



CORPORATE GOVERNANCE IN AFRICA CASE STUDY SERIES: NO 6

To study the effectiveness of legal corporate governance mechanisms that exist to protect shareholders of multinational companies operating in Zimbabwe

This case study aims to investigate the effectiveness of corporate governance mechanisms that exist to protect shareholders of multinational banks operating in Zimbabwe. Motivation for this case study has been derived from a need to contribute to the body of research on the issue which has thus far been subjected to inadequate research.

Using information based on a case study of Standard Chartered Bank Zimbabwe and other multinational banks operating in Zimbabwe, notably Stanbic and Barclays, the author examines the effectiveness of the legal mechanisms available for shareholder protection.

Findings reveal that laws and regulations that exist to protect shareholders' investments and rights are indeed available. The challenge, however, is ensuring their enforcement, which appears to be weak or non-existent in most cases. This makes the legal mechanisms highly ineffective.

These findings have implications for policymakers in Zimbabwe as they endeavour to improve the quality and effectiveness of laws on shareholder protection to encourage foreign direct investment (both human and capital). These findings are also useful for managers and regulators of banks, similar financial institutions and other multinational companies in other sectors of the economy.

1. Overview of corporate governance and the business environment in Africa

Africa is traditionally viewed as a high-risk continent by international investors. It is often believed that African economies are characterised by macro-economic instability, trade restrictions, weak institutional environments regarding property rights and the judicial system, and onerous state regulations for economic activities. In effect, countries that fail to establish acceptable standards of transparency and governance, within the bounds of good laws and an efficient criminal justice system, lose the trust and support of their citizens and the international community. Such countries find it increasingly difficult to attract trade and foreign investment. Foreign investors comfortably assess political risk, business risk, market risk and currency risk but they shy away from risks of lawlessness and corruption that all too often results from poor governance. Both of these last two risks impute unpredictability and volatility where the risk-reward equation becomes difficult to calculate (Lamberti, 2002). This further accentuates the importance of good corporate governance in developing countries such as Zimbabwe.

This case study aims to investigate the effectiveness of the corporate governance mechanisms that exist to protect shareholders of multinational companies -- specifically of foreign-owned banks operating in Zimbabwe, a developing country in Southern Africa.

2. Overview of the banking sector in Zimbabwe

Zimbabwe has a predominantly English common law system with some Dutch civil law influence. The country is a former British colony and has a commercial code derived from the UK Companies Act of 1948. Two Acts substantively govern corporate activity in Zimbabwe: the Companies Act (Chapter 24:03) of 1996 and the Zimbabwe Stock Exchange Act of 1996. The Companies Act regulates the pre-incorporation, incorporation, operations and duties of a company operating in Zimbabwe. It also deals with the rights and obligations of directors and shareholders. All public and private companies are governed by the Companies Act and its regulations.

By African standards, Zimbabwe's financial system is relatively well developed and diverse. In its role as the arbiter of the financial sector, regulator and lender of last resort, the Reserve Bank of Zimbabwe has a direct and central role to play in bank regulation. The Reserve Bank of Zimbabwe currently supervises 32 banking institutions made up of 14 commercial banks, 6 merchant banks, 4 building societies, 4 discount houses and 2 finance houses. Two of the commercial banks, namely, Standard Chartered Bank and Stanbic are wholly owned subsidiaries; two of the building societies, namely, Beverly and CABS, are wholly foreign-owned entities. Barclays (67.7%) and MBCA (78.5%) are majority foreign owned.

Banking institutions in Zimbabwe are required to comply with numerous regulatory requirements, including prudential requirements and reporting obligations. These institutions have the most developed regulatory and corporate governance system: they are subject to multiple layers of regulation under company law and market regulation. The Reserve Bank of Zimbabwe as the licensor and supervisor of banking institutions enacted the Banking Act of 1999 (Chapter 24:20). This Act governs all banks in Zimbabwe and compels them to have certain corporate governance structures. The mandate of the Reserve Bank of Zimbabwe is to ensure that all statutory and regulatory requirements are adhered to and to highlight potential or actual breaches if they occur.

Standard Chartered Bank is a wholly owned subsidiary of Standard Chartered PLC (UK), listed on both the London Stock Exchange and Stock Exchange of Hong Kong. It has sufficient share capital in public hands. The bank is governed by the UK Principles of Best Practice as contained in the Combined Code on Corporate Governance issued by the Financial Reporting Council in June 2006 (the Combined Code). The board of Standard Chartered PLC (UK) is responsible for managing the Standard Chartered Group and for ensuring that proper standards of corporate governance are maintained.

Standard Chartered Bank is the oldest and largest international bank in Zimbabwe and is recognised as the leading bank in the country. It was the first banking institution to be established in Zimbabwe (in 1892) and, after more than a hundred years of service to Zimbabwe, it continues to be committed to the country and the Zimbabwean financial sector. Standard Chartered is not listed on the Zimbabwe Stock Exchange (ZSE), but is privately owned and remains in the hands of foreign shareholders who have a controlling stake in the company.

Stanbic Bank is a wholly, foreign-owned subsidiary of Standard Bank Group. The holding company is publicly owned with headquarters in Johannesburg, South Africa. Standard Bank Group PLC is listed on the Johannesburg Stock Exchange (JSE) and the Namibian Stock Exchange. Stanbic subscribes to the Code of Corporate Practices and Conduct (King Code). Subsidiary entities within the Standard Bank Group, including Stanbic Zimbabwe, are guided by these principles to establish their respective governance frameworks which are aligned to Group standards in addition to meeting the relevant jurisdictional requirements in their areas of operations.

Barclays Bank is majority foreign-owned by Barclays PLC. The holding company is publicly owned with headquarters in London, United Kingdom. Barclays also subscribes to the Combined Code.

This research is based on a case study of Standard Chartered Bank Zimbabwe and an analysis of two other notable multinational banks (Stanbic and Barclays) operating in Zimbabwe. For simplicity, the term multinational companies shall be used interchangeably with multinational banks in this case study. However, the findings can also apply to other wholly owned or majority foreign-owned subsidiaries in other sectors of the economy in Zimbabwe, for instance, in mining, retailing and manufacturing.

The collapse of ENG Capital and Century Discount House in December 2003 heralded the onset of unfortunate events which culminated in some financial institutions being placed under curatorship. Corporate scandals and failures were witnessed in the banking and financial services industry in 2004, revealing serious flaws and lapses in corporate governance standards for banks and similar financial institutions. These scandals and failures also exposed the fact that if banks and other financial institutions are not effectively regulated, they will be prone to bouts of instability which would affect other banks and the entire national financial system.

These events convinced the Central Bank to move in and exercise its statutory mandate as supervisor of financial institutions. To ensure that banks adopted good corporate governance principles and practices, the Reserve Bank of Zimbabwe in 2004 issued a guidelines on corporate governance (Guideline No. 02 – 2004 / BSD) as well as a guideline on Minimum Internal Audit Standards in Banking Institutions (Guideline No. 01 – 2004 / BSD).

These imposed tough regulatory constraints on financial institutions, with market analysts regarding this as a militarisation of the commercial economy. This resulted in regulatory failure because of the difficulty of getting government to control itself. Regulations by the Central Bank Governor, a political appointee, had far-reaching consequences on shareholder investment: the regulations were seen as being vindictive rather than making business sense. Market analysts perceived that efforts made to improve corporate governance based on recommendations by Basel Committee on Bank Supervision were being misconstrued or abused by the Reserve Bank of Zimbabwe for personal reasons.

Multinational banks, being wholly owned and majority foreign-owned by shareholders from the 'West', invest their capital in the expectation of a positive return. Investment in Africa, specifically in Zimbabwe, comes with risks: takeovers by government; the inability to repatriate dividends because of foreign exchange controls; confiscation of assets; and even closure. Many questions arise, such as:

- what legal mechanisms exist to protect shareholder's investment?
- are these legal mechanisms effective?
- are enforced mechanisms effective?
- if these mechanisms are not effective, what should be done to remedy the situation to attract direct foreign investment (both human and capital) into Zimbabwe?

Addressing these questions is the thrust of this case study.

3. Problem statement, research objectives and hypothesis

The question this case study poses is: Are the corporate governance mechanisms available in Zimbabwe effective in protecting shareholders of multinational companies operating in that country?

The research seeks to:

- explore legal mechanisms available that seek to protect foreign shareholders of multinational banks operating in Zimbabwe
- study the effectiveness of the legal mechanisms
- study the enforcement levels of available laws and regulations, and
- make recommendations where necessary.

The case study hypothesises that legal mechanisms on corporate governance that exist *are effective* in protecting foreign shareholders of multinational banks.

4. Justification of case study, rationale and significance

Southern Africa is of interest to foreign investors because of the vast natural resources and the potential for high returns (Siddiqi, 1998; Bekaert et al., 2003), yet little research has been undertaken in countries in this region. After South Africa, Zimbabwe is the most important country in the region with its diversified economy (OECD, 2003).

The area of shareholder protection is probably one of the most interesting and intriguing aspects of corporate governance. Despite considerable and well-articulated research into shareholder protection, especially when the majority or controlling shareholder is foreign, findings are inadequate. This case study aims to contribute to the area of interest with regard to legal mechanisms that are available to protect shareholders of multinational banks.

The high-risk profile of Zimbabwe's economic and political environment as well as events in the banking sector have brought an interesting twist to an area where research is inadequate. Much research has been based on legal protection of minority shareholders. It is fascinating to see the paradigm shift to the focus on the need for legal protection for the majority or controlling shareholders, especially in light of threats and public governance (political) interference in the commercial economy and specifically the banking sector.

The author believes that investigating corporate governance mechanisms and particularly their effectiveness and enforcement levels is a fundamental research problem whose findings may inform public policy decisions as well as provide guidance for existing and potential foreign shareholders.

From the perspective of policymakers, the importance of investigating the effectiveness of corporate governance mechanisms of multinational banks in Zimbabwe is where to concentrate efforts to improve the laws and regulations, their effectiveness and enforcement levels. If judicial apparatus and market regulators are important determinants for protecting foreign shareholders, regulatory changes may be considered to improve the legal system and enforcement structures. For shareholders, the list of the legal structures available, the effectiveness of protection for shareholders' investments, and the rights and recourse channels will successfully address these issues.

On the academic front, the findings could improve understanding of shareholder protection, particularly foreign shareholders with investments in Zimbabwe, thus contributing to the body of research or even extending beyond the boundaries of contemporary knowledge and academic literature.

5. Research questions, scope and limitations

The author seeks to answer, among others, the following questions:

- What do foreign shareholders need to be protected from?
- What commercial codes are available that protect shareholders of multinational banks, and are they effective?
- What statutes govern the operation of multinational banks?
- What is the commercial legal system in Zimbabwe constituted of? Is it able to effectively enforce the commercial codes, laws and regulations that protect foreign shareholders (court system, its efficiency and competency of personnel)?
- Are there alternative courses of redress for aggrieved shareholders (statutory remedies for violations)?
- What is the role of the Commercial Arbitration Centre? Is it effective and competent?
- What is the level of independence, efficiency and competency of the judiciary system in Zimbabwe?
- What rights are shareholders entitled to? Are these rights enshrined in the law?
- How well are the laws and regulations implemented in practice?
- What developments have there been on corporate governance recently?
- What International Accounting Standards (IAS) and disclosure requirements for banks are available, and are they enforced and effective?
- Which are the main audit firms and how are they and the accounting profession regulated?

- What is the level of shareholder awareness and activism in Zimbabwe?
- What is the level of enforcement of laws around shareholder protection?
- What is the level of quality of laws and relevance to the present environment?
- Are the legal mechanisms effective in attracting foreign direct investment?
- What are the laws and regulations regarding board composition, proposition of non-executive directors, audit committees' independence, disclosure requirements, and board size?

The research is limited to the measure of the effectiveness of the corporate governance mechanisms available in Zimbabwe to protect majority and controlling foreign shareholders of multinational banks operating in Zimbabwe. The context is Zimbabwean, with the primary case study being Standard Chartered Bank (SCB) Zimbabwe, and Stanbic and Barclays Banks being secondary information sources.

The findings of this case study must be interpreted in light of the following potential limitations: First, due to scarcity of quantitative research data on protection mechanisms and enforcement levels, many of the findings are qualitative, based on in-depth interviews with Standard Chartered Bank's top management executives, legal practitioners on business law, regulators, market analysts and financial journalists. It is believed that insights derived from these findings can form the basis for detailed quantitative research in this area.

A second limitation regards the research methodology instruments used. Though interviews provided high quality responses, interviewer-interviewee bias cannot be completely ruled out.

Third, time constraints on respondents due to busy schedules, particularly captains of industry, lawyers and representatives from the Ministry of Justice, Legal and Parliamentary Affairs cannot be ignored.

Finally, financial constraints also limited the author. Stationery, booking appointments (lawyers charge per hour) and travelling to respondents' locations (secondary sources) meant having to rely on telephonic interviews, which by nature have their own drawbacks and limitations. Furthermore, lack of cases (exhibits) from primary and secondary sources also starved the research of hard evidence. Respondents cited sensitivity and client confidentiality.

6. Literature review

Saunders et al (2000) see literature review as the basis for research, its main purpose being to give an insight into what other authors have researched in the same area. This enhances insight into the problem and helps to refine the research questions being explored by the researcher. This chapter reviews relevant literature and explores areas of legal protection mechanisms for shareholders evaluated by other authors. Having established useful pointers, these will be adopted to the research objectives of this study where they relate to the Zimbabwean context.

- **Concept of shareholder protection**

Consistent with previous case studies, this case study defines corporate governance as '...ways suppliers of finance to corporations assure themselves of getting a return on their investment...' (Shleifer and Vishny, 1997).

The most prominent vehicle for corporate governance are the legal protections in national laws. The claim is that national legal protections have a profound influence on the willingness to invest resources in firms.

'[T]he principal problem is not that laws are not strong enough, but that they are not enforced....unhappy shareholders can rarely develop enough facts to prove the rampant self-dealing that occurs every day. The courts respect only documentary evidence, which is rarely available, given limited discovery and a manager's skill in covering their tracks... [so] pursuing a case...will take years and when done, enforcing a judgment is problematic because enforcement is by the same biased or corrupt lower court that the shareholder began at. '

Reference to the history of institutions in markets that have developed provides a guide. Literature that has adopted this approach suggests that legal protections for corporate governance can only be effective if there are four additional institutions: social norms; political structures to limit the sovereign; the location of the judicial authority; and information or reputation of intermediaries.

- **Social norms and judicial efficiency**

Cooter (1996), among others, emphasises that there needs to be social support for legal reforms to have an impact. In states where laws are consistent with social norms: 'the law is obeyed out of respect. Under such a system, private citizens supplement official enforcement of the law, which is critical because officials lack the *information* and *motivation to enforce* the law effectively on their own.'

Critically, Cooper argues that legal protection will simply be ignored where the legal protection is inconsistent with social norms. There is growing recognition of the interaction between behavioural patterns and legal institutions. New laws are not enough to stimulate financial restructuring. Changing a culture is necessary.

- **Political structure and judicial efficiency**

For legal protections to matter, there must also be expectations that those laws will be followed. The efficiency of the judiciary does not just come from sophistication in the organs of state that interpret and implement judicial judgements; it also comes from the judiciary's interest in enforcing the law. Such interest has been linked to political structures that limit the power of the sovereign relative to other interest groups in society.

- **Location of judicial authority and efficiency**

This refers to how government organises and allocates judicial authority. The argument here is that to provide information and lower the costs of enforcement, it may be optimal not to keep judicial authority in the general court system but to delegate authority to a specific regulatory agency tasked with that job and even to allow that regulator to delegate further to private sector organisations.

Johnson and Shleifer (1999) provide more recent evidence of the importance of legal protections and their enforcement through specific regulatory authorities rather than relying on a *laissez-faire* approach backed by the general court system.

- **Efficient collection of information**

With information, shareholders can use the powers embodied in legal protections to change the allocation of resources or simply to exit the country. Recent literature finds that differences in laws and their enforcement affect dividend payment, availability and cost of external finance and market valuations. Firms could improve shareholder protection rights by increasing disclosure, selecting well-functioning and independent boards, and imposing disciplinary mechanisms to prevent management from engaging in expropriation.

Klapper and Love (2002) assert that firm-level governance is lower where there is a weak legal system. This is supported by La Porta et al (1998) whose conclusion found Zimbabwe scored low on regulatory state, professionalism, stability and reliability. It was also found that Zimbabwe is high risk with regard to rule of law, expropriation and corruption in government. The commitment of government and the relationship is an overriding factor in developing countries where an environment conducive to corporate governance must be created to ensure enterprise sustainability (Botha, 2001).

7. Research methodology

This section provides an overview of the strategy used to conduct the research and collect the necessary information. This section entails choice of research techniques applied to corresponding research objectives.

The research on the effectiveness of the corporate governance mechanisms that exist to protect shareholders of multinational companies is based on a case study of an international commercial bank – Standard Chartered Bank Zimbabwe. The author used a combination of primary and secondary sources of information to ensure that data was current and relevant to the study. Secondary data was important as some of the data could not be collected first-hand due to time and financial constraints. As an employee of Standard Chartered Bank, the author had access to primary information through access to confidential information, internal website data bases and exposure to high-level meetings.

Secondary sources entailed the use of banks' annual reports, the internet, judicial reports (from the Ministry of Justice, Legal and Parliamentary Affairs), banking bulletins, the Reserve Bank of Zimbabwe guidelines, Banking Association of Zimbabwe (BAZ) reports, Institute of Directors of Zimbabwe (IODZ) reports, Institute of Chartered Accountant Zimbabwe (ICAZ) journals, Institute of Bankers Zimbabwe (IOBZ) reports, Chamber of Commerce reports, lawyers and financial analysts. Secondary sources were also obtained for the other two international commercial banks, Stanbic and Barclays.

- **Research design and data collection**

A combination of survey and desk research was undertaken to collect data from respondents. Survey research entailed one-on-one, in-depth interviews (both face-to-face and telephonic) as well as questionnaires (mostly through emails as it was less costly). Desk research mainly relied on internet and analysis of industrial publications and observations other researchers have made on the subject matter. The design ensured relevant and high quality information was obtained.

The analysis performed in this study is based on financial institutions. The researcher selected financial institutions (international banks) for three reasons: first, the banking sector is over-regulated and restrictive; second, multinational banks are at more risk as the major shareholders are largely British; and third, findings can be inferred to other multinational companies in other sectors of the economy.

Respondents targeted in Standard Chartered Bank were heads of units, specifically of Legal and Compliance, Corporate Affairs, Global Markets, Internal Audit, Fraud Risk, Consumer Banking and Human Resources. Questionnaires were flighted and in-depth interviews were conducted with these top management executives.

Questionnaires were useful as they were easy to administer (via email) and fair measurement and analysis was possible since all respondents answered exactly the same questions. Interviews were useful as they provided opportunities for clarification on ambiguous areas due. Interviews also allowed for greater flexibility to explore further remarks. The interviews elicited in-depth information, views, feelings, perceptions, experience and knowledge of the industry on shareholder protection mechanisms available and their effectiveness.

Data was collected mainly in the following areas:

- commercial codes on corporate governance available
- the effectiveness and quality of laws and regulations that protect foreign shareholders of multinational companies
- efficiency and competency of the Zimbabwean court system
- availability and effectiveness of alternative courses of redress for aggrieved shareholders
- the enforcement of levels of laws and regulations in practice, and
- any recommendations.

8. Research findings

The major findings or concerns about the effectiveness of corporate governance mechanisms that exist to protect shareholders of multinational banks were:

- **Laws and regulations**

- a. **Internally**

Standard Chartered Bank Zimbabwe has corporate governance codes derived from the Standard Chartered Group which is governed by the UK Principles of Best Practice as contained in the Combined Code. The subsidiary therefore aligns itself to the standards of its parent company. The Legal and Compliance Department is responsible for monitoring and ensuring compliance to the Combined Code. Likewise, Stanbic and Barclays have corporate codes aligned to those of parent companies. It can, however, be seen from the interviews that local laws or national codes take precedence over group codes.

Enforcement by the Reserve Bank of Zimbabwe through penalty for non-compliance can result in the withdrawal of a banking license. This threat has apparently sufficed to entice banks to comply with the provisions of the Acts, for example, the Reserve Bank of Zimbabwe Act, the Banking Act and Companies Act of Zimbabwe.

Respondents believe that internal protection mechanisms of multinational banks are highly effective but selectivity in the Central Bank as a regulator on compliance matters poses a threat to shareholders' investments as the assessments for withdrawing banking licences are quite subjective.

Standard Chartered Bank Zimbabwe has guidelines for its staff and management on Code of Conduct, Anti-Money Laundering, Speak Up Policy and Conflict of Interest. Every employee is expected to undertake e-learning courses on these subjects and sign their consent to abide by these policies. The Financial Crime Risk department also helps the company to curb fraud and money laundering activities by staff and customers. These policies and mechanisms help to manage risk and instil discipline in management and staff and thus protect shareholders from expropriation by insiders. This was proved during the bank scandals between 2006 and 2008 where commercial banks, merchant banks, building societies and finance houses were closed and some placed under curatorship because they had departed from their core business to concentrate on money market and liquidity positions. According to the Reserve Bank of Zimbabwe, this created a fictitious excess money supply. As a result of sound corporate governance mechanisms, Standard Chartered Bank, Stanbic and Barclays were not involved in these scandals, which in turn protected the investments of their shareholders.

Standard Chartered Bank Zimbabwe (The Bank in this section) also complies with rules and regulations regarding:

- **Board composition (proportion of non executive directors)**

The Bank ensures the majority of directors who sit on the board at group and country level are non-executive as stated by the requirements of the Combined Code and Zimbabwe Corporate Governance Code.

- **Audit committee independence**

Tax, audit and consultancy services by external auditors are provided by reputable firms, for example KPMG. The Bank has adopted International Accounting Standards (IAS) which are enforced by the Institute of Chartered Accountants of Zimbabwe (ICAZ). As a statutory requirement in Zimbabwe, the Bank has also complied and has an independent internal audit department or function.

- **Disclosure requirements**

The Bank follows a disclosure-based regime as required by the Companies Act to publish financial statements including material, financial and non-financial information. This regime helps shareholders to monitor their investments by accessing information about the Bank's activities.

These protection mechanisms on corporate governance are highly effective in ensuring shareholders of the Bank are adequately protected from expropriation by insiders through outright theft of assets, transfer pricing, excessive executive compensation, entrenchment of inept management teams and diversion of funds to unsuitable projects that benefit one group of insiders.

By complying with these requirements on corporate governance, the Bank also protects its shareholders from violating local laws regarding the minimum acceptable standards.

b. Externally

The research found that banks in Zimbabwe have the most developed regulations on corporate governance. They are subject to multiple layers of regulation by the requirements of company law and market regulators (principally the Reserve Bank of Zimbabwe).

For the purpose of this research, the codes have been grouped under international, regional and local.

i. International

Multinational banks (Standard Chartered Bank, Stanbic and Barclays) adhere to the principles and provisions of the Combined Code on Corporate Governance. They also subscribe to the Basel Committees' views and standards on legal corporate governance and protection of shareholders as recommended in the Basel II Banking Regulations.

ii. Regional

Banks are also governed by the Code of Best Practice developed by the Commonwealth Secretariat and derived from the corporate governance code of the Organisation for Economic Co-operation and Development (OECD). The OECD's Principles of Corporate Governance represent the minimum standards that countries agree upon, without being prescriptive and binding. They are equally applicable to countries with civil and common law traditions such as Zimbabwe. The OECD principles encourage the rights of shareholders (and others) to receive relevant information about the company in a timely manner and equitable treatment of foreign shareholders, among other things.

Banks are also subject to the principles and provisions of the Commonwealth Association for Corporate Governance Guidelines: Principles for Corporate Governance in the Commonwealth (November 1999).

Lastly, the King Report of South Africa also provides guidelines on effective corporate governance practices and the legal protection foreign shareholders have.

iii. Local

Multinational banks as well as other financial institutions operating in Zimbabwe are governed by the Companies Act of 1996 (Chapter 24:03) and a host of other regulatory laws. A commercial code on corporate governance is available: the Principles of Corporate Governance in Zimbabwe: Manual for Best Practice was published in 2001 and launched by the Ministry of Industry and International Trade. These principles encourage banks to comply with the Combined Code which has provisions for the protection of shareholders. The Companies Act regulates business activities and protects shareholders by making the board accountable to them. Section 196 of the Companies Act provides for an aggrieved shareholder to report to the Registrar of Companies within 30 days. The Registrar of Companies under the Ministry of Justice administers and regulates the Companies Act. The

Registrar is empowered to investigate potential violations of the Companies Act and to prosecute when appropriate. The Ministry of Justice has powers to investigate the affairs of a company either as a result of an application by a shareholder or by the Registrar of Companies or on its own accord if it has reasons to believe that the management is guilty of fraud or misconduct towards a shareholder.

Respondents noted, however, that lack of resources, technology and capacity to effectively monitor the vast number of registered companies often hinders the Registrar of Companies in enforcing laws on protection of foreign shareholders.

The Reserve Bank of Zimbabwe, as the principal supervisor of all financial institutions, follows its own laws and regulations. There are two pieces of legislation: the Banking Act of 1999 (Chapter 24:20) and the Reserve Bank of Zimbabwe Act 22:15. Two guidelines were also issued in 2004, namely, Corporate Governance (Guideline No. 02 – 2004/ BSD) and Minimum Internal Audit Standards in Banking Institutions (Guideline No. 01 – 2004/BSD). Banks are compelled to comply with both the laws and the guidelines to ensure good standards of corporate governance. These laws and guidelines, also called principles, policies, recommendations or codes of best practice are legal mechanisms that greatly help in the protection of foreign shareholders' investments through sound corporate practices by their management and staff.

The Reserve Bank of Zimbabwe plays an important role in promoting effective corporate governance for banks and similar financial institutions it regulates. The Reserve Bank of Zimbabwe has a strong interest in ensuring that there is effective corporate governance at every bank and financial institution. Supervision underscores the need to have appropriate levels of accountability, disclosure and checks and balances within each bank. The Reserve Bank of Zimbabwe has a dedicated Corporate Governance, Supervision and Surveillance Division.

However, the excessive supervisory powers vested in the Central Bank are cause for concern by multinational banks. The banks assert these powers are prone to abuse as is currently evidenced where guidelines, policies and codes which are highly 'perishable' are enacted and issued at short notice and with immediate effect. Failure to comply may result in the closure of a bank or the withdrawal of the banking licence. Respondents noted that this is a threat to normal business operations and to shareholders' investment.

An issue that has dominated the banking sector for the past few years are the new capitalisation requirements. By September 2006, commercial banks had to revise their capital base to USD10million; merchant banks, finance houses and building societies to USD7.5million, while for discount houses it was pegged at USD5million. Failure to comply meant closure, with shareholders having no remedies. Market analysts noted that although this was a regulatory requirement recommended by the Basel Committee on Capitalisation for Banks, the manner, execution and timing was considered punitive as shareholders had to inject more capital to protect their investment from the regulatory risk. The banking sector has thus become excessively regulated and volatile which constrains normal banking activities.

To a large extent the legal and institutional framework for effective corporate governance, including the protection of foreign shareholders, exists in Zimbabwe by virtue of laws such as those related to Companies Act, Banking Act, and various Codes. The problem, however, lies with enforcement, which appears to be weak or non-existent in most instances.

- **The challenge of enforcement**

Rules on corporate governance are not credible unless they are applied effectively. For this to happen, regulators must have sufficient authority and resources. The review of the regulatory framework for multinational banks in Zimbabwe indicates that, in most cases, reasonable

regulations have been put in place to achieve the key objectives of corporate governance, particularly in the areas of board composition, disclosures, board sizes and internal audit committees' independence. However, the effectiveness of these rules depends on the ability of the regulatory agencies to enforce, that is, to execute a process that provides restitution when rules are broken. Anecdotal evidence indicates that enforcement of rules and regulations is increasingly challenged by a weak judiciary system, making it difficult to obtain convictions when rules are violated. Thus, banks or financial regulators can work hard to administer the law and identify violators but the normal process of enforcement is not equipped to apply the new laws.

Enforcement of laws via courts assumes that:

- courts have resources to handle cases in a timely way, and
- judges understand the banking sector and new legal concepts well enough to enforce the law.

The judiciary in Zimbabwe is plagued by weaknesses that include:

- politicisation and lack of independence
- corruption and low remuneration (low morale)
- too few judges, staff and lawyers with little commercial expertise (brain drain)
- ignorance of the legal system, hence a slow and patchy process to obtain a satisfactory resolution due to backlogged courts, and
- bias or selectivity in judgements due to corrupt court officials and judges.

In summary, laws that recognise shareholders (including foreign shareholders) as the legitimate owners of the corporation and, therefore, deserving of equitable treatment do exist. However, the regulatory framework for the protection of foreign shareholders will be ineffective unless there is an enforcement regime that works. The effectiveness of enforcement determines regulators' success in achieving disclosure and transparency.

▪ **Alternative courts (Commercial Arbitration Centre)**

Although aggrieved foreign shareholders can approach the courts directly if their statutory rights are allegedly violated, courts appear not to provide a reliable mechanism for protecting these rights. The commercial law system in Zimbabwe is thus perceived to be inefficient. In cases of redress against violations (statutory remedies), the Commercial Arbitration Centre (CAC) provides effective alternatives to the courts as a means of recourse for aggrieved shareholders. The CAC is an independent entity, perceived to be efficient and speedy in the resolution of cases. The CAC has thus emerged as an alternative legal protection mechanism to the inefficient courts. The establishment of the CAC in July 1995 has gone a long way towards complementing the administrator of justice in Zimbabwe. Arbitration is now regularly chosen by shareholders of multinational banks as the means of resolving commercial disputes and the superior courts have an enviable record of enforcing arbitrage agreements and awards expeditiously, economically and reliably. However, some analysts have expressed concern about the effectiveness of the CAC as it only sits as an arbiter in cases where both parties to a dispute have agreed to arbitration in the Articles of Association. Without mutual consent, the arbitration court is not applicable.

The degree of independence of the CAC has also been questioned as some of its management have political affiliations, for example, one of the directors is also the Mayor of Harare.

▪ **Uncertainty of property rights**

Another finding is that there is a lack of security about property rights that currently pervades the banking sector following moves by the Zimbabwe government (through the Department of Indigenisation and Empowerment) towards nationalisation or indigenisation of foreign-owned banks. The new bill on property rights states that all multinational companies, including banks operating in Zimbabwe, should compulsorily dispose of a stake of their shareholding to locals in a 51:49 ratio in favour of the locals. This has resulted in shareholders of Standard Chartered

Bank adopting a conservative stance evidenced by the withholding of foreign investment into the Zimbabwe subsidiary. Uncertainty about property rights has played a significant role in dampening investment in the economy (Business and Banking Survey 2006). Courts are a last resort for shareholders due to their ineffectiveness in protecting shareholders' rights and so multinational banks have experienced the absence of foreign participation, technology transfer and skills shortage because of intellectual capital flight. The financial services industry, and particularly the multinational banks, is on the verge of collapse -- together with shareholder investment.

- **Corruption**

The Zimbabwean banking sector has of late been plagued by a spate of corruption scandals involving junior and senior level management. As a result, banks such as CFX Bank Holdings were placed under curatorship and some, for example, Barbican, were closed. The Zimbabwean government enacted the Anti-corruption Commission Bill in 2003 to establish an independently powerful and high-profile body to spearhead the battle against corruption. This Bill provides mechanisms to investigate corruption at all levels and in all sectors, including the banking sector. Findings revealed that the enforcers in the banking sector tend to be on the forefront of corrupt activities which impacts negatively on the enforcement levels. In the December 2008 edition of *Zimbabwe Situation*, an editorial writer observed that: 'The RBZ Bank Licensing Supervision and Surveillance Chief has been exposed for the entire institution's duplicity, amid reports of his near 20% stake in NDH Bank Ltd - against bank regulation and general corporate governance. This is because the Zimbabwe Banking Act expressly discourages and prohibits the Reserve Bank of Zimbabwe from owning shares in allied businesses, which are subject to their routine scrutiny or checks for fear of subjective views on appraisals and under operational issues. The RBZ has also been accused by Non-Governmental Organisations (NGOs) of plundering unknown millions of United States Dollars from companies and charities' accounts to pay for elections in March and June 2008.'

According to the *Banks and Banking Survey 2006* edition, corruption in banks tends to be higher in countries with more heavy-handed supervision except in places with strong, independent legal systems and political institutions. Brutal supervisory powers exist in Zimbabwe. They are characterised by a disregard of the rule of law. Weak governance may invariably give officials more chances to 'help themselves.' To a greater degree, corruption has resulted in foreign shareholders' investments being at risk because the authorities responsible for monitoring and protecting these investments are the very same perpetrators of corruption.

Although laws on corruption exist, their enforcement is the greatest challenge because of the political immunity of such officials.

- **Institute of Directors Zimbabwe (IODZ)**

Standard Chartered Bank, as well as other multinational banks, are active members of the IODZ, a body with corporate governance that is gaining recognition in the country largely due to its efforts of promoting the principles set out in the Cadbury Report of UK, the King Report of South Africa and UK Code of Best Practice developed by the Commonwealth Secretariat and derived from the OECD's Corporate Governance Code. The IODZ is dedicated to improving the expertise, status and professionalism of managers and directors of Zimbabwean companies through training and education. It also seeks to curb fraud and corruption. The IODZ has set up a special purpose committee that prepares and disseminates guidelines on corporate governance. The IODZ is also responsible for monitoring compliance of governance principles of member organisations.

The IODZ has been active in boosting shareholders activism in Zimbabwe. Multinational banks are also members of the Bankers Association of Zimbabwe, which is a coalition of banks in Zimbabwe. These institutions actively seek to protect shareholder investment as shown in an article of the *Banks & Banking Survey 2006*: '.....sensing danger, the Bankers Association of Zimbabwe (BAZ) wrote a letter to the Reserve Bank of Zimbabwe Governor warning him of an

imminent collapse of the industry's heavyweights.' The Governor responded to their plea by announcing a new monetary policy stance. BAZ's efforts seem to suggest that, to some extent, they are influential in protecting their members as well as foreign shareholders investments in these international banks.

However, it was noted from the research that efforts of these institutions (IODZ and BAZ) are severely limited due to government's total disregard of the rule of law. In the end, their efforts are checked, making this mechanism less effective in protecting shareholders of multinational companies.

9. Conclusion

As shown above, the findings are not consistent with the hypothesis that the corporate governance mechanisms available to protect shareholders of multinational banks in Zimbabwe are effective.

The evidence suggests that, to a large extent, the legal framework for effective corporate governance existing in Zimbabwe is by virtue of laws related to Companies Act, Banking Act, and the various Codes. The problem, however, lies with enforcement which appears to be weak or non-existent, making the legal mechanisms highly ineffective. Shareholders of multinational banks in Zimbabwe are right to concern themselves with the legal protection of their investments and rights.

The banking sector appears generally to be over-regulated, volatile, risky, corruption-infested, and susceptible to political interference through takeovers by the government (nationalisation) or closure by the Central Bank at any time.

The judicial system and the Registrar of Companies are highly ineffective and incompetent to deal decisively and independently on commercial matters or disputes. This can be related to:

- backlogged courts due to shortages of staff
- politicisation and lack of independence
- a lack of judges with commercial expertise (ignorance of law) and hence incompetence
- corruption, and
- low remuneration.

The Central Bank has too much power at executive and supervisory levels, which is prone to abuse. This is to the detriment of the shareholders as well as the entire national financial system. Internally, the legal mechanisms and the structure of banks to protect shareholders are highly robust and effective. The CAC's effectiveness is limited to those entities with arbitration clauses in their Articles of Association. The legal mechanisms of corporate governance are being overtaken by events and new business developments in the commercial sectors of the economy. They are slowly becoming irrelevant and inapplicable.

10. Recommendations

- **Changes to the court system**
 - The monitoring and enforcement capabilities of the Registrar of Companies and courts need to be enhanced for better implementation of corporate governance and protection of foreign shareholders. Courts need to be capacitated with resources and technology. Judicial apparatus (courts) needs to be made independent, completely free of political interference.
 - The High Court judges need to be adequately remunerated to entice capable legal practitioners to leave their practices and become judges. This would increase personnel, reduce backlogs and speed up the resolution of commercial cases. Adequate remuneration will counter brain drain, will increase the level of morale among judicial personnel, and will reduce corruption. These measures will greatly improve confidence in the judicial system in Zimbabwe and in foreign shareholder protection. As a result, foreign direct investment will flow.

- There is also a need for legislative enactments or decrees that establish a regulatory agency and indicate its functions, including an enforcement process.
- There is a need for an effective and sound legislative framework for various aspects of corporate governance, including the protection of foreign shareholders of multinational companies in Zimbabwe.
- **Complementary institutions to the courts**
There is a need for complementary institutions to assist understaffed courts and policymakers. The effectiveness of the legal protection of foreign shareholders for providing the functions of corporate governance rest substantially on four additional institutions, namely:
 - i. **Social norms and judicial efficiency**
For social reforms to have an impact there is a need for social support. Laws must be consistent with social norms and obeyed out of respect. Where legal protection is inconsistent with social norms, it will simply be ignored. There is growing recognition of the interaction between behavioural patterns and legal institutions. New laws are not enough to stimulate financial restructuring: changing a culture is necessary.
 - ii. **Political structure and judicial efficiency**
For legal protections to have significance, there must also be the expectation that those laws will be followed. For the judiciary to be efficient, it must have an interest in enforcing the law. Such interest has been linked to political structures that limit the power of the sovereign relative to other interest groups in society.
 - iii. **Location of judicial authority and efficiency**
This refers to how government organises and allocates judicial authority. It is suggested here to provide information and lower the costs of enforcement, it may be optimal to delegate authority to a specific regulatory agency tasked with that job or even to allow that regulator to delegate further to private sector organisations.
 - iv. **Efficient collection of information**
With information, shareholders can use their powers embodied in legal protections to change the allocation of resources. There is also a need for the financial press to be empowered through freedom of expression, for example, to combat corruption and bribery cases in courts through the provision of such information.
- **Limit the executive and supervisory powers of the Reserve Bank of Zimbabwe**
As a regulator, the powers of the Reserve Bank of Zimbabwe must be capable of being checked and limited. This is to avoid abuse and corrupt tendencies by officials from the Central Bank. Laws or guidelines need to be enacted that govern the Reserve Bank of Zimbabwe and an independent committee established to supervise the Central Bank and put in checks and balances.

The delegation of roles and responsibilities to other market regulators also increases the efficiency and independence of the Central Bank and, at the same time, protects foreign shareholders from politicisation of the Central Bank. There is a need for legislative enactment or a decree to establish a regulatory agency with functions that include enforcement powers.
- **Ministry of Industry and International Trade needs to revisit legislation**
It is recommended that the Industrialisation Bill be considered for removal as it has contributed immensely to dampening foreign direct investment as it has caused insecurity among foreign shareholders about their investment. To attract foreign direct investment and stimulate the banking sector and other sectors of the economy, the Ministry needs to consider enacting laws that favour multinational companies and assure protection of investments.

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- **Government needs to abide by the rule of law**

Through its various ministries, for example, the Ministries of Industry and International Trade, Justice, Legal and Parliamentary Affairs, the Zimbabwean government should consider adopting and upholding the rule of law and court decisions. The government needs to abide by the rules of the Constitution. The rule of law helps to attract foreign direct investment, increase shareholder investment and protection, promote activism in the economy and offer a safe haven for foreign shareholder investment. This will greatly help to resuscitate all sectors of the economy, including the banking sector, which happens to be key in financial intermediation. There is a need to strength the enforcement mechanisms of regulatory instruments and the judicial system to restore shareholder confidence in the rule of law (CIPE, 2001). Government needs to show political will by committing time and money to the processes and structures of protecting multinational companies and their shareholders.
 - **Multinational Companies' Shareholder Associations**

These will in spearhead pressure on the government to protect directors' shareholders' rights and increase shareholders' level of activism in the economy.
 - **Rules and regulations (Acts and Codes)**

There is a need to amend the statutes governing corporate governance in Zimbabwe, that is, the Companies Act (Chapter 24:03), as revised in 1996, and the Banking Act of 1996. These should be updated to include more contemporary business issues and problems in Zimbabwe, especially those affecting foreign shareholders and their protection.
 - **Community watchdogs**

The establishment of strong monitoring and watchdog organisations on corporate governance and shareholder protection can also be an effective legal protection mechanism capable of protecting shareholder value and investment.

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