

ASIAN DEVELOPMENT BANK

TAR:BAN 36197

TECHNICAL ASSISTANCE

TO THE

PEOPLE'S REPUBLIC OF BANGLADESH

FOR PREPARING THE

FINANCIAL MARKETS GOVERNANCE PROGRAM

December 2003

CURRENCY EQUIVALENTS

(as of 2 December 2003)

Currency Unit	–	taka (Tk)
Tk1.00	=	\$0.0172
\$1.00	=	Tk58.15

ABBREVIATIONS

ADB	–	Asian Development Bank
CMDP	–	Capital Market Development Program
CSE	–	Chittagong Stock Exchange
DLS	–	domestic legal specialist
DSE	–	Dhaka Stock Exchange
FD-MOF	–	Finance Division, Ministry of Finance
FIS	–	financial institutions specialist
FMGP	–	Financial Markets Governance Program
GDP	–	gross domestic product
IAS	–	international accounting standards
ICAB	–	Institute of Chartered Accountants of Bangladesh
ICB	–	Investment Corporation of Bangladesh
I-PRSP	–	interim poverty reduction strategy paper
ISA	–	international standards on auditing
NBFI	–	nonbank financial institution
SEC	–	Securities and Exchange Commission
STAS	–	securities training and accreditation specialist
TA	–	technical assistance
TL-FMGE	–	team leader-financial markets governance expert

NOTE

In this report, "\$" refers to US dollars.

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I. INTRODUCTION

1. Despite earlier efforts to resuscitate Bangladesh's ailing financial markets, the level of investment mobilization has remained low and the market has remained largely underdeveloped. This situation is traceable mainly to the low level of investor confidence associated with poor market governance and the consequent negative perception of investors. In a continued effort to strengthen and deepen the financial system for mobilizing resources for private sector-led economic growth, the Financial Markets Governance Program (FMGP) was included in the Country Strategy and Program Update of the Asian Development Bank (ADB) as a firm loan project for 2004. An ADB Mission visited Dhaka in July 2003 to undertake fact-finding for the technical assistance (TA) in preparation for the FMGP loan. Understanding was reached with the Government of Bangladesh on the objectives, scope, cost estimates and financing plan, implementation arrangements, and terms of reference of the proposed program preparatory TA.¹ The summary initial poverty and social analysis of the TA is in Appendix 1.

II. ISSUES

2. The Capital Market Development Program (CMDP)² made significant progress in strengthening regulations and establishing the supervisory structure for the capital market, developing the basic market infrastructure, and laying down the foundation for the legal and institutional framework to support capital market development. The future growth and development of the financial markets require that the continuing low level of investor confidence and underlying impediments to increased investments be addressed. Weak governance impedes market development and gives rise to inefficiencies in financial intermediation. Systemic issues in the domestic financial markets include weak enforcement, poor corporate governance, slow development of the market infrastructure, and low level of capacity of major market players.

3. The general observation is that governance structures are deficient, and market regulators have ineffective enforcement and weak implementation capacity. Regulations were introduced under the CMDP, but recurring violations of securities laws and regulations have been reported. The absence to this day of any convictions in cases filed in connection with the 1996 stock market scams has reflected the lack of credibility and effectiveness of the Securities and Exchange Commission (SEC) as regulator. SEC has problems recruiting private sector professionals due to its low pay scales. Its dependence on the national budget and lack of financial independence constrain its ability to attract qualified professionals to its ranks. To improve its credibility and profile, SEC must be seen as a competent authority with adequate autonomy and free from external interference, with clear mandate to carry out its tasks.

4. Public trust in the two stock exchanges, Dhaka Stock Exchange (DSE) and Chittagong Stock Exchange (CSE), is low. A large number of member firms of the exchanges have limited capitalization, weak governance structures, and inefficient operations. The market is mooted the merger of the two exchanges, with merely 323 companies listed, as more cost-effective than having separate exchanges—it will remove duplication of efforts and allow optimum use of scarce trained human resources among the exchanges themselves, the brokers, and the regulator. Furthermore, separating ownership from membership in the stock exchanges through

¹ The TA first appeared in *ADB Business Opportunities* (Internet edition) on 22 April 2003.

² ADB. 1997. *Report and Recommendation of the President to the Board of Directors on a Proposed Loan to the People's Republic of Bangladesh for Capital Market Development Program*. Manila (Loan 1580-BAN, approved on 20 November 1997 for \$80 million). The program completion report on the loan, circulated to the Board in August 2003, recommended that gaps and weaknesses in governance be addressed in future ADB assistance.

demutualization is being considered by a number of market participants as a more effective way of reducing potential conflicts of interest and improving governance of the exchanges. However, practical difficulties arising from vested interests of exchange members who desire to keep their seats or resist change in long-established modes of operation have to be addressed as well as the potential conflict of regulation versus commercial interest in a demutualized environment.

5. The state-owned Investment Corporation of Bangladesh (ICB) remains the single largest integrated capital market operator. While ICB has transferred its brokerage license to its stock brokerage subsidiary, it continues to operate as a merchant banker and manager of its existing mutual funds. Conflicts of interests are inherent in ICB's operations as owner, operator, and self-regulator. As a matter of practice, the ICB mutual funds borrow to finance equity investments, while privately managed funds are forbidden from doing so. Unlike private mutual funds, ICB mutual funds are not regulated under the SEC rules and ICB is not required to submit performance reports. Since ICB operations also lack transparency, its actual performance and financial position are subject to conjecture.

6. Nonbank financial institutions (NBFIs) face uneven competition with the banks. Commercial banks are permitted to undertake leasing operations, but leasing companies cannot obtain a banking license. NBFIs are not given tax exemption for provisioning for nonperforming assets, which is enjoyed by banks. Under SEC regulations, banks are allowed to be merchant bankers, managers of public issues, underwriters and managers of mutual funds, giving rise to potential conflicts of interests. Experience also shows inherent dangers in commercial banks undertaking investment banking functions or investment banks managing mutual funds, while appropriate checks and balances are not in place and supervision remains relatively weak. Comparable conditions are necessary to ensure fair and effective market competition and to promote greater private sector participation in resource mobilization.

7. On the other hand, listed companies lack transparency and rules are perceived to favor majority shareholders to the detriment of minority shareholders. Financial statements do not reflect the true financial condition of corporate entities and do not provide a reliable basis for informed decision making as they still do not fully comply with international accounting standards (IAS) and are not audited according to international standards on auditing (ISA). As of end-April 2003, the Institute of Chartered Accountants of Bangladesh (ICAB) had adopted only 8 of the 34 IAS and 14 of the 46 ISA. However, ICAB does not have the authority to regulate the accounting profession and to ensure that such standards are followed and disclosure norms are faithfully complied with.

8. Investments are highly retail in nature in the country and investors have limited recourse for redress of grievances. Investors are also apparently unaware of their rights and obligations under existing rules. Appropriate investment vehicles, as well as investment mechanisms, that could operate effectively within the existing financial system still have to be explored.

III. THE TECHNICAL ASSISTANCE

A. Purpose and Output

9. The TA will help prepare a sector development program that will underpin the FMGP for promoting good governance in the Bangladesh financial markets to raise investor confidence and enable Bangladesh to compete effectively for funds in the international markets and to encourage greater investments in its domestic market.

B. Methodology and Key Activities

10. The TA will focus on (i) strengthening regulatory and supervisory capacity; (ii) improving governance and operations of market intermediaries; (iii) strengthening corporate governance and public disclosures; (iv) raising accounting and auditing standards to comply with international norms; and (v) enhancing market knowledge, institutional capacity, and skills of market participants. Findings and recommendations from previous and ongoing TAs of ADB and projects of the World Bank and other donor agencies on these areas of focus will be reviewed.³

11. **Strengthening Regulatory and Supervisory Capacity.** To strengthen the enforcement capability of SEC, first, it must be vested with full powers to investigate, levy penalties, and impose administrative sanctions, including laying down cease-and-desist orders, and must have other means to address malpractices in the financial markets. SEC's powers, and ability to secure information, investigate and pursue criminal and civil cases against wrongdoers will have to be reviewed based on best practices and the provisions of local laws and rules. Second, SEC's capacity to regulate and supervise the domestic capital market needs to be improved. The proposed TA will also review SEC's rule-making process and procedures to ensure appropriate stakeholder consultation when new laws are drafted or existing laws amended, and to recommend improvements to ensure greater transparency and adequate market participation and ownership. Considering best practices, the proposed TA will review the current structure, analyze alternative measures for achieving greater autonomy particularly in SEC's decision-making process, and make suitable recommendations.

12. To upgrade the quality of its staff, SEC should provide competitive compensation and benefits to attract experienced professionals and therefore may deviate from the civil service pay scale and civil recruitment policies. SEC can have its own sources of revenues (possibly from fees, penalties, contributions, etc.) to enhance its independence from the government budget. The proposed TA will review the funding, income, and salary practices of other security and exchange regulators in the region to provide useful models and recommend alternatives for the Bangladesh SEC.

13. **Improving Governance and Operations of Market Intermediaries.** This component will consider improvements in the governance structure of the two stock exchanges and analyze the advantages and disadvantages of demutualization as well as of merging the exchanges. Suitable recommendations will be made for more efficient operations and more effective intermediation functions. How best to promote institutional investments and strengthen the operations of NBFIs will also be analyzed.

14. Reforming the mutual funds industry entails addressing the role of ICB, which continues to be an impediment to increased institutional investments due to its entrenched privileges. In the interest of transparency, an IAS audit of ICB should be conducted to reflect its true state of operations and financial position. Depending on the findings, the Government may undertake remedial measures to strengthen governance and eliminate potential conflicts of interest. That will involve the valuation and transfer or sale of assets and liabilities. The fully separated ICB units and its subsidiaries will have to be brought within the scope of SEC regulations. Ultimately, the question of whether the Government is justified to continue to engage in such commercial

³ ADB has been the main aid institution in financial markets. The World Bank has an ongoing Financial Institutions Development Project with focus on developing term financing on a sustainable basis using NBFIs. As part of this loan, technical assistance is provided to SEC to develop issue rules for bonds and debentures. The World Bank also provided training to ICAB in development of accounting and auditing standards in Bangladesh, which was completed in 2002.

operations as ICB does will be revisited. Mutual funds industry regulations will also be reviewed to identify impediments to the industry's accelerated development.

15. For improved governance of NBFIs and their future role in the Bangladesh financial market, the scope of their operations and the regulatory environment need to be clearly drawn. Comparable conditions should be ensured by making incentives and market access uniform across different financial institutions. In this way, market competition will be enhanced. The TA will review current laws and regulations pertaining to banks and NBFIs and their merchant banking, securities dealership, asset management, and leasing operations; and assess the adequacy of safeguards against conflicts of interest. The TA will also support, through policy dialogue and stakeholder consultations, the introduction of a legal framework for secured transactions and transparent electronic registry for movable assets.⁴

16. **Strengthening Corporate Governance and Public Disclosures.** Corporate governance will be strengthened by adopting best practices on (i) the structure of the boards of directors and the role of independent directors; (ii) protection of minority shareholders; (iii) transparency; (iv) setting up a commission to revise the Companies Act 1994; and (v) formulating a code of corporate governance. Some provisions in the Companies Act 1994 must be reviewed: independence and responsibilities of board members; management accountabilities; internal controls; shareholders' rights and protection of minority interests; and disclosure requirements. Considering the recommendations in the ADB advisory TA,⁵ the proposed TA will review amendments to the Companies Act and other legislative and regulatory amendments, assess corporate governance structures and practices in Bangladesh, and help formulate an action program for corporate governance reforms.

17. **Strengthening Accounting and Auditing.** The accounting and auditing component has three elements: (i) phased adoption of IAS and ISA and how it can be expeditiously carried out, (ii) setting up an accountancy board to implement and monitor compliance with international standards, and (iii) strengthening ICAB to enable it to operate as a self-regulatory body. It is proposed that the accountancy board be responsible for accrediting accounting practitioners and auditing firms and for enforcing professional standards and ethics. The TA will look at comparative practices and will coordinate with the World Bank's program to enact a new Financial Reporting Act, amend accounting and auditing provisions of related laws, enhance the capacity of regulatory agencies and professional bodies, and improve the programs in accounting and auditing of training institutes (including universities and colleges).⁶

18. **Enhancing Market Knowledge, Institutional Capacity, and Skills of Market Participants.** To upgrade the know-how of market participants, including company directors, in discharging their responsibilities, the TA will assess (i) the feasibility of setting up training facilities or (ii) using existing facilities for the purpose. In case (i), the alternatives are individual training facilities at the stock exchanges or SEC and a common Financial Markets Institute that may be attached to an educational institution. In support of skills development, the following merit attention: (i) assessing priority skills needs of financial market institutions (NBFIs, merchant banks, securities firms, and asset management companies); (ii) syllabi for various skills development courses, including seminars on roles, duties, and responsibilities of company

⁴ ADB. 2003. *Technical Assistance to the People's Republic of Bangladesh for Supporting Good Governance Initiatives*. Manila.

⁵ ADB. 2000. *Technical Assistance to the People's Republic of Bangladesh for Capacity Building of the Securities and Exchange Commission and Selected Capital Market Institutions*. Manila.

⁶ Part of the action plan under the World Bank-International Monetary Fund joint initiative Report on the Observance of Standards and Codes.

directors; (iii) institutional arrangements for sustainable offering of courses; (iv) the certification process; and (v) a program for promoting investor awareness that SEC, the exchanges, and other institutional players can undertake. In the final analysis, a knowledgeable, responsive market is the best assurance that market players conduct themselves properly and exercise good governance.

C. Cost and Financing

19. The total cost of the TA is estimated at \$690,000 equivalent comprising of \$496,000 in foreign exchange and \$194,000 equivalent in local currency. ADB will finance \$550,000 equivalent, covering the entire foreign exchange cost and \$4,000 equivalent of the local currency cost. The TA will be financed on a grant basis by ADB's TA funding program. The Government will contribute the balance of the local currency cost equivalent to \$140,000 in kind for office space and facilities, counterpart staff, local transportation, and administrative and secretariat support. The cost estimates and financing plan are in Appendix 2. The Government was advised that approval of the TA does not commit ADB to finance any ensuing program or project.

D. Implementation Arrangements

20. The Finance Division of the Ministry of Finance (FD-MOF) will be the Executing Agency for the TA. The FD-MOF will assign full-time counterpart staff to work closely with the TA consultants and will coordinate support needed to implement the TA. A steering committee, chaired by the Finance Secretary will be set up. Members will be from the Ministry of Commerce, Planning Commission, SEC, Bangladesh Bank, and private sector institutions including ICAB, professional bodies, and chambers of commerce and industry. The committee will meet bi-monthly, or more frequently as needed, to monitor and guide TA implementation.

21. Implementation will cover 5 months, starting in January 2004 and with completion in June 2004. A team of consultants from a firm will provide 21 person-months of consulting services (13.5 international and 7.5 domestic). ADB will select and engage the consulting firm in accordance with the *Guidelines on the Use of Consultants* and other arrangements satisfactory to ADB for engaging domestic consultants. The quality-based selection method for selecting the consulting firm will be used because the program is complex covering several subsectors, debt and equity markets, and market participants. Furthermore, the issues are highly sensitive and will require high-level policy interaction with government officials and extensive consultations with other stakeholders, particularly aid agencies, in the field. Selected consultants will have a high level of credibility and competence. Consultant selection will use a simplified technical proposal. Equipment procured will be in accordance with ADB's *Guidelines for Procurement*. Outline terms of reference are in Appendix 3. The consultants will submit to FD-MOF, the steering committee, and ADB an inception report 3 weeks after TA starts, a midterm report at the end of the third month, a draft final report 3 weeks before TA completion, and a final report on TA completion. The recommendations of the draft final report will be discussed at a tripartite meeting. A workshop will be held to present TA outputs.

IV. THE PRESIDENT'S DECISION

22. The President, acting under the authority delegated by the Board, has approved the provision of technical assistance not exceeding the equivalent of \$550,000 on a grant basis to the Government of Bangladesh for Preparing the Financial Markets Governance Program, and hereby reports this action to the Board.

SUMMARY INITIAL POVERTY AND SOCIAL ANALYSIS

A. Linkages to the Country Poverty Analysis

<p>Sector identified as a national priority in country poverty analysis? Yes</p> <p>The interim poverty reduction strategy paper (I-PRSP), entitled A National Strategy for Economic Growth, Poverty Reduction and Social Development, dated December 2002, reflects Government's strong commitment to poverty reduction, and notes the various means of targeting different sectors for achieving this goal. The I-PRSP notes : "A sound and well functioning financial system is required for ensuring growth and providing access to financial resources to the poor." Poor governance, lack of discipline, and inadequate disclosure and transparency are fundamental problems afflicting the financial sector in Bangladesh.</p>	<p>Sector identified as a national priority in country poverty partnership agreement? Yes</p> <p>The poverty partnership agreement was signed in 2000 with the Government of Bangladesh aimed at reducing both income and human poverty over the medium term (2005) and the long term (2010). ADB's strategy includes continued support for developing basic physical and social infrastructure, with more emphasis on governance and environment issues. A noticeable contribution to poverty reduction is envisaged through improved macroeconomic management including integrated efforts to improve governance, resulting in key policy and institutional changes to increase private sector participation and improve sector efficiency.</p>
<p>Contribution of the sector/subsector to reduce poverty in People's Republic of Bangladesh:</p> <p>Financial markets governance will increase the flow of resources to finance productive investments, improve the process of financial intermediation, and promote efficiency through enhanced market competition. Different social groups (investors, savers, market participants, enterprises and their employees, suppliers, and customers, and other stakeholders) will benefit from a deeper, more sound, and more stable financial system. The Financial Markets Governance Program will have an indirect but important strategic role in reducing poverty. With enhanced efficiency in mobilizing and allocating funds and proper enforcement mechanism in place, the Government may use cost savings from efficient financial markets for poverty reduction and social development. Transparency in the flow of financial resources is expected to remove inherent structural impediments to financial sector growth that result from an inefficient, opaque financial system.</p>	

B. Poverty Analysis

Improved governance/ Economic development

<p>What type of poverty analysis is needed?</p> <p>Inappropriate governance is mainly responsible for abnormal practices in the financial markets such as insider lending, insider trading, accounting and auditing wrongdoings, etc. It constrains overall private sector growth and potential investor participation. To enhance investor confidence and promote economic growth, intensified reforms are needed to strengthen the regulatory and supervisory framework, strengthen corporate governance and market discipline, and apply international accounting and auditing standards. The reforms should be backed by relevant fiscal incentives, including investment in human capacity development, that have broader poverty and social impacts. The key focus of poverty analysis is on identifying structural impediments to adopting and implementing proper governance reforms. To the extent that these impediments cause failure in achieving efficiencies in the financial markets, the benefits to various social groups will be less. The poor and disadvantaged may be expected to have a smaller share of benefits to be realized from the reforms. Government intervention through social programs is needed to allocate to the poor and disadvantaged funds generated from efficient financial markets and economic growth.</p> <p>Poverty in Bangladesh. Progress in reducing poverty in Bangladesh has, to some extent, been successful over the last decade, with poverty rates declining from 59% to 50%. However, high national poverty rates are still of major concern. Substantial urban-rural and regional disparities exist. Slower progress on structural reforms, rising revenue-expenditure gaps, the unstable financial condition of government-owned financial institutions, and the drain on the budget of the large number of state-owned enterprises together adversely affect Government's fiscal position and limit the stimulating effect on economic growth. The government budget deficit is 4-5% and is largely financed through substantial flow of external assistance. Bangladesh was able to achieve 5% growth of real gross domestic product (GDP) in FY2002; however, revenue, savings, and investments as ratios of the GDP are extremely low. In FY2002, total government spending on social safety net programs was only 1% of GDP and 5.6% of total government expenditures. Through extensive assistance by aid organizations and support from the Government, social sectors such as education, health, and nutrition have made reasonable progress. Joint efforts on the development of social sector programs should continue. Some of the savings that the Government would make from efficient financial markets would augment the budget for its social sector program.</p>

C. Participation Process**Stakeholder analysis? Yes**

Government agencies, chambers of commerce and industry, trade associations, aid organizations and the financial and private sector, and existing and potential foreign and domestic financial market participants .

Participation strategy? Yes

The participation strategy will involve consultation and feedback from concerned stakeholders on issues concerning financial markets governance. The derived outcome will be used to identify, prioritize, and address governance concerns and develop recommendations leading to actions.

D. Gender and Development

There is no specific strategy of maximizing impact on women. However, it is envisaged that encouraging proper functioning of the financial markets will lead to increased direct and indirect investments from foreign as well as domestic institutional and individual investors . Companies will benefit as a result of greater availability of financial resources at lower costs. Improved profitability, asset growth, and expansion of business will generate more employment and increased disposable income for average households, where women have a central role. When families are no longer at the subsistence level of existence and women are not tied to household chores, women are able to seize economic opportunities to augment their family income through micro or small enterprise pursuits.

No gender plan has been prepared.

E. Social Safeguards and other Social Risks

	Significant/ Nonsignificant/ None	Strategy to Address Issues	Plan Required
Resettlement	None	None	None
Indigenous Peoples	None	No adverse issues are anticipated.	None
Labor	Nonsignificant	Positive labor impact is expected.	No
Affordability	Nonsignificant	There will be no affordability-related issues. Through improved efficiency and increased competition, reduced costs for regulators, companies, and investors are envisaged.	No
Other Risks/ Vulnerabilities	None	No other risks are anticipated.	No

COST ESTIMATES AND FINANCING PLAN
(\$)

Item	Foreign Exchange	Local Currency	Total Cost
A. Asian Development Bank Financing^a			
1. Consultants			
a. Remuneration	337,500	33,750	371,250
b. Per Diem	62,400	0	62,400
c. International Travel	35,000	0	35,000
2. Seminars	0	3,000	3,000
3. Local Transport	0	3,000	3,000
4. Reports and Communications	3,000	500	3,500
5. Computer and Office Equipment	3,000	9,000	12,000
6. Contract Negotiation	5,000	0	5,000
7. Contingencies	50,100	4,750	54,850
Subtotal (A)	496,000	54,000	550,000
B. Government Financing			
1. Counterpart Staff	0	70,000	70,000
2. Office Accommodation and Facilities	0	35,000	35,000
3. Administrative and Other Expenses	0	35,000	35,000
Subtotal (B)	0	140,000	140,000
Total	496,000	194,000	690,000

^a Financed by Asian Development Bank's technical assistance funding program.
Source: Asian Development Bank estimates.

OUTLINE TERMS OF REFERENCE FOR CONSULTANTS

A. International Consultants

1. The team of consultants will consist of eight consultants led by the team leader-financial markets governance expert (TL-FMGE). The terms of reference of the five international consultants follow.

2. **Team Leader-Financial Markets Governance Expert** (5 person-months). The tasks of the TL-FMGE include the following:

- (i) Review the recommendations from previous technical assistances (TAs) of the Asian Development Bank (ADB) and other external funding institutions and assess the status of implementation of recommendations by the Securities and Exchange Commission (SEC) and other regulatory bodies.
- (ii) In collaboration with the domestic legal specialist (DLS), review alternative measures for achieving greater autonomy for SEC and insulating the market regulator from outside interference, study comparative practices within the region and elsewhere, and make suitable recommendations to strengthen SEC and make it financially autonomous. Identify possible sources of revenues for establishing its own budget. Consider adopting a collegial body structure for deciding on policy and securities under a one-member, one-vote rule, with fixed tenure for the members and removal only for cause.
- (iii) In collaboration with the DLS, recommend improvements in formulating and implementing regulations and rules. Define the formal stakeholder consultative process and formulate guidelines on who and when to consult, formal versus informal consultation, dissemination of drafts of proposals, need for exposure drafts or white papers, and appropriate consultation mechanisms such as open forums, publication, and feedback. Recommend ways for appropriate disclosure of the decision-making process at SEC that the public may be informed of the basis of SEC decisions (e.g. minutes of meetings, etc.). Determine enhancements in enforcement powers of SEC needed to effectively pursue securities cases. Determine, within the existing judicial system, what modalities may be introduced to facilitate the speedy resolution of securities cases.
- (iv) Review current mechanisms available to investors for seeking redress for grievances, e.g. complaints desk at SEC, and for the settling of disputes; and recommend improvements.
- (v) Review the skills inventory report on SEC staff prepared under TA-3533,¹ determine skills required by the organization now and for the next level of market development, and recommend suitable long-term training programs for the existing staff. Review recruitment policies, salary structures, performance evaluation procedures, and overall incentive framework. Determine ways for key salary positions at SEC to be competitive with the private sector.

¹ ADB. 2000. *Technical Assistance to the People's Republic of Bangladesh for Capacity Building of the Securities and Exchange Commission and Selected Capital Market Institutions*. Manila.

- (vi) Design and recommend the appropriate TA modality and program that can address SEC technical support requirements over the medium term, e.g., funds that can be tapped from time to time to finance short-term expert support requirements, medium-term placement of technical experts to help SEC in specific areas, etc.
- (vii) Propose amendments to the Companies Act to strengthen corporate governance in Bangladesh, the recommendations of TA-3533 (footnote 1) and the Corporate Governance Workshop of 12-13 July 2003. Interface with the Company Law Reform Committee to review Companies Act 1994 and help formulate an action program for corporate governance reforms.
- (viii) In collaboration with the financial institutions specialist (FIS), review the nonbank financial institution (NBFI) subsector, addressing issues of conflicts of interest, unequal opportunities, and market competition, and outlining the broad options in completing the restructuring of Investment Corporation of Bangladesh (ICB).
- (ix) Interface with consultants under TA-4140² tasked to draft a law on secured transactions and the development of the overall architecture for a transparent, electronic registration system for movable assets.
- (x) Assist in conceptualizing the design and scope of the Financial Markets Governance Program (FMGP), assess risks and possible implementation difficulties, and suggest mitigating measures. Provide inputs to a policy matrix for the FMGP. Assess the implementation and procurement arrangements and prepare a detailed logical framework for the ensuing sector development program.

3. **Demutualization and Exchange Expert** (3 person-months). The expert will have these tasks.

- (i) Consider whether it would be appropriate to preserve the current two stock exchanges or to merge their operations in the interest of market efficiency and development. Should the recommendation be to maintain the status quo, propose suitable ways for enhancing current operations, including specialization in specific areas to minimize overlapping. If a merger is the better option, propose suitable and practical ways for implementing it.
- (ii) Determine the feasibility of demutualizing the Dhaka Stock Exchange (DSE) and Chittagong Stock Exchange (CSE), define advantages and disadvantages and costs involved, prepare a detailed analysis and time-bound action plan for demutualization and/or merger. The plan should consider valuation of the exchanges; reconciliation of commercial interest and regulatory responsibilities relating to monitoring, investigation, dispute resolution, and sanctions; differentiation between right to trade and ownership of the new or merged exchange, and specific requirements and limitations on listing and transferring shares of the new exchange; avoidance of monopolistic practices; and

² ADB. 2003. *Technical Assistance to the People's Republic of Bangladesh for Supporting Good Governance Initiatives*. Manila.

adherence to international standards. Provide technical support for a program of stakeholder consultation and consensus building to carry out the action plan.

4. **Financial Institutions Specialist** (2 person-months). The FIS will undertake the following tasks:

- (i) Review Banking Companies Act 1991 and Financial Institutions Act 1993 as well as tax laws and regulations to identify provisions that give rise to unequal opportunities and distort market competition.
- (ii) Review SEC rules and regulations that allow commercial banks to undertake securities trading, merchant banking (public issue management and underwriting), and asset management, to determine potential conflicts of interest, and safeguards that regulatory authorities have prescribed against such potential conflicts of interest. Consider also brokerage functions performed by wholly owned subsidiaries of banks.
- (iii) To assess the NBF subsector, review (a) the legal and regulatory framework, including prudential regulations and tax regime, compared with international best practices; (b) sub-sectoral profile and structure; and (c) governance, performance, and potential, with a view to improving the ability to meet market requirements of products, services, and service delivery, and enhancing market competition. Recommend phased compliance with international norms if prudential regulations do not meet international standards.
- (iv) Consider gaps in the financial markets that are not served or are underserved in the present system, such as housing finance, asset securitization, asset management companies for dealing with nonperforming assets; and determine impediments to their introduction and development.
- (v) Review the mutual funds industry regulations, including the tax regime, with a view to creating comparable conditions and removing disincentives to greater private sector participation that can accelerate development of the industry.
- (vi) Draft the terms of reference for the international audit of ICB, define the action steps to be taken by ICB and the Government prior to the audit, and outline broad options to consider on completion of the audit.

5. **Accounting and Auditing Specialist** (1.5 person-months). The tasks of the specialist follow.

- (i) Update the assessment of accounting and audit practices carried out as part of the World Bank-International Monetary Fund joint initiative Report on the Observance of Standards and Codes for Bangladesh, and progress in implementing the World Bank assistance relating to the adoption of international accounting standards (IAS) and international standards on auditing (ISA).
- (ii) In accordance with the recommendation of TA-3533 (footnote 1) to establish an accountancy board, propose a plan for setting up a regulatory board for accounting based on best practices covering, among others, mandate and objectives, powers, and functions of the proposed board; its organizational

structure, budget, and steps required for its establishment. The accountancy board or equivalent will be responsible for (a) implementing and monitoring compliance with IAS and ISA, (b) certifying and training accounting professionals, (c) enforcing professional standards and ethics, and (d) developing the appropriate college curriculum.

- (iii) Consider how the Institute of Chartered Accountants of Bangladesh (ICAB) can function as a self-regulatory organization.

6. **Securities Training and Accreditation Specialist** (2 person-months). The securities training and accreditation specialist (STAS) will undertake the following tasks:

- (i) In consultation with existing training institutes, assess the needs for training key market players and participants, including listed companies, concerning their obligations in discharging their duties to the investing public and shareholders, as well as to investors. In coordination with FIS, assess the skills needs of financial market institutions and recommend measures for skills upgrading. Develop syllabi for various skills development courses on securities markets operations, including programs for company directors. Give particular attention to governance of family-owned and family-run listed companies.
- (ii) Determine what training facilities will be required to pursue a long-term training and education program on securities market operations and governance, including accounting, auditing and corporation law. Recommend which among the existing training facilities can be utilized for the purpose. Determine an appropriate budget for such a training institution.
- (iii) Review the status of implementing accreditation of brokers and broker representatives developed under TA-2913³ and develop a system and process for certifying or accrediting securities professionals other than brokers who deal with the investing public such as mutual funds solicitors, portfolio managers, etc.
- (iv) Review the status of implementing the investor awareness program of SEC developed under TA-2913 (footnote 3), and develop a model investor awareness program that the securities market operators and exchanges can pursue over a defined time and which can complement that of SEC.
- (v) Collaborate with the TL-FMGE in assessing the skills that SEC needs to operate effectively, and in proposing suitable long-term training programs for the existing staff to acquire the necessary skills.

B. Domestic Consultants

7. The terms of reference of the three domestic consultants are outlined here.

8. **Legal Specialist** (3 person-months). The tasks of the DLS follow.

³ ADB. 1997. *Technical Assistance to the People's Republic of Bangladesh for Capacity Building of the Securities and Exchange Commission and Stock Exchanges*. Manila.

- (i) In general, collaborate with the TL-FMGE and FIS to provide legal inputs needed in carrying out their tasks.
- (ii) In particular, prepare a report on the legal aspects of making SEC financially autonomous and restructuring it into collegial body. Write on the salient aspects of corporate governance recommended under TA-3533 (footnote 1) and the key aspects of the Companies Act, and Securities Laws and Regulations—i.e., Securities and Exchange Ordinance and Securities and Exchange Act—that need to be reassessed or amended. Comment on the appointment of special courts or bench in the High Court for settling securities disputes. Report on the key legal aspects to consider in the review of the NBF subsector and for the demutualization and/or merger of DSE and CSE. Identify steps and measures needed to bring government-controlled mutual funds under SEC's uniform regulatory regime and to establish an accountancy board.
- (iii) Prepare a draft administrative order creating a Commission on Amendments of Securities Laws and Regulations. Review proposed amendments to the Companies Act and other legislative and regulatory amendments for improving corporate governance.

9. **Financial and Securities Analyst** (3 person-months). The analyst will undertake these tasks.

- (i) Collaborate with the TL-FMGE, FIS, and STAS to provide data inputs needed in carrying out their tasks. Analyze, with appropriate statistical tables and annexes, the market structure and profile and key issues concerning (a) the NBF sector and (b) securities markets. Analyze the organization, management, policies, systems, operations, financial performance and condition of seven largest private NBFs including leasing companies, DSE, CSE, and the brokerage industry.
- (ii) Assist the STAS in (a) assessing the needs for training among key market players and participants as well as investors, (b) conducting a survey of training facilities that may be used for a long-term training and education program on securities market operations and governance, and (c) developing syllabi for various skills development courses on securities markets operations.
- (iii) Assist the TL-FMGE and STAS in assessing skills that the SEC needs to operate effectively.

10. **National Accountant** (1.5 person-months). The accountant will accomplish these tasks.

- (i) Collaborate with the accounting and auditing specialist to provide whatever appropriate inputs are needed in carrying out the specialist's tasks.
- (ii) In particular, provide a brief on (a) progress in implementing the multilateral technical assistance on the adoption of IAS in the country; (b) the major differences in IAS and Bangladesh Accounting Standards; (c) government requirements on the certification of chartered accountants; (d) the curriculum content of colleges offering degrees in accounting and auditing; and (e) the charter, organization, membership, activities, self-regulation, and training programs of ICAB.