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An Assessment of Corporate Governance Practice in Private Commercial Banks of Ethiopia: Case of Wegagen Bank

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ABSTRACT: Many academics have looked at the factors that influence economic behavior and their impact on economical decision, particularly cognitive bias. Dealers are often unaware of their prejudices and assumptions. If investors are aware of the prejudices they might face, they are greater likely to act rationally. to board and senior management to govern the bank. As banks are the backbone of a nation's economy, they need to implement sound corporate governance. In Ethiopia, most of the banks are private, but information on their corporate governance practices is limited. This study was designed to assess corporate governance practice in Wegagen Bank. Data were collected via questionnaire from board and senior managers, and from documents and analyzed using SPSS. Corporate governance like board size, BODs meeting and composition, role separations between CEO and board chairman, identifying and reviewing business risks, qualification of audit committee, competence of auditors, equal treatment of shareholders, strategic objectives and ethical standards were in line with codes of good corporate governance practices. However, the bank has showed some deviations and should comply to codes of good corporate governance practices in audit committee composition, auditors' independence, internal auditors' access to board chairman/audit committee, shareholders' knowledge and exercising their rights, transparency about influential shareholders, lack of remuneration committee, CEO ownership concentration, directors pay/incentive.

KEYWORDS: Board of Directors, Corporate governance, Companies, Ethiopia, Wegagen Bank.

I. INTRODUCTION

Corporate governance is a broad concept which defined differently by different scholars[1]. It was The mechanism that directs and controls businesses is known as the command and management network. It refers to the processes, guidelines and laws that lead companies in the way they performance, administer and control their operations[2]. The rules, methods, and execution of the company's agreements with its owners, lenders, workers, vendors, consumers, and government are described as governance practices. Corporate governance can be defined by the Central Bank as the procedure and framework used to develop and control a bank's, insurer's, or microfinance institution's business and affairs in order to improve biz wealth and responsibility, with the ultimate goal of act recognizes stockholder value and other stockholders' interests . It seems that a corporate governance system can be defined as a more-or-less prevailing country-specific framework of legal, organizational and cultural factors affecting the ways take holders influence managers decision[3].

In companies with dispersed ownership, shareholders are usually unable to watchfully monitor management so that Business management supplies them with guidelines and regulatory tools via that they may monitor management' choices [4]. Legatees of corporate governance comprise banks, investors, suppliers or public as a whole. Shareholders have more faith in organizations with strong company management, smooth operations of the overall business, higher investment opportunities and access to cheaper debt[5].

In banking, The attribution of power and responsibility to the board members and senior leadership to oversee a bank's different concerns is referred to as corporate administration. It is of great relevance not only to individual banking but also to international financial systems[6]. Effective corporate governance practices pave the way to gain and sustain public trust and faith in the financial sector that enhances the proper operation of banking sector and the entire economy. On the other hand, poor corporate governance deteriorates the ability of banks to properly manage their assets and liabilities resulting in financial crises and scandals. Global corporate failures like Enron, WorldCom, HealthSouth and Arthur initiated many countries to have compulsory norms and guidelines to strengthen corporate governance framework[7].

In the past two decades, banking becomes a fast-growing financial service sector in Ethiopia though the first bank, called Bank of Abyssinia, was inaugurated in 1906[8]. By December 2020, there were 18 different banks with around 2357 branches across the country. There are also banks in the process of establishment. Most of the banks in the country

are private banks and few of them are government owned[9]. As banking institutions are the backbone of a nation's economy, They must apply excellent company management to improve outreach, openness, integrity, durability, prosperity, effectiveness, efficacy, accountability, and adaptability to a changing market [10]. In sound corporate governance, rights and responsibilities are allocated based on rules and procedures to various corporate stakeholders: the board, managers, shareholders, creditors, auditors, regulators and customers. The majority of study findings revealed a favorable link between corporate management and business success. According to a research done on banks functioning in 7 Arab World nations, there is a strong relationship amongst organisational integrity and bank profitability. In Ethiopia, there is a favorable association among corporation management procedures and private sector banks economic success. Similarly, three dimensions of corporate governance had influenced the performance Bank of Abyssinian Ethiopia[11]. Though corporate governance is vital for corporate businesses, information on sound corporate governance practices is limited in Ethiopia banks in generally, and in specifically, banking companies. Scientific investigation is important to adopt sound corporate governance practices that commensurate with their size, complexity and risk profiles of banking organizations in the country. However, corporate governance is the least studied area of management especially in developing economies like Ethiopia. Thus, this study was designed to assess corporate governance practice in Wegagen Bank, a private commercial banks in Ethiopia. The attribution issue that occurred when a company's owner separated out of its management in the event of big and complicated enterprises gave rise to the concept of corporation administration. due to lack of the skills necessitating to hire managerial specialists. The responsibility of controlling management shifts from owners to the directors (agents) of the companies. However, A corporation 's board might utilize their management role to benefit their personal interests rather than the shareholders'. As a result, governance were established to guarantee that the agents of the business's ownership exercise control over the organization in ways that benefit the company's business. Companies should follow a recognized local or global corporate governance code to attract investors and enable stakeholder's greater access to information about the corporation. Many countries have adopted corporate governance codes of best practices that may need to be revisited, improved, and revised in accordance with dynamic business environment. For instance, the National Bank of Ethiopia (NBE) issues Corporate Governance Directives for financial institutes including commercial banks. Generally, The business administration regulations create standards and proper regulatory tools for stakeholders to monitor management actions. In corporate governance practice, senior managers manage day-to-day operations, decide on policies and measures related to business execution, create necessary infrastructure like ICT, oversight policies and procedures. They are responsible for directing; planning and controlling work and take necessary corrective actions as well as should manage risk and provide accurate information As a supervisory body for an industry's executive leadership, a professional board of directors is essential. Generally, board members encompass executive directors, non-executive directors and independent directors. The executive director may be General Director, Executive Board member or manager of the company who is not an Executive Board member, all holding an executive position in the company. Independence Governors must not have been the Managing Manager, the Foreign Manager, or a member of the Executive Board. Non-Executive Boards are Supervision Board member who do not occupy any executive positions in the organization. As a guideline, at least 1/3 of the board should be non-executive, mostly consisting of Independent Directors, and most studies have shown that the ideal amount of autonomous directors would be around 1/4 and 1/2 of the entire board size. The roles and responsibilities of a Board of directors differ depending on the nature of organizations and the laws applied in various countries. The executive board is in charge of establishing plans and policies, as well as overseeing the organization and acting as the guardian of the owners' interest. National Bank of Ethiopia described that the board of a bank, an insurer or a microfinance institution shall at least be responsible for establishing clear policies for shareholder relations and at least annually reviewing and approving strategies, policies, procedures/guidelines, annual business plans and budgets; and monitoring management's performance in implementing issues by setting key performance indicators. Board behaviors that affect its effective performances include Board structures, Board processes and Board committee. Board structure includes board size, composition, leadership and the information within board structures. The size of the board influences the degree of supervision, controlling, monitoring, and decision making in a firm. The ideal board size is nine according to and a bank should also have at least nine directors. Board size may have positive or negative impact on corporate governance performance according to and, respectively. Board processes is the behavioral dynamics of the Board that comprises Cohesion, cognitively conflict, emotional confrontation, communication quality, work standards, trust, and information and skills utilization are all factors to consider. Board committees; commonly Nomination, Compensation/Remuneration and Audit Committees are part of internal corporate governance mechanisms formed according to policies, rules and procedures laid down by the board to ensure the best interest of the stakeholders. Fears about method of appointing directors of Directors prompted the creation of appoint commissioners, whilst the audit team is an anti - anti of the management board dealing with monitoring and reviewing financial statements of a firm to ensure the interests of shareholders. Formation of remuneration committee is mainly linked with the Concerns about pay transparency, excessive salary, and the perception of a weak relationship among achievement and compensation.

II. LITERATURE REVIEW

C. W. Anderson and T. L. Campbell [12] stated the outside and inner company management activities that Japanese banks engaged in between 1985 and 1996. External oversight

seems to be dormant, and there have been few mergers, collapses, and other change in management and control since the 1990s financial crisis. We found no link amongst banking profitability and CEO turnover prior to the financial crisis. In the 1990s, however, non-routine bank president turnover was negatively connected to all stock returns and profitability. As a result, internal governance activity may be seen after the start of the Japanese financial crisis, a time marked by passive external governance and regulatory tolerance.

T. G. Arun and J. D. Turner [13] proposed the This is a serious concern, given the crucial role that institutions serve in developing countries' economic institutions and the various banking reforms that those countries have adopted. According to the authors, banking changes can only be incorporated if a prudent supervisory system has been established, based on a theoretical examination of bank corporate governance. The privatization of banks is an important aspect of banking reform in developing countries. Corporate governance changes, we believe, might be a need for the effective divestment of government ownership. Furthermore, we believe that increasing rivalry brought on by international banks may help developing-country banks strengthen their corporate governance. D. E. A.O., A. T.O., and O. A. J [14] stated the strategies for theft protection in the banking business are examined in this paper. This research relied on primary data. The data for this research was gathered from 15 Nigerian commercial banks that were publicly traded as of December 31, 2015. The simple minimum square regression model was used in this investigation. Strong internal control systems, effective corporate governance, and adherence to banking ethics have all been shown to have a positive and substantial impact on fraud prevention in the banking business. This suggests that putting the factors of this research into practice will minimize fraud, mistakes, and misappropriations in the banking industry. Banking institutions should create and assure effective and tight application of all of these elements in order to avoid fraud, mistakes, and misappropriation, according to the report.

Research question

- How corporate governance practice perform in banks?

III. METHODOLOGY

A. Research design

The study used descriptive and opinion survey research method based on primary and secondary data. The target population of the study was all Ethiopian business institutions that are privately held and have a framework that enables for the examination of corporation control efficiency. Purposive sampling technique was employed to select Wegagen bank depending on the amount of period it has being in existence from the targeted private bankers, modicum of required and the accessibility of board members and management of the banks. Because material concerning the bank's business control structure was organized and made accessible to the board of governors and top managers at the top, nine participants consisting the board of directors and senior executives were considered for the study. Data were collected from 01 November to 30 December 2020.

B. Data collection

For both the non-director upper leadership category and the Board, responses ranged in age from 39 to 70 of the bank meeting the minimum age (30) put forward in directive issued by the NBE. In terms of level of education and work experience, all of the Board of Directors (BODs) had Master's Degree and served for at least 10 years as shown in Table 1.

Table 1: Illustrating the Years of work experience of the respondents.

Experience in years	10-20	21-25	26-30	More than 30	total
Number	2	1	3	3	9
percent	22.2	11.1	33.3	33.3	100

Having a firm grasp of their position in company management. The study showed that the BODs of the bank were well experienced with at least 10 years of service. Experienced Board of BODs can add value to effective corporate governance, effectively establish strategic objectives and monitor its performance against challenges of a dynamic business environment.

C. Data analysis

Primary data were collected via questionnaire from the board and senior managers whereas secondary data on professional profile of board were gathered from company's documents. Questionnaire (in English) was developed based on the current corporate governance frameworks, the Basel committee for financial oversight, and the OECD's corporate governance evaluation matrix The Statistics Software for Scientific Biosciences version 20 was used to analyze the data. Before collecting data, the validity of the questionnaire was tested on five employees of the bank and Cronbach's alpha score varied from 0.833 to 0.911, all higher than 0.70.

IV. RESULT AND DISCUSSION

The size of the BODs of the bank was 9 which is within the range (8 to 16) suggested by many codes of practices. It has been reported that board size can affect the performance of firms [36]. All of the BODs of the bank were outsiders with no executive directorsin line with most Best standards advise that the bulk of governors be chosen from the public a company to minimize any conflicts of interest. All respondents expressed the existence of unitary system indicating the separation between the role of chairman and CEO in line with recommendation in codes of best practice like Cadbury Code of Best Practice [37]. Hundred percent of the respondents pointed out that the board was strong enough to identify the risks inherent in the business. They also added that the board regularly reviews the nature of the risks in light of the changing internal and external business environment indicating they were dedicated to the success of the bank.

The auditing board were made up entirely of non-executive

directors, according to four fifths of responders (80%) in line with theories and principles of corporate governance including OECD and Basel committee that suggest the majority of audit committee should non-executive directors of the banks. All of the respondents indicated that the Audit committees possessed necessary financial background while 60% of them said significant financial pronouncements of the bank have been thoroughly reviewed as suggested by OECD. The majority of the respondents (80%) said that auditors of the bank were competent and independent while the remaining 20% said the auditors were competence but not independent. This urges the bank should allow auditors to act as stressed by the Basel Committee. Forty percent of the respondents said internal auditor's had no direct access to board chairman and audit committee against .Smith guidance and OECD principles of corporate. 22, 55.6 and 22.2 percent of the respondents indicated that all, most and very few of shareholders know their rights and obligations, respectively indicating these factors might not well communicated against the OECD principles of corporate governance. The majority of the respondents (66..7%) expressed that shareholders may openly use their voting rights, partake in the gross income, and attend public sessions whereas 33.3% of them replied shareholders rarely exercise their rights. But, OECD and Basel committee emphasize that the rights of the stakeholders should be ensured and protected by law. Eighty percent of the respondents rated the shareholders' degree of discharging duties and their responsibilities as "high" or "very high" but 20% of rated as "low" which might be due to lack of information that negatively impact the BODs. However, all respondents pointed out the existence of equal treatment of shareholders of the bank in line with directives of NBE and OECD principles. Regarding influential shareholders, the respondents expressed it is confidential and directed to the top five shareholders as shown in Table 2. This lack of transparency in the corporate governance is contrary to banking business proclamation No.592/2008 issued by NBE that indicated the maintained register shall be open to the public and the influential shareholders are those with hold at least 2% of the total shares of that bank.

Table 2: Illustrating the Influential shareholders and percentage of the total share.

Category of Influential share holders	Percentage of the total share
A(1STTop holder)	(5%)
B (2ndtop holder)	(3.8%)
C(3rd Top holder)	(1.8%)
D(4Th Top holder)	(1.6%)
E(5th Top holder)	(1.5%)

All respondents expressed that the BODs effectively established Set strategic goals for itself, as well as corporate values and ethical standards, senior managers andother employees, and communicated efficiently as indicated by codes of best corporate governance practices. They also added the plans and objective were clearly stated. All the respondents indicated the absence of any The BODs as a group have power over the salary of the CEO, which is handled by a commission specially created for that aim. The boards, on the other hand, is required by OECD business management standards to develop a pay strategy for platform members and senior managers. with respect to remuneration and performance. Concerning the ownership concentration of the CEO, 40%, 40% and 20% of the respondents indicated that the CEO'S holding is larger than other shareholders, same to other shareholders and null, respectively. CEO ownership is usually related to operating performance and can be taken as good governance asit plays a role in mitigating agency problems. All the respondents indicated that audit committee members/chair have specialized in Management (40%), Economics (20%) or Accounting (40%)plus certificate in specialized areas of business such as ACCA and insurance implying they had appropriate backgrounds compatible with their duties as recommended by Basel committee and Sarbanes-Oxley. The outside accountants are suggested by the boards of managers, according to the majority of responders (80%) and approved byof the general meeting of shareholders. The remaining 20% of the respondents indicated that shareholders directly elects the external auditor. In both cases, final approval is made by NBE. This practice goes with OECD and Basel committee that emphasize external auditors need to be recommended by an independent audit committee of the board/an equivalent body and that external auditors are appointed either by that committee/body or by the shareholders' Sixty percent of the respondents said the nominating panel has been charged with leading/chairing the director nomination procedure and offering suggestions to the boards , but 20% replied nomination process of directors is led by external auditors and the other 20% indicated that the process is led chairman of the board. Eighty percent of the respondents replied that the directors pay and performance has been fairly comparable other similar banks, but the rest said not comparable. OECD requires that payment to the Directors should be determined based on company's earned return and relative to that of a comparator group. Similarly. 80% of the respondents indicated that targets were set for bonuses/ for outstanding performance in accordance of OECD principles. Regarding how often the BODs of the bank meets, 40%, 20%, 20% and 20% said the BODs meets every week, every 15 days, every month and as required, respectively. The panel must convene adequately often to fulfill its obligations efficiently, as stated by the Combined Rule, although research suggests that boards should weigh the expenses and advantages of about regular frequency. All the respondents replied remuneration of BODs was determined based on the annual profit of the bank; usually 5% of the net annual profit together with additional monthly allowance payments. It is suggested by the boards of management and must be approved by the owners in a public session. However, according to resolution passed in 2011 by NBE, the annual remuneration shall not exceed 50,000.00 Birr for all commercial banks which can affect the motivation of directors as all the respondents indicated that the compensations are not sufficient and attractive compared

to the high annual profit generated by the bank. Moreover, the Directors were compensated by cash only though researches showed Share choices must also be granted because they offer motivation for panels to operate the company in a manner that matches their interests with objectives of the stakeholders, allowing them to make greater successful strategy choices and avoid the agencies issue.

V. CONCLUSION

Wegagene bank showed strengths in some corporate governance practices and weakness in others. Corporate governance practices of the bank was mainly set to meet the directive issued by the National Bank of Ethiopia (NBE). Corporate governance practices of the bank like board size (9), BODs being outsiders or non-executive directors, separation of roles of CEO and the chairman of the board, Board strength in identifying and reviewing business risks, the majority of audit committee being composed solely of non-executive directors, reliable financial background of the audit committee, presence of competent auditors, equal treatment of shareholders, effectiveness of BODs in establishing strategic objectives and setting corporate values and ethical standards, educational qualification of Audit committee, appointment process of External Auditors and regular meeting of BODs were in line with the directives of NBE, and codes of practices indicated by others like OECD Corporate management standards, the Basel Committee on Banking Oversight, Sarbanes-Oxley, and so on. However, the bank has showed some deviation from the recommendation forwarded by OECD, Basel committee and the like in terms of the composition of the audit committee (executive and non-executive directors), auditors' independence, Internally accountants have direct access to the chairman of the board and the audit team, shareholders' knowledge of their rights and obligations and exercising rights, lack of transparency with respect to influential shareholders, lack of remuneration committee in general and for ECO (Economic Cooperation Organization) in particular, relative ownership concentration of the CEO, directors pay and setting for bonuses/incentive. So the bank should strengthen its efforts to maintain its strong aspects and improve its weak aspects of corporate governance practices in accordance to the widely recommended and accepted principles and guidelines.

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