

# Corporate Governance in Maldives

**Paper for the Workshop on “Developments, Structures, Capacity & Roadmap for Enhancing Corporate Standards in Commonwealth Countries”**

**Bandos Island Resort, 17 - 18 June 2006**



**CMDA**

Capital Market Development Authority

The Capital Market Development Authority  
MTCC Tower 4<sup>TH</sup> Floor,  
Male', Maldives.  
[www.cmda.gov.mv](http://www.cmda.gov.mv)

## Contents

1 Background Information.....	3
2 Developing Economy.....	3
3 Corporate Structure .....	3
4 Government Ownership.....	4
5 Capital Markets.....	5
6 Extent Of Legal Status .....	5
7 Acceptance Level By Companies Which Have Been Listed And Which Will Be Listing .....	6
8 Key Issues That Can / Cannot Be Addressed In Code Of Corporate Governance.....	6
8.1 Government Ownership.....	6
8.2 Director Issues .....	6
8.3 Conflicts Of Interest.....	7
8.4 Related Party Transactions .....	7
8.5 Audit, Book Keeping, Internal Controls.....	7
8.6 Different Treatment Of Private-Sector Companies From Public-Sector Companies .....	8
8.7 Lack Of Capacity / Resources For Enforcement Purposes .....	8
8.8 Lack Of Qualified Professionals In Accounting And Legal Fields .....	8
8.9 Disparate Efforts On Going – Need To Coordinate .....	9
8.10 Company Secretary .....	9
8.11 Training And Awareness .....	9
8.12 Journalist As A Key Stakeholders .....	9
9 Purpose, Scope & Structure Of The Code.....	9
9.2 Whether The Rules Should Be Made Mandatory .....	10
9.3 Whether There Should Be A Stand-Alone Code .....	10
9.4 Companies To Which Code Should Extent To.....	10
10 Proposed Issues To Be Addressed In The Code.....	10
11 Conclusion .....	11

# Corporate Governance In Maldives

## 1 BACKGROUND INFORMATION

The Capital Market Development Authority was established for the purpose of developing and regulating a capital market in the Maldives. The Capital Market Development Authority has taken the initiative to promote a culture of good corporate governance in Maldives with the aim to raise investor (both local and foreign) confidence, develop the capital markets and to achieve high sustained growth from the corporate sector and the economy as a whole.

## 2 DEVELOPING ECONOMY

2.1 Corporate Governance is at its infancy in the Maldives. This mirrors the state of development of the capital markets and the general financial sector in the Maldives. More importantly, it is reflective of the typical developing country facing the challenge of transforming economic governance arrangements from relationship-based systems into rules-based systems.

2.2 The Maldives is geographically scattered across tiny islands and is poor in resources. The primary industry is tourism which has grown with the introduction of taxation and leasing rules for tourist resorts. Tourism is the greatest contributor to the Maldives' GDP. It is understood that the country has been transformed from an industry primarily developed in an ad hoc manner to a well-planned and profitable one. The current push is to develop this sector further, including by encouraging more private sector involvement.

## 3 CORPORATE STRUCTURE

3.1 In Maldives the majority of the companies are typical small businesses comprising of two-men mom-and-pop shops or companies established by friends. There are allegedly over 2000 companies registered with the Registry of Companies, with only approximately 500 which remain active currently. Out of these 500 over 95% are small companies. The concept of small and medium enterprises in the Maldives was quite different from that as is typically understood in most developed countries.

3.2 Whilst the concept of the separate legal entity does exist in Maldives, the individual is usually bigger than the company. This concept is, however, not unusual even in the developed world, where the corporate entity is just a means of structure for doing business.

3.3 Many of the companies are closely held in the Maldives. This does affect how one conceives the corporate governance problem and potential dispute resolution methodologies. In the debate about ownership and control, the focus shifts from conflicts between management and shareholders to a three-way conflict between large block holders, managers, and minority investors. Furthermore, the identity of investors comes into play, and it becomes important who monitors them, what their incentives are, and how they are constrained by the legal framework. When the firm is closely held, the

emphasis shifts from shareholder-oriented governance institutions such as boards of directors, general shareholders' meetings, and takeovers to a broader set of devices for re-designing ownership and control, such as pyramiding of share holdings, cross-ownership, managerial networks, and block trading. Also in the analysis of capital market activity, the paradigm of the competitive stock market must be seen more in terms of models of bilateral negotiations, block holder conflicts, and market design.

3.4 On balance, however, it was found that there was a general knowledge at very senior level amongst the public companies of the need for corporate governance. Therefore, in principle at least (or in form at least), the culture in Maldives is one of acceptance and a feel that corporate governance is an economic necessity.

3.5 Another key issue that arises when there are closely held companies is the definition to be accorded to independent directors. Care would have to be exercised on this front to ensure that any definition that is adopted is workable. Clearly, it is not possible to simply adopt a definition from an existing code of corporate governance in a developed country.

#### **4 GOVERNMENT OWNERSHIP**

4.1 The largest corporations in the Maldives continue to have government ownership or some form of strong interest group holding.

4.2 The private sector which is starting to flourish, however, lacks the financial resources to undertake some of the services currently provided by state-owned enterprises. This can be overcome over time.

4.3 Considering the involvement / ownership of the Government in certain enterprises, there is a risk that such preferential treatment might be used for personal gains by directors by manipulating the economic environment, although it is not necessarily happening. It will represent an immense challenge that must be overcome if corporate governance is to be introduced. Yet, the challenge is a perceived one.

4.4 It is understood that efforts are being taken to change the traditional business approaches. Key amongst this is the Government's step in gradually divesting its stake in state-owned enterprises. The intent is to promote capital markets development and corporate governance. Since the commencement of the stock exchange in the Maldives, four public companies are listed on the Securities Trading Floor- Maldives Transport and Contracting Company ('MTCC'), Bank of Maldives ('BML'), State Trading Organization STO. There is a proposed listed company, the Maldives Tourism Corporation Development Corporation ('MTDC') which will be 55% owned by the public and 45% owned by the government.

4.5 It is felt that with more state-owned enterprises taking steps to list or open themselves to additional shareholders, the Maldives' corporate culture is getting ready to undergo wide-reaching change. This is clearly reflective of an environment that is ready for a Corporate Governance Code to be introduced.

## **5 CAPITAL MARKETS**

5.1 Corporate Governance continues to be seen by some as unimportant in developing countries, in large because of the small number of firms with widely traded shares. Where it is accepted that there should be a Corporate Governance Code, the suggestion is for the Code to be framed in the same way as those that exists in a more developed country and more so from a Western country. There are limitations to such an approach, and it is strongly recommend that such an approach be adopted. Instead, a more prescriptive approach recognising the needs and requirements of Maldives should be introduced.

5.2 Introducing a Code at a time when the capital markets is still young is the right way to go as it would aid in cultivating the promotion of good corporate governance practices amongst all newly listed companies.

## **6 EXTENT OF LEGAL STATUS**

6.1 In developing countries, the roots of what is now recognized as corporate governance type issues can be found in the drive for privatization. Clearly, creating a sound corporate structure should have been central to the success of privatization both from the point of view of the government seeking to sell the firm and from the point of view of the potential investors. In fact, some of the failures in the privatization experiences of some countries can be traced back to a lack of sound regulatory structures that allowed unwise business practices.

6.2 Given this, it is only logical and indeed promising that Maldives has embarked on a corporate governance drive fairly early in the day.

6.3 The legal structure and ability for enforcement, however, is severely lacking in the Maldives. The judiciary is dynamic, but perhaps is not best equipped to handle corporate governance concerns due to trained judges in this particular area and the lack of adequate laws.

6.4 A large body of commercial laws have only been introduced in recent times, and some continue to be introduced. There is currently no Banking Act, for instance, that regulates the banking industry, although the Maldives Monetary Authority does provide the relevant licensing framework and regulatory oversight. There is also currently no tax law in place, although draft tax legislation has been drafted and it is expected to be passed into law during the course of 2006, and become effective from 1 January 2008. The legislation which has been introduced has to be revised in some instances,

including several provisions of the Companies Act. As an example, the provisions on directors' duties and responsibilities must be enhanced. Amendments have been previously proposed to the Companies Act, but these remain under study.

6.5 There is also concern as to whether there are sufficient resources / skills for the purpose of regulating and enforcing corporate governance. If such resources / skills exist, their numbers are wanting. For instance, several of the regulators seem extremely lean currently. This obviously calls for considerable nurturing of resources / skills with training at different levels a necessity. Any training that is provided will have to be on a continuing basis.

## **7 ACCEPTANCE LEVEL BY COMPANIES WHICH HAVE BEEN LISTED AND WHICH WILL BE LISTING**

7.1 Companies which have been listed do take corporate governance very seriously and would ensure compliance if a code of corporate governance is introduced.

7.2 Companies which are in the midst of being listed are also receptive to the idea.

## **8 KEY ISSUES THAT CAN / CANNOT BE ADDRESSED IN CODE OF CORPORATE GOVERNANCE**

This Paragraph 8 sets out in summary fashion the key issues that surfaced during the fact finding mission\* at a corporate level.

### **8.1 Government Ownership**

8.1.1 Government ownership is not a unique feature only to be found in the Maldives. Hence, the same issues that plague most other countries where there is widespread Government ownership also finds its way into the Maldives.

8.1.2 Such ownership cannot, however, go unaddressed. Specific provisions need to be spelt out to handle issues arising from such ownership so as to ensure that any Code introduced is not merely in form but also in substance, workable. This may not at this time be included into the Code being proposed.

---

\* Kala Anandarajah is a partner at the Singapore Law firm of M/s Rajah & Tann. She leads the Corporate Governance Practice at the firm. She has been engaged to draft the Maldives Corporate Governance Code in conjunction with the Capital Markets Development Authority and the Commonwealth Secretariat.

## **8.2 Director Issues**

8.2.1 One of the key concerns that were observed is the mandated requirement (in the Companies Act) for directors to own shares in the company. However, the purpose of this requirement was to prevent foreigners from setting up companies in the Maldives, potentially exploiting the country and its people, and then leaving as soon as a quick dollar has been made. This is an important point that must be borne in mind in making a call as to whether to remove this qualification to be a director.

8.2.2 Next, there is a practical problem in identifying sufficient individuals to act as independent directors, given the small population of the country. However, given the importance of the role such a person can perform in the corporate structure, any definition accorded to 'independence' must recognize the specific limitation in the Maldives and hopefully work around it.

8.2.3 A review of the various companies showed that it was not common to have the roles of chairman and chief executive officer / managing director separated. The role was often situated within the one person. This person was also frequently the one who wielded the most power (which is typical even in developed countries). There has been no consistent approach adopted globally as to whether the roles should be fused or held by two separate people. In a country which is in infancy in corporate governance, it is beneficial to have the two roles separated. This would work as a means of enforcement as it is effectively a check and balance.

8.2.4 A further limitation that currently exists is that the duties and obligations of directors are not clearly spelt out in the Companies Act or other legislation. There is also insufficient case law, if at all, that stipulates what a directors' duty encompasses. At the very least, there should be a provision included into the Companies Act, for instance, providing that directors owe fiduciary duties. The provision should also identify the key elements of what being a fiduciary entails and provide a broad indication of what the other duties of a director should be. The Consultant understands that proposals on directors' duties have already been made and are currently being considered by the Government of Maldives.

8.2.5 Given that numerous adults in Maldives work at least two jobs, inter-locking directorships are not at all uncommon. This is a practical problem that needs addressing in the Code.

### **8.3 Conflicts of Interest**

8.3.1 Given the small population in Maldives, it is not unusual to have cross-shareholdings (as noted above), which in turn results quite clearly in potential conflict problems. Conflicts could potentially arise as an individual could be a director of several major companies at one and the same time, all of which have similar interest in pursuing a particular course of action.

8.3.2 A typical provision in most companies' legislation in various jurisdictions would prohibit such conflicts unless there has been disclosure and due approval. Likewise, the codes of corporate governance would also contain provisions guiding how conflicts should be addressed. Such provisions would be particularly important for the Maldives.

### **8.4 Related Party Transactions**

8.4.1 Given the nature of the shareholding structure and interlocking directorships, related party transactions arise every so often. Indeed, this could potentially be a problem in trying to ensure improved corporate governance.

8.4.2 Special care, therefore, needs to be exercised in spelling out legislation on this issue. The focus ought to be on disclosure and transparency rather than a prohibition of such transactions.

### **8.5 Audit, Book Keeping, Internal Controls**

8.5.1 Auditing as is common in other jurisdictions is not a common practice in the Maldives, although the Companies Act does require it. Book keeping in a very traditional sense is practiced. One of the reasons for this is the strong desire to maintain confidentiality. This stems from the traditional patriarchal manner of doing business.

8.5.2 It was emphasized that a US style auditing requirement could not be imposed in the Maldives. This is despite the fact that international accounting standards are currently adopted in the Maldives.

8.5.3 Whilst the few listed companies claim to have good internal control processes, it would appear that most companies only have rudimentary internal control systems. This would have to be enhanced generally.

8.5.4 It was observed that banks could play a strong role in ensuring that there is good corporate governance, which would include internal control mechanisms, within companies seeking financing from them. This is done only to a very small extent; and can certainly be increased upon substantially.

## **8.6 Different Treatment Of Private-Sector Companies From Public-Sector Companies**

8.6.1 The Companies Act currently treats private-sector companies (which would include listed companies) differently from public sector companies. This is a requirement that ought to be modified. It will call for a change to be made to the Companies.

8.6.2 However, this Act is beyond the scope of the Team. In any event, any proposed changes need not be undertaken immediately. Plans should nevertheless be put in place to take appropriate steps moving forward.

## **8.7 Lack Of Capacity / Resources For Enforcement Purposes**

10.7.1 The lack of resources for enforcement and the inadequacy of the enforcement process was factor that surfaced several times throughout various meetings.

8.7.2 This is indeed an acute problem and attention needs to be given to how this can be best addressed.

## **8.8 Lack Of Qualified Professionals In Accounting And Legal Fields**

8.8.1 A clear element which is lacking in the Maldives is the insufficient number of qualified professionals in the accounting and legal industries. These are two professional groups which are absolutely crucial in aiding the improvement of corporate governance.

8.8.2 It is understood that steps are being taken to improve the accounting profession in the Maldives. Accreditation and a chartered accounting programme will be introduced in due course.

8.8.3 Insofar as the legal profession is concerned, a more concerted effort needs to be undertaken to improve the understanding of the role that the profession can play.

8.8.4 Much training needs to be conducted.

## **8.9 Disparate Efforts On Going – Need To Coordinate**

8.9.1 There appears to be disparate efforts in putting together codes, laws and other best practices on-going. A way has to be found to crystallize and adopt a consistent approach.

## **8.10 Company Secretary**

8.10.1 The company secretary has never been taken seriously in most companies in the Maldives. Many simply have a director, and usually the managing director, act as the company secretary as well. This creates conflicts, and more importantly does not ensure an efficient performance of the function. Indeed, only one company, amongst several that the Team met, had a lawyer as a company secretary.

8.10.2 It is, therefore, essential to introduce a provision that deals with the company secretary. The company secretary's detailed roles must be spelt out in the Code.

8.10.3 Additionally, the facilitative role that the company secretary can play in collating relevant information and acting as an effective bridge between the board and management and amongst board members must be set out.

8.10.4 There is currently no chartered secretaries' programme in the Maldives. This is something that should be reviewed and implementation considered.

### **8.11 Training And Awareness**

8.11.1 On all accounts this was a fact that was repeated time and again. There was clear and distinct lack of training going on and also as a matter of culture, it was not something that was automatically accepted.

8.11.2 There is, however, a keen interest to explore how this can be achieved on a sustained basis. It is evident that the various stakeholders are eager to be trained.

8.11.3 The proposed Capital Market and Corporate Governance institute will play a pivotal in training and inculcating the culture of corporate governance in Maldives.

### **8.12 Journalist As A Key Stakeholders**

8.12.1 The journalists were identified as a key tool in trying to create awareness about corporate governance and the manner in which companies operate. However, to enable the journalist to create such awareness, they need to be educated first.

8.12.2 Some felt that perhaps the Code should include provisions dealing with journalists as well, specifically setting out details about the role they play, and providing suggestions as to how they can achieve the role.

## **9 PURPOSE, SCOPE & STRUCTURE OF THE CODE**

9.1 There is a keenness to ensure that there is a greater degree of corporate governance within Maldives. This Paragraph 9 sets out key elements of the type of code that should be introduced and explores the issues of whether a mandatory or voluntary code should be introduced.

## **9.2 Whether The Rules Should Be Made Mandatory**

The recommendation is for corporate governance code that comprise a combination of mandatory and voluntary provisions. Some of the mandatory provisions would have to be included into the Companies Act, whilst others could be retained within the Code, which would be in two parts; namely a mandatory section and a voluntary section.

## **9.3 Whether There Should Be A Stand-Alone Code**

The recommendation is to have a stand-alone Code that is given sufficient teeth through a reference from the Companies Act or through the Listing Manual.

## **9.4 Companies To Which Code Should Extent To**

The preferred recommendation is for a Code that applies to all listed companies and all public companies. However at this juncture it is envisaged that it will only apply to listed companies although it is open for any company to adopt the code on a voluntary basis.

## **10 PROPOSED ISSUES TO BE ADDRESSED IN THE CODE**

With the above background in mind, this Paragraph provides an overview of the key areas that MUST be addressed in a Code of Corporate Governance will be drafted. The code will be finalized after giving adequate consultation time to the public, relevant international agencies and other parties. The code will take into consideration matters relating to board, audit, management concerns internal controls, company secretary, shareholder communications, disclosure and transparency and training amongst other issues

## **11 CONCLUSION**

11.1 This Paper has provided a broad overview of the state of corporate governance in the Maldives and recommendations as to some of the things that could be implemented in a proposed corporate governance code that will come into force in mid 2007. The proposed code was discussed at the stakeholders session which was mainly attended by the Maldivians.

11.2 For further information, please do not hesitate to contact Capital Market Development Authority at 960 333 6621 or email at [shafeega@cmda.gov.mv](mailto:shafeega@cmda.gov.mv).