down. Share price may fall below the face value/original price i.e. less than TK 100. It may be occurred for many reasons. It generally occurs when company goes into liquidation due to huge debt in the market or with the creditors, banks, financial institutions and it has to go for forceful liquidation/winding up either by the court or by law. It may also occur when company voluntarily goes into liquidation. Ultimately, who are possessing the share by purchasing the same each at TK 380 - TK 400 will suffer huge loss since they have no knowledge about the real affairs of the company; and as there is no provision for suing the directors/management of the company for suffering loss in secondary share market, and also there is no provision for suing the stock exchanges who fail to assure secure investment; consequently such kind of ill suffering people go uncompensated and the perpetrators goes unpunished. No theory on this sensitive issue has been developed yet in any country all

around the world. However, the developed countries try to balance this situation through various policies, such as, by reducing the gap of share price of companies in the market and their real assets, keeping reserve capital; by maintaining consistency in share price, giving more protection to the shareholders, etc.

(D) Internal Auditor: Along with the external/statutory Auditor as stated under Sections 210-221 of the Companies Act, 1994 now the companies are under obligation to enunciate internal audit system by appointing an Audit Committee as a sub-committee of the Board of Directors. This Committee shall 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 Committee shall be responsible to the Board of Directors. The duties of the Audit Committee shall be clearly set forth in writing. This is the strongest provision of this Notification.

Without reiterating the roles of the Auditor some basic points of deficiencies in this provision needs to be examined. For example, internal Auditors will be paid by the concerned company and the Auditors will act as a sub-committee of the Board of Directors of the company. However, the Audit Committee shall have no reporting obligation about the affairs of the company before any independent/autonomous/higher managing authority, such as, Ministry of Commerce, BSEC, RJSC, etc. The same questions need to be asked for justifying the neutrality, fairness and independence of the Independent Director of the company. As stated earlier that under this Guideline every listed company is under obligation to appoint independent director. The problem is, independent director will be remunerated by the company; hence it cannot reasonably be expected that one person receiving interest (or capital of survivorship) from a particular corporation can say or disclose anything prejudicial to the interest of the Governors (directors-principal runner of companies) of that corporation.

(E) Subsidiaries: This Notification provides additional conditions along with others relating to corporate governance of subsidiary companies as set out by other legislations earlier. It provides that the provisions relating to the composition of the Board of Directors of the holding company shall be made applicable to the composition of the Board of Directors of the subsidiary company and at least one independent director of holding company will be the director of subsidiary company. It further provides that minutes of subsidiary company shall be placed before the holding company who will state its minutes that it has reviewed the minutes of subsidiary company and the audit company of holding company will audit the account fo subsidiary company. The major fallouts of this provision are: (i) it fails to impose any responsibility upon the holding/parent company because of the default of the subsidiary company, (ii) it fails to mark the core point of governing nexus between the holding company and the subsidiary company, (iii) it fails to prevent the unfair governance and

illegal trading carried out by the holding company through subsidiary company, (iv) if fails to distribute the responsibility in case of liquidation of subsidiary company by the holding company, (v) it fails to apportion the loss and profit account of holding company and subsidiary company without piercing the traditional doctrine of each company with distinctive personality and (iv) it also fails to determine the role of holding company and subsidiary company in the stock market under the same fame and name.

(F) CEO and CFO: This notification mandates the listed companies to have CEO and CFO who shall certify to the Board that they have reviewed financial statements for the year and that to the best of their knowledge and belief. Again, referring the same example as above where “A”, a big company dominates the stock market capturing 40% investment of the investors. There are 3.5 lacs investors in secondary market. The face value of each share is TK 100 but in the secondary market each share is traded between TK 380 – TK 400. But, in fact, the turnover of “A” Company is very poor and the people do not know about it and the same has not been disclosed in the director’s report, financial statement or Annual Report of the Company. CFO/CEO/Internal/External audit/Company Secretary/Company Management prepare the Audit Report and Financial Statement of a Company and they also certify those statements. Therefore, for any kind of misleading, wrong and incorrect information in those important documents in the company the CFO/CEO/Internal/External audit/Company Secretary/Company Management ought to bear responsibility but the law fails to impose any kind of responsibility upon them. This is a part of corporate governance but not effective corporate governance because it lacks ensuring accountability, answerability and liability upon CFO/CEO/Internal/External audit/Company Secretary/Company Management. By this way this corporate governance guideline fails to cover many important aspects which are necessary for ensuring effective corporate governance.

(G) Reporting and Compliance of Corporate Governance: This Notification emphasizes that every listed company ‘shall obtain a certificate from a practicing Professional Accountant/Secretary (Chartered Accountant/Cost and Management Accountant/Chartered Secretary) regarding compliance of condition of Corporate Governance Guidelines of the Commission and shall send the same to the shareholders along with the Annual Report on a yearly basis.’ To this effects this Notification also provides a format using of which the directors of the company shall state in the directors report whether the companies has complied with the conditions of this Notification.

#### **4.2 Critical Analysis of the Corporate Governance Guidelines Framed by the BSEC**

To know the efficacy and practical compliance of this Notification it is necessary first to examine the binding nature of this Notification. The binding nature of this Notification has already been discussed precisely. However, its binding nature can be analyzed under four fold –

Firstly, in the very beginning of this Notification i.e. in the Preamble its binding nature is imposed as on 'comply' basis subject to further conditions. However, nowhere in the Notification the word 'comply' is either defined or explained.

Secondly, in several places for several conditions of this Notification the complying effect is described with the word 'may/can' and under the law of interpretation, these words have always less binding effect.

Thirdly, the Notification No. SEC/CMRRCD/2009-193/151/Admin dated 18.08.2013 has come into effect only for giving this Notification immediate binding effect (mandatory effect) by using the word 'shall' in all purpose in the tune of 'no issuer of a listed security shall issue right share, if the issuer of a listed security fails to comply with the Commission's Notification No. SEC/CMRRCD/2006-158/134/Admin/44 dated 7.08.2013 regarding Corporate Governance Guidelines' since 18 August, 2013. Positive interpretation would lead to avoid any confusion between the aforesaid 'imposition on comply basis' as stated under first head and also to have a harmonious interpretation concluding that both the binding nature as stated under first and third heads emphasis on the binding nature of this Notification.

Fourthly, this is a mere Notification and it is not a primary statute and further, some of its provisions are conflicting with the primary laws. It cannot supersede any provision of primary statutes. It cannot supersede even any provision of secondary statutes which are in higher recognition that it (e.g. Order, Rules, and Regulations). Therefore, it would automatically lose its binding effect if it is challenged by any person.

Though, Section 2CC of the Securities and Exchange Commission Ordinance, 1969 specifically provides superseding jurisdiction to the BSEC, it still remains controversial. Section 2CC reads out - 'Notwithstanding anything contained in the Companies Act, 1994 or in any other law for the time being in force, or in any contract or any Memorandum and Articles of Association of any company, any consent or recognition accorded under section 2A, section 2B or section 2C, whether before or after the commencement of this section, shall be subject to such conditions, if any, as the Commission may, from time to time, think fit to impose'. This provision is not clear. The clear sense of this provision denotes that the Commission can impose any conditions superseding all other primary laws. If so, this is against the basic norm of hierarchy of laws, against democracy and rule of law as well.

This provision, in one hand, makes the BSEC more powerful and at the same time makes it more arbitrary, whimsical and unregulated. In no case it is accepted in a democratic country with a Constitution in black and white that the Commission's decision would supersede laws enacted by the Parliament. Of course, the BSEC is not a wing of independent judiciary. This provision requires a judicial clarification. According to the best knowledge and information till date, this provision is neither



challenged nor questioned yet. But it should be, at least for merging the legal gap and to get a legal solution. However, the original Ordinance did not contain such provision. This provision is included in the year of 1997 by the Securities and Exchange (Amendment) Act (Act No. VI of 1997) under Section 2CC. It is highly pertinent to mention here that this provision is hastily added after the great share market scam of 1996 in failure of erstwhile share management laws and only for providing a ready-made solution. Before 1997 the BSEC was not empowered to take independent decision by enacting regulations and notifications giving those superlative effects. This provision has empowered the BSEC to take any decision and to formulate notification giving superior effect much more than anything including primary laws and secondary laws framed by any other authority including Parliament and the other Ministries. In this way BSEC has been entrusted with more power by Section 2CC than it was entrusted earlier.

In Bangladesh, the BSEC is made the ultimate authority and it was expected that the BSEC would work so efficiently and diligently that in future nothing unexpected would occur like 1996 share market scam. In fact, the BSEC is made enable to control, manage, frame regulation, govern and direct the overall functions of stock exchanges, depositors, brokers, broker houses, trading houses, companies, banks, financial institutions, investors and all other personals relating to the activities of stock and other securities market. However, it fails to solve any problem and the recent share market scam of 2011 is a horrible example of it. Some of the personals of the BSEC have become corrupted and for 2011 share market scam the BSEC is held one of the contributories. As a result some of the personals of the BSEC including the then Chairman, Ziaul Haque were suspended permanently. This leads to highlight the major shortcomings of this Notification.

The biggest failure of this Notification is that it provides corporate governance guidelines of listed companies with any stock exchanges of Bangladesh but no guideline is provided for the corporate governance of the stock exchanges. An effective and compact corporate governance guideline for the listed companies certainly requires corporate governance guidelines for the stock exchanges and the BSEC also. But, this Notification fundamentally fails to provide any guideline either for the BSEC or for stock exchanges. It fails to depict a cumulative picture of the relationship of the listed companies and the stock exchanges in share trading in stock market. It also fails to state the role of the BSEC and other managerial authorities in order to ensuring fair corporate practice.

As discussed earlier effective corporate governance guidelines depends on many factors. And, for ensuring sound, good, viable, transparent and stable practice in stock market it is more important to cover many issues under a comprehensive code of corporate governance guidelines. It may not be possible to cover all the issues as there are other laws and policies providing corporate governance guidelines but some basic issues need to

be covered must. Amongst those, corporate governance guidelines for the stock exchanges, the BSEC, listed companies, broker houses, and depository institutions are particularly important to be covered by a code of corporate governance of listed companies especially. Under this Notification the BSEC owes no duty of monitoring, inspecting, questioning and examining the fair and accountable corporate governance practice of listed companies. It provides no mandatory obligation upon the BSEC itself. Being the ultimate supervisory authority of all listed companies of Bangladesh BSEC owes no mandatory duty and it has no accountability. The BSEC has no responsibility to be accountable to anyone, even before the judiciary for its failure to ensure effective corporate governance and fair trading of listed companies and stock exchanges in the share and securities markets.

Judiciary can also exercise some kinds of extra power *suo moto* where law is silent but scope of which is very limited. Here needs laws to be enforced by the judiciary because judiciary can enforce law when aggrieved person moves before it for seeking relief under law. When there is no law, judiciary may not exercise its inherent power. Moreover, where people have little knowledge about this sector and corporate legal practice is in elementary stage; BSEC owes more responsibility to determine its own duty, responsibility and accountability. So, reasonably this Notification cannot be commended as it can provide effective corporate governance guidelines for the listed companies of Bangladesh.

Despite of all of the controversies, this Notification is good amongst the worst. A study amongst 30 listed companies listed with Chittagong Stock Exchange shows that only 14 companies have an independent directors, 80% have appointed a CFO, Head of Internal Audit and Company Secretary, 67% did have an Audit Committee as a sub-committee of the Board of Directors, no company gave proper information regarding external/statutory audit and directors of 21% company comply with their obligation of reporting.<sup>5</sup> This report provides a satisfactory condition of corporations regarding the compliance of said rules. It clearly depicts there are still many companies who failed to fulfil the conditions of this guidelines but still are enlisted with the stock market and openly trading in market. It corroborates the earlier observation that absence of the penal provision gives an opportunity to evade/avoid the law. As stated earlier, none of these Notifications (Notification 134 and Notification 151) makes it clear that if any listed company fails to do so, what the consequence would be and does the company will be delisted from the stock exchange. This is one of shortcomings of this Notification.

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<sup>5</sup> Abdullah Golam, Mohammad Nayeem and Sabrina Hossain, *Corporate Governance Compliance: A Study of Listed Companies based on CSE-30 Index* (Dhaka: Institute of Cost and Management Account of Bangladesh (ICMAB), 2008) 13-20.

As observed the aforesaid corporate governance guidelines of BSEC fails

(i) to ensure transparency, clearness of the affairs, functions and internal activities of the board of directors of the companies to the general investors and shareholder in secondary stock market; (ii) to ensure transparency and accountability of the shadow directors; fails to disclose the ghosts of share market who silently make money under the veil;

(iii) to provide reasonable security to catch the thieves of stock market; fails to ensure the reasonable consistence between the value of company's real assets and properties and share price in secondary market;

(iv) to balance between super-fall and super-rise of the share price;

(v) to bring the investor's confidence back; fails to identify the share market perpetrators and attribute proper responsibility upon them to redress the loss suffer unreasonably; and

(vi) to ensure many things.

These are the central areas of worries about contemporary stock market governance in Bangladesh. However, strict compliance of this Notification may ensure good corporate governance of listed companies in the stock market to a few extents but it requires amendment. It may not ensure comprehensive governance but still it is a good start. It is a start from the bay and recollects the hope, courage and possibility of future development. It will also signify the mark that we are developing and trying to develop. So, it highly reminds that the door of development and intention to move for betterment is not stopped. However, it again requires high attention that the Notification 134 is given binding effect by the Notification being No. SEC/CMRRCD/2009-193/151/Admin dated 18.08.2013. Therefore, all the listed corporations are under strict obligation to comply with the conditions imposed by this Notification.

Another major limitation of this Notification is that it fails to provide any consequential effect in failure of complying with this Notification. Imposition of liability, fine, penalty or other kind of charge and legal accountability ensures greater binding effect. However, this Notification contains no liability upon the listed companies if they do not comply with this. It seems to reduce its value and mandatory binding effect. It does not even empower the BSEC to take action against the listed companies who would fail to comply with the provisions of this Notification. Further, it does not say anything about the authority of the BSEC whether it can delist any listed company from any stock exchange who would fail to carry out the obligations of this Notification. Despite all of its limitations, it is the responsibility of the BSEC itself to ensure the implementation of this Notification and to press the listed corporations to comply with the

conditions provided in this Notification. However, stakeholders, general investors and other persons of interest-concern can play a vital role for assuring the good governance of the listed companies in strict compliance with the existing provisions of law and also with the international standard.

### **5. Reasons Why Further Effective Corporate Governance is Necessary in the Stock Market of Bangladesh**

The share market in Bangladesh appears as under-developed, weak, unregulated, and unsafe for the investors and the existing corporate governance guidelines fail to ensure effective protection to this effect. The areas of concern can be addressed by emphasizing on having comprehensive corporate governance policies for overcoming the existing problems. As stated above, lack of provisions for maintaining reserve fund by the listed companies and the stock exchanges for the investors poses a great threat to the investors. In addition, major weaknesses may be attributed to different factors such as lack of legal and scientific research on share market, lack of laws and policies assuring fair trading in stock exchanges, lack of laws assuring fair and sound corporate behavior of the stock exchanges, the BSEC and other major players in the stock market. The weaknesses may also arise due to managerial fallout to prevent the continuous share price rising and sudden loss.

The lack of monitoring and controlling system of the fake beneficiary account and real account, or the absence of preventing mechanism of omnibus account and subsidiary trading, and the lack of legal provisions for holding the BSEC and stock exchanges responsible in their default and will negligence and malicious intention to ensure fair trading in stock market may contribute to the weakness of corporate governance regulations. Further, the lack of regulatory and monitoring body to prevent the fraud and loss-suffered companies from trading in stock market, or regulatory failure to prevent unsecured investors and to prevent internal trading of shares are also in the list of weaknesses. Other failures may include regulatory failure to distribute majority percentage of shares in secondary market and to prevent the insider investor from retaining majority percentage of shares, failure to remove corruption and ghosts of securities market, lack of experienced and well-trained people in the composition of securities regulators.

There are also weaknesses due to lack of regulatory authority to sue for compensation on behalf of investors in the absence of shareholders class action, lack of legal authority to redress the loss suffered investors, inactive court, lack of authority to regulate auditors and lawyers who play significant roles in preparing defective prospectuses for public consumption. Apart from all these worries, the emergence of the securities

market in Bangladesh appears to be a “natural outcome” of conditions as a result of the economic reform and open-door policy. It is to be admitted that share market does have a very lucrative prospect in future Bangladesh for different kinds of investors including foreign investors if security can be ensured. To uphold the faith of investors in stock market, to maintain the balance between fall and rise of share price, to ensure transparency, clearness of the affairs, functions and internal activities of the board of directors of the companies to the general investors and shareholder in secondary stock market, viable corporate governance regulation is necessary. It is also necessary to ensure transparency and accountability of the shadow directors; to disclose the ghosts of share market who silently take money from market under veil; to provide reasonable security to catch the thieves of stock market. Additionally, to ensure the reasonable consistence between the value of company's real assets and properties and share price in secondary market; to balance between super-fall and super-rise of the share price; to bring the investor's confidence back; to identify the share market perpetrators and attribute proper responsibility upon them to redress the loss suffer unreasonably, the assurance of fair, proper and effective corporate governance both regulated by appropriate laws and institutions is very inevitable.

## **6. Conclusion**

As observed, the stock market has become an integral part in the national economy of Bangladesh and listed companies are the vital players in the stock market. Cumulative practice of stock exchanges and listed companies requires effective corporate governance guidelines for ensuring fair trading in the stock market and providing security to the investors. In Bangladesh, corporate governance guidelines are embedded in several legislations, such as, the Companies Act, 1994, Bangladesh Bank Order, 1972, Financial Institutions Act, 1993, Bankruptcy Act, 1997, Banking Companies Act, 1991, Securities and Exchange Ordinance, 1969, Securities and Exchange Commission Act, 1993 and other rules, regulations, notifications framed by the BSEC, Bangladesh Bank, Ministry and Stock Exchanges. Amongst all, the viability of the Corporate Governance Guidelines provided by the BSEC for the listed companies vides Notification Nos. SEC/CMRRCD/2006-158/Admin/02-08 dated 20.02.2006, SEC/CMRRCD/2006-158/134/Admin/44 dated 7.08.2012 and SEC/CMRRCD/2009-193/151/Admin dated 18.08.2013 have been analyzed above. It is examined that the said Notification fundamentally fails to assure fair corporate practice of listed companies and it badly fails to provide any corporate guidelines for the stock exchanges and the BSEC in relation to the trading of securities/stock of listed companies in share market. Under the aforesaid circumstances and justifying the viability of existing legal framework of the corporate governance guidelines of the

listed companies with any stock exchange of Bangladesh it can be concluded that Bangladesh has yet to work out a code containing comprehensive, proper, fair and effective corporate governance guidelines for the listed companies and the stock exchanges. This is one structural change that needs to be made and made soon to make a good start.