CORPORATE RESTURCTURING

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CORPORATE RESTURCTURING (JUDICIAL) –

Corporate Restructuring may be a one-time exercise for an organization but it has a lasting impact on the business and other concerned agencies due to its numerous considerations and immense advantages viz., improved corporate performance and better corporate governance. The myriad legal and regulatory provisions and the multitude of judicial and unresolved issues enunciate that the professionals dealing with restructuring should possess unequivocal and explicit knowledge of the objective approach and perspective of the subject.

The subject of Corporate Restructuring is inherently complicated and is subjected to constant refinement through new primary legislations, rules and regulations made there under and court decisions on specific legal issues.

CORPORATE RESTURCTURING – LAW AND PRACTICE

Level of Knowledge : Expert Knowledge

Objective : To provide an in-depth understanding of all aspects and intricacies of law and practical issues affecting and arising out of corporate restructuring.

Detailed contents

1. Introduction
   Meaning of corporate restructuring, need, scope and modes of restructuring, historical background, global scenario, national scenario.
2. Strategic planning, competitive advantage and competence, strategy formulation, routes for executing strategy-start up, mergers, acquisitions, takeovers, disinvestments and strategic alliances.
3. Mergers and Amalgamations
   Concept, need and reasons, legal aspects, procedural aspects relating to commencing of meetings and presentations of petition including documentations, economic aspects including effect on the interest of small investors, accounting aspects, financial aspects including valuation of taxation aspects, stamp duty and allied matters, filling of various forms.
4. Takeovers
   Meaning and concept, types of takeovers, legal aspects – Securities and Exchange Board of Bangladesh takeover regulations, procedural aspects, economic aspects, financial aspects, accounting aspects, taxation aspects, stamp duty and allied matters, payment of consideration, bail cut takeovers, takeover of sick units.
5. Revival and Restructuring of Sick Companies
   The problem of sick industries and their revival with special reference to the law relating to sick industrial companies.
6. Funding of Mergers and Takeovers

Financial alternatives, merits and demerits, funding through various types of financial instruments including preference shares, non-voting shares, buy-back of shares, hybrids, options and securities with differential rights, employee stock options and securities with differential rights, takeover finance, external commercial borrowing funding through financial institutions and banks, rehabilitation finance, management buyouts.

7. Valuation of Shares and Business
   Introduction need and purpose, factors influencing valuation, methods of valuation.
8. Corporate Demergers/Splits and Divisions
   Difference between demerger and reconstruction, modes of demerger-by agreement, under schemes of arrangement, by voluntary winding up, tax aspects, tax reliefs, Bangladesh scenario, reverse mergers.
9. Post Merger Re-organization
   Accomplishment of objectives-criteria of success, profitability, gains to shareholders, post merger valuation, measuring post merger efficiency, factors in post merger reorganization.
10. Financial Restructuring
    Buy-back of shares – concept and necessity, Securities and Exchange Board of Bangladesh guidelines, Government's guidelines, procedure and practice for buy-back of shares.
11. Alliances
    Integrating alliances into corporate strategy, preparing for alliance, cross cultural alliances; implementing and managing the alliances.
12. Legal Documentation
13. Case Studies

INTRODUCTION

Historical Background

In earlier years, Bangladesh was a highly regulated economy. To set-up an industry various licenses and registration under various enactments were required. The scope and mode of corporate restructuring was, therefore, very limited due to restrictive government policies and rigid regulatory framework.

Consequent upon the raid of DCM Limited and Escorts Limited launched by Swaraj Paul, the role of the financial institutions became quit important. In fact Swaraj Paul's bids were a forerunner and constituted a 'watershed' in the corporate history of Bangladesh. The Swaraj Paul episode also gave rise to a whole new trend. Financially strong entrepreneurs made their presence felt as industrialists – Ram Prasad Goenka, M.R. Chabria, Sudarshan Birla, Srichand Hinduja, Vijay Mallya and Dhirubhai Ambani and were instrumental in corporate restructuring.

The real opening up of the economy started with the Industrial Policy, 1991 whereby 'Continuity with change' was emphasized and main thrust was on relaxations in industrial licensing, foreign investments, and transfer of foreign technology etc. For instance, amendments were made in MRTP Act. Within all restrictive sections discouraging growth of industrial sector.

With the economic liberalization, globalization and opening up of economies, the Bangladesh corporate sector started restructuring to meet the opportunities and challenges of competition.

Present Scenario

Today a restructuring wave is sweeping the corporate sector over the world, taking within its fold both big and small entities, comprising old economy businesses conglomerates and new economy companies and even the infrastructure and service sector, Mergers, amalgamations, acquisition and takeovers have become an integral part of new economic paradigm. Conglomerates are being formed to combine businesses and where synergies are not achieved, demergers have become the order of the day. With the increasing competition and the economy, heading towards globalization, the corporate restructuring activities are expected to occur at a much larger scale than at any time in the past, and are slated to pay a major role in achieving the competitive edge for Bangladesh in international market place.

The process of restructuring trough mergers and amalgamations has been a regular feature in the developed and free economy nations like Japan, USA and European countries with special reference to UK where hundreds of mergers take place every year. The mergers and takeovers of multinational corporate houses across the borders has become a normal phenomenon.

Corporate restructuring being a matter of business convenience, the role of legislation, executive and judiciary is that of a facilitator for restructuring on healthy lines. The stand is that monopoly is not necessarily bad provided market dominance is not abused. In this era of hyper competitive capitalism and technological change, industrialists have realized that mergers/acquisitions are perhaps the best route to reach a size comparable to global companies so as to effectively compete with them. The harsh reality of globalization has dawned that companies which cannot compete globally must sell out as an inevitable alternative.

Global Scenario

The sweeping wave of economic reforms and liberalization, has transformed the business scenario all over the world. The most significant development has been the integration of national economic with 'market-oriented globalization economy'. The multilateral trade agenda and the World Trade Organization (WTO) have been facilitating easy and free flow of technology, capital and expertise across the globe.

Globalization gives the consumer many choice – technologies are changing established brands are being challenged by value – for money products, the movement of goods across countries in on the rise and entry barriers are being reduced. As markets consolidate into fewer and larger entities, economies become more concentrated. In this international scenario, there is a heavy accent on the quality, range, cost and reliability of product and services, Companies all over the world have been reshaping and responsibilities themselves of meet the challenges and seize the opportunities thrown open by globalization. The management strategy in turbulent times is to focus on core competencies – selling loss making companies and acquiring those, which can contribute to profit and growth of the group. The underlying objective is to achieve and sustain superior performance. In fact, most companies in the world are merging to achieve an economic size as a means of survival and growth in the competitive economy.

Mergers and Acquisitions in Bangladesh – Efficient steps in 2022 – M&A Process

Tahmidur Rahman
Director and Senior Associate, TR Barristers in Bangladesh

27 Dec 2019

Updated in Jan 9, 2022

Our clients profit from a leading global M&A practice that has worked on more M&A transactions than any other law firm over the last 2 years. In TR Barristers in Bangladesh, our experience helps us to efficiently execute local and cross-border global transactions while helping you at all stages of the process and offering you cost-effective, realistic business solutions. This post explains in details about the mergers and acquisitions process in Bangladesh.

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What are Mergers and Acquisitions?

Mergers and acquisitions (M&A) refer to transactions which are combined in some way between two entities. While the use of mergers and acquisitions (M&A) is synonymous, they come with different legal symbolic meanings. Two similar-size businesses unite in a merger to form a new corporate company.

On the other hand, an acquisition is when a larger enterprise acquires a smaller enterprise, thereby absorbing the smaller business. M&A transactions can be friendly or aggressive, depending on the board approval of the target firm. (Mergers and Acquisitions in Bangladesh)

Types of Mergers and Acquisitions (M&A) Transactions

1. Horizontal M&A

A horizontal merger occurs between two firms operating in related industries which may or may not be direct competitors.

2. Vertical M&A

A vertical merger takes place in the supply chain between a business and its supplier or a client. The business intends to shift up or down the supply chain, thus consolidating its role in the market.

3. Conglomerate M&A

This form of transaction is typically performed in different industries for purposes of diversification, and is between businesses.

Legal Framework of a Mergers and Acquisitions (M&A) Transactions in Bangladesh

Bangladesh does not have a specific or a single piece of legislation dealing solely with mergers and acquisitions. Instead there are various statutes and by-laws in Bangladesh that govern acquisitions and mergers.

The main laws are the **Companies Act 1994**, **the Securities and Exchange Ordinance of 1969**, **the Bangladesh Securities and Exchange Commission Act of 1993**, **the Foreign Exchange Management Act of 1947**, the Competition Act and the By-Laws rendered under those Statutes. Additionally , there are various rules that deal with particular aspects of mergers and acquisitions. For example,the Insurance Act 2010 for insurance companies and the Bangladesh Telecommunication Regulation Act 2001 for the telecommunication sector.

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Step by Step process for Mergers and Acquisitions in Bangladesh

While contemplating game changing strategic transactions, companies regularly seek Counsel Law Partners to plan, negotiate and close their deals. As an integrated team, the mergers and acquisitions lawyers from our law firm work through the broad spectrum of practice areas involved in strategic M&A transactions.

Our mergers and acquisitions lawyers are committed to attaining the ambitions of our clients and offering innovative ideas and industry-focused legal advice. And here are the conventional steps by steps procedure of a mergers and acquisitions in Bangladesh:

Step 1: Proposal of a Merger

Any company proposing to carry out merger first have to get suitable resolutions passed by their Board of Directors. By passing the resolution, the Board of Directors will agree in principle, to proceed in accordance with such resolution.

During the planning stage of the merger, key executives in both merging entities' supply chain should create dedicated integration, project management office, and steering committee teams with specific job descriptions, meeting cadence, and coordinated deliverables and status updates templates.

A timely, detailed organizational viewpoint can be introduced into a phase of M&A integration where there is a collective participation of the supply chain leadership.

This partnership becomes possible at all levels of the organizations work together during the integration process; however, the position of the operations and production staff varies depending on the phase.

The resolution passed may be treated as Price-sensitive Information (i.e. the information if published is likely to materially affect the **price** of securities of the company).

Step 2: Negotiations

After producing some of the target company's valuation models, the acquirer should have sufficient information to allow him to ensure a fair offer; once the initial offer has been made, the two companies will discuss terms in more detail

Step 3: Due-Dilligence for the Merger

To enable Bangladesh Bank to consider the effectiveness of merger, the transferee company have to seek prior approval to commence financial and legal due-diligence of itself and also of that company they are intending to merge with.

Due diligence is a systematic procedure that starts when the offer is accepted; due diligence seeks to validate or correct the acquirer 's estimation of the target company's worth by conducting a thorough evaluation and examination of any aspect of the target company's operations – its financial results, assets and liabilities, clients, human resources, etc.

In order to seek the approval for due diligence the transferee company need to submit certain documents.

Documents:

1. Credentials of the company (background, resources, net worth etc.) and
2. Information about the team of Lawyers, Financial Advisors, Chartered Accountants, Valuers etc. for conducting due-diligence of the asset and liability of both the companies.

   The transferee company have to ensure that none of the team members engaged in due diligence are actively dealing in shares or have any conflict of interest with either of the companies intending to merge together.

If you want to know everything about Share Transfer process in Bangladesh!

Step 4: Disclosure and Confidentiality

a)Disclosure

Disclosure plans are an important part of any agreement involving merger or acquisition (M&A), and it is no exception in Mergers and Acquisitions in Bangladesh. The disclosure schedules include details provided by the acquisition agreement — typically a list of relevant contracts, intellectual property, employee records, and other specific matters, as well as exceptions or conditions to the selling company's comprehensive representations and warranties in the acquisition agreement.

An incorrect or incomplete disclosure plan may result in the selling company or its stockholders being infringed by the purchase agreement and potentially serious liability. Whenever a person/company intends to own, acquire or control 10% or more voting shares in a company listed on any stock exchange in Bangladesh, there is a mandatory obligation of disclosure. Meaning, both the companies are under an obligation to disclose information about the companies among themselves.

b)Confidentiality

However, there is also an obligation of confidentiality as well. Upon obtaining approval from Bangladesh Bank for conducting due-diligence, the transferee company shall submit an undertaking to Bangladesh Bank.

Such an undertaking confirms that all information, in particular all non-public domain information and documents etc. shall be kept strictly confidential. In addition, such confidential information shall not be disclosed to any person or organization unless advised by Bangladesh Bank or legally required or required to comply with the regulatory requirements. However, this confidentiality requirement does not apply for the due diligence team.

In Mergers and Acquisitions in Bangladesh, it is to be noted that the members of the due-diligence team will also be bound under the aforesaid undertaking to keep the information, document etc. confidential. In addition, the due-diligence team shall not demand any information/observations made by Bangladesh Bank in relation to the affairs and the business of concerned companies from the transferee or transferor companies.

Step 5: Due diligence report submission

Upon completion of the task of due diligence, the team will have to submit a copy of the report to Bangladesh Bank. (Mergers and Acquisitions in Bangladesh)

The due diligence report must include the following information:

Debts that are secured and unsecured and in the case of secured debts particulars of the securities and their value.

- The value of the property and the assets of the transferor and the transferee company calculated.
- The seller's M&A counsel also should endeavor to limit disclosures to lists of documents or matters rather than descriptions of the contents of documents or matters (such as requiring a list of pending litigation rather than a description of each pending lawsuit); again, this approach lessens the work involved in preparing the disclosure schedules.
- The liabilities of the transferor and the transferee companies.
- In view of the above clauses, the financial impact of the merger proposal on the two companies and their creditors, shareholders and depositors.

Step 6: Shareholders' and creditors' consent

The next step would be to prepare a scheme of merger by the transferor or transferee companies based on the due diligence report. The Board of Directors of the respective companies will have to pass a resolution in this regard.

While passing the resolution the scheme shall be considered as so drawn and then, in accordance to the provisions of Companies Act -1994, hold meetings of their respective members to consider and approve, the concerned scheme.

If a majority in number representing three-fourth in value of members present in the meeting, either in person or by proxy, approve the scheme, the same shall be deemed to have the approval of the members.

Step 7: Scheme Submission to Bangladesh Bank

Thereafter, an application will have to be submitted to Bangladesh bank by the transferee company. In addition to the application, a copy of the Scheme of merger/amalgamation, together with such other documents will have to be submitted.

Other documents include:

1. Name, address and occupation of the Directors of the transferee company as proposed to be reconstituted after the amalgamation
2. Details of the proposed Chief Executive Officer of the transferee company after the amalgamation.
3. Post-merger Branch Plan, Technology Plan, Human Resource Plan and proposal to address Corporate Governance issues.

   Information relevant for consideration of the scheme and the swap ratio including the following:

- Valuer Report explaining the method of valuation and the justification for it. If market value of shares has been considered in computation of swap ratio, the value so considered,
- Last three years annual report of each of the companies,
- Financial results, if any, published by companies covering the periods subsequent to the Annual reports
- Significant anticipated changes in service and products.
- Pro forma combined balance sheet of the transferee company as it will appear following the amalgamation,

  Computation based on pro forma balance sheets of the following items:

- Tier I Capital
- Tier II Capital
- Risk weighted assets
- Gross and net Non-Performing Loans
- Ratio of tier I capital to risk weighted assets
- Ratio of tier II capital to risk weighted assets
- Ratio of tier I capital to total assets

- Ratio of total capital to risk weighted assets
- Ratio of gross and net NPLs to advances.

Any other information or explanation as sought by Bangladesh Bank.

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- Step by Step Process of Registering a Company in Bangladesh

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Here is a table outlining the process of mergers and acquisitions in Bangladesh:

Step	Description	Relevant Law	Figures
1. Pre-acquisition planning	The acquiring company conducts due diligence on the target company and develops a plan for the acquisition.	Companies Act 1994, Securities and Exchange Ordinance 1969, Bangladesh Competition Act 2010	The acquiring company may need to engage legal, financial, and other advisors to assist with the planning process. The cost of these services may be significant.
2. Negotiation and agreement	The acquiring and target companies negotiate and agree on the terms of the acquisition, including the purchase price and any conditions that must be met. These terms may be set out in a letter of intent or a term sheet.	Companies Act 1994, Securities and Exchange Ordinance 1969, Bangladesh Competition Act 2010, Contract Act 1872	The purchase price may be paid in cash, securities, or a combination of both. The terms of payment may be negotiated between the parties.
3. Regulatory approvals	The acquisition may need to be approved by regulatory bodies, such as the Bangladesh Securities and Exchange Commission (BSEC) and the Bangladesh Competition Commission (BCC).	Companies Act 1994, Securities and Exchange Ordinance 1969, Bangladesh Competition Act 2010	The BSEC may require the acquiring company to make a public announcement of the acquisition and provide certain information to the market. The BCC may need to review the acquisition to ensure it does not result in a substantial lessening of competition.
4. Shareholder approval	The acquisition must be approved by the shareholders of both the acquiring and target companies. This may require a vote at a general	Companies Act 1994, Securities and Exchange Ordinance 1969, Bangladesh Companies Act	The shareholders of the target company may be entitled to receive compensation for their shares in the form of cash, securities, or other assets. The amount of compensation may be

Step	Description	Relevant Law	Figures
	meeting of shareholders.	1994	determined by the purchase price negotiated between the parties.
5. Completion	The acquisition is completed and the target company becomes a subsidiary of the acquiring company.	Companies Act 1994, Securities and Exchange Ordinance 1969, Bangladesh Companies Act 1994	The target company's assets and liabilities are transferred to the acquiring company, and the target company's shares are cancelled. The acquiring company may also need to register the acquisition with the relevant authorities, such as the Registrar of Joint Stock Companies and Firms.
6. Integration	The acquiring company integrates the target company's operations, including its employees, systems, and processes.	Companies Act 1994, Securities and Exchange Ordinance 1969, Bangladesh Labor Act 2006	The integration process may involve restructuring, cost-cutting measures, and other changes to the way the combined company does business

Step 8: Draft Scheme Examination

After receiving the draft Scheme, Bangladesh Bank will satisfy itself that the Scheme as proposed by the transferee company can be implemented successfully. In deciding such, Bangladesh Bank will consider various factors through examination of the scheme. The factors that may be considered are the capital of the merged entity, valuation of assets and liabilities, the impact on the profitability etc.

Step 9: Assets and liabilities valuation

It is upon the merging companies to mutually agree the valuation of the assets. Bangladesh Bank does not generally interfere in this regard except where there are reasons to believe that the valuation is not fair and reasonable. If mutual agreement is not possible in relation to certain items then any of the parties to the merger can seek advice of Bangladesh Bank.

The Bangladesh Bank plays the role of a mediator and help resolve the differences. In case the mediation fails, the Bangladesh Bank will decide the value and the decision of the Bank in this regard shall be binding. The cost of obtaining such advice will be borne by the transferor company.

In a case where mutual agreement has not been possible in relation to certain items for example:

(a) Valuation of a particular asset

(b) Classification of any advance
(c) determination of any liability or any like issue, the bank / financial institution, shall highlight those areas and seek advice of Bangladesh Bank.

Step 10: Transaction Price in Mergers and Acquisitions in Bangladesh

Again the transaction cost/price is a matter to be mutually agreed between the transferor and the transferee on the basis of fair valuation of assets and liabilities proposed to be transferred.

Parties have the option to fix the price at a premium or discount to valuation. However, Bangladesh Bank have a right to be satisfied that the mutually agreed price is fair and reasonable.

For this purpose, Bangladesh bank may ask for pricing rationale to examine the same and accept or suggest alteration. In order to do so Bangladesh bank will seek explanatory note on price mechanism along with supporting documents.

Step 11: Bangladesh Bank approval in Mergers and Acquisitions

At this stage, Bangladesh bank will approve the Scheme as proposed if two conditions are satisfied. It can be implemented:

- to the benefit of the company and/or the financial system of the country and
- the scheme is not detrimental to the interest of the depositors

Thereafter, Bangladesh Bank may give its approval to the said Scheme with or without such modifications as deemed necessary.

"For this purpose, Bangladesh bank may ask for pricing rationale to examine the same and accept or suggest alteration. In order to do so Bangladesh bank will seek explanatory note on price mechanism along with supporting documents."

Step 12: High court petition in regards to Mergers and Acquisitions in Bangladesh

After the scheme of merger/amalgamation has been permitted by Bangladesh Bank, the transferor and the transferee now must comply with other formalities required under the Companies Act 1994. As such they need to file an application before the High Court and submit the scheme for the merger/amalgamation.

In addition, the transferee company will mark a copy of the application as filed before the Court together with annexure, if any, to Bangladesh Bank and will keep the Bank informed from time to time as the progress in the matter.

If the company, after obtaining approval of the Scheme from the Bangladesh Bank, fails to take these steps within the next three months from the date of approval, the approval so granted lapses, unless otherwise extended on justifiable consideration.

The high court will hear the application for merger/amalgamation and considering the objections if any, raised by any of the stakeholders. As such, based on that the Court may with or without such modification as it deems fit approve the Scheme.

Step 13: File certified copy of High court order to RJSC

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Restructuring For Large Corporations: Process

Many large, international corporations are like huge sea tankers carrying oil. It is difficult to change their collision course quickly and avoid hitting objects that stand in your way or react properly to unexpected market circumstances. Large organisations tend to follow routine, gain "organisational fat" and play th
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[Remember, your journey starts with the right talent! Get started today]

This knowledge is brought to you by organizational restructuring expert Witold Kowalski, just one of the thousands of top business management consultants on Expert360.

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Introduction

Many large, international corporations are like huge sea tankers carrying oil. It is difficult to change their collision course quickly and avoid hitting objects that stand in your way or react properly to unexpected market circumstances.

Large organizations tend to follow routine, gain "organizational fat" and play the same game that made them successful in the past. However, the global market and consumer trends evolve so quickly that corporations cannot afford to do business as usual. If they want to play big roles in the market or even survive, they have to firm organizational restructuring processes in place.

Business restructuring (or organizational restructuring) is a process that can address a company's unsatisfactory status quo in the constantly evolving market. It should be based on **proper strategic planning**, fuelled by innovation, or it can be a **tactical reaction** to unexpected circumstances.

The final sections of this article will detail some real-life case studies of restructuring I encountered during my time as the CEO of Nike Poland.

Strategy first

A strategy is about creating a long-lasting competitive advantage by focusing on key priorities to succeed. It can be written on a piece of paper only accessible by a company's top management team or a clear template given to each and every employee to follow.

An organizational restructuring process has to be rooted in corporate strategy.

You cannot predict everything, but a strategic approach can help you react better. Wherever you plan to go, you should know where 'north' is. Tactical organizational restructuring can work and is sometimes necessary, but if you do not see the long-term vision on the horizon, you may end up in the wrong place.

Being active or reactive

The proactive approach to reorganisation is a virtue of **market leaders**.

It is the way to change the rules of the game. Market leaders follow market trends, but also create them.

Having strategic initiative is extremely important in any market, just like in war. All famous business leaders and military commanders were always prepared for constant attack and ready to restructure organisations/troops to address unforeseen problems.

A reactive approach to reorganisation is an adaptation to the actions of market leaders or to market developments, which is a strategy that often adversely impacts any company's financial situation.

Reactive companies usually act **too late**. However, it's better to react late than never.

Why Do Companies Restructure?

Nowadays, companies have to be consumer-centric if they want to succeed.

As Nike likes to say: "consumer decides". If consumer behaviors' evolve, companies need to adjust their organisations to address these changes. Following and creating consumer trends through periodic adjustment can be considered as a non-financial reason for reorganisation.

In fact, if restructuring is part of a company's strategy, it will have a direct impact on long-term financial results.

Examples of internal reasons behind corporate restructuring

Profitability below expectations:

- Stagnant or decreasing revenues,
- Too low gross margin,
- Too high operating costs,
- Bad cash flow,
- Over- or under-investment,
- Productivity/KPIs below market standards,
- High labour costs,
- Unclear roles & responsibilities,
- Poor internal communication,
- Lack of leadership,
- Bad design of processes,
- Marketing budgets allocated ineffectively.

Of course, there are some "easy" ways in which one can address the low profitability problem, for example, through headcount reduction or closing unprofitable stores/branches/facilities/countries.

As large organisations tend to grow in an uncontrolled way, such cost cuts may help. Nevertheless, simple cost-cutting exercises may jeopardize the long-term market position of companies affected by such restructuring. It is much more difficult to increase profit by growing revenues, gross margin and through cost optimizing, all at the same time.

Such restructuring process is very complex, time-consuming and often requires top management to **get out of its comfort zone** and to apply strategic thinking. A lack of strategic approach in corporate restructuring is short-term **problem fixing** or **"fire fighting"**.

You should not forget that "corporate politics" are sometimes the driving force of some organisational restructuring requirements. Some of the transformations have just one goal for top management: to gain more time to stay at their position as long as possible. It is false, but usually minor, scale restructuring.

Examples of external reasons behind corporate restructuring

- New consumer trends
- Innovations that redefine the market
- Company's market share decrease due to actions of competition

Most companies declare their commitment to address market changes in their strategies, but not many of them really realize this goal in practice.

Deep organisational restructuring is not an easy fix and requires radical changes in distribution network, channel management, supply chain, HR policy, production and its sourcing, communication with consumers, product/category management, etc.

Common Obstacles To Restructuring

Resistance from employees

Successful restructuring process requires support of the majority of company's employees from all levels. The **flow of internal communication** should be from top to bottom of the organisation, but also from the opposite direction.

We do not realise how much the middle and lower layers of each organisation know about how to make positive changes to their organisations and impact the overall process of organisational restructuring.

Every employee has certain psychological limitations, own comfort zone, old habits, limiting beliefs, etc. During restructuring process, employees and managers go through the process presented in Figure 1 below.

Corporate obstacles

Many corporations are never fully ready for deep, advanced forms of organisational restructuring. That is why many of them are not successful. We do not live in an ideal world and there is gain without pain or mistakes.

However, realising the elements that have to be fixed to make any restructuring successful may help managers prepare better.

To make organisational restructuring processes successful, companies need clear vision (as part of the strategy), should seriously take care of the human aspect of the process (knowledge and motivation), have sufficient resources and a realistic and actionable template for its implementation.

Actionable Steps For The Restructuring Process

The scopes of the restructuring process can vary a lot. There are organisational restructuring efforts with short implementation times, and which are extended even for years. “One size fits all” approach can be a big mistake.

Once the test phase is completed, sometimes after going through many cycles, full restructuring can be implemented. In fact, it is not a process with a predetermined end, but a stream of continuous cycles of improvements.

Figure 4: Organisational restructuring as a process of constant improvements. Source: Adaptation of Management Cycle Concept [/caption] The following detailed, actionable steps serve as an application template for short-term restructuring projects

1. Planning Phase

- **SMART objectives, ROI**

Restructuring makes sense only if profitability and market position are improved. The business objectives should be ambitious, but realistic, time bound, specific and clearly measured.

- **Budget for restructuring**

Without a sufficient budget, any restructuring is “mission impossible”.

- **Internal communication to gain team’s support & give/get ongoing feedback**

Incorrect/poor communication of the process creates chaos.

- **Project team creation: x-functional, x-country**

The project team should include all key people who are needed to make the project successful.

- **One fully dedicated project manager/coordinator**

“Shared” responsibility does not work in restructuring.

- **1 “sponsor” from top management team who will support the process**

Without support from the top management level, the process can get stacked easily.

- **1 person responsible for each country**

For multinational restructuring, the voice from the country level with first hand, local knowledge should be heard.

- **Project management tools and procedures in place**

Project management tools should be used, especially in complex projects. A company can use existing procedures or create new ones.

2. Implementation test phase

- **Test phase for one country, area, division, function, head office, etc.**

Small-scale tests are needed to avoid the risk of big and costly mistakes affecting the whole organisation.

3. Measuring & analysis of test phase

- **Measuring results against SMART objectives**
- **Corrections of initial plans, if necessary**

This is the most important part of organisational restructuring process in its implementation phase. If a test is not successful, the whole organisational restructuring is in danger.

4. Full rollout

- **Measuring results against SMART objectives**
- **Corrections to implementation**

Large implementation projects are never mistake free. Companies should be ready to make the necessary corrections, as many times as needed.

Typical mistakes in the planning and implementation of the organisational restructuring process

Some project objectives **do not meet SMART criteria** and results of restructuring are **not fully measured and analysed properly**. In such a case, it is easier to "sell" a doubtful project as a success.

Insufficient internal communication destabilises the organisation too much during the process.

Limited co-ownership of the project at all organisational levels negatively affects the implementation. Restructuring is **not rooted in the company's strategy**.

In the worst case, scenario restructuring is tactical, with vague objectives, planned at top level only, without collecting feedback from all levels of the organisation, and with diluted responsibility. A great recipe for total failure!

Organisational Restructuring Case Study From Nike, Inc.

Nike Inc. is a globally recognised company as a world's leader of the sports market, famous for product and organisational innovations, with a globally known brand and sport marketing assets.

It can serve as a perfect example and inspiration for numerous organisational restructuring processes implemented in its 40-year history. The author of this post – Witold Kowalski – was a General Manager of Nike Poland and a member of Nike's CEMEA management team for 13 years and has experienced Nike's evolution over that period.

The following are case studies of Nike's organisational restructuring projects, selected by him.

From business units to category management

Nike started as a company selling **footwear for runners**. After some years, they added sneakers for other sports categories like **soccer, sportswear (lifestyle), tennis, basketball, x-training, women's fitness and American football**.

Nike quickly realized that its consumers need specialized apparel and equipment to practice their sports, so the two business units were added to the product portfolio. The company's organisation reflected all these changes by including "business unit" departments: **footwear, apparel and equipment** for all sports to typical functional divisions.

At a later stage, Nike's top management decided to organize the company by **sports categories**. The main reason was that, for example, products for soccer differ significantly from products for running by product range, expertise needed, distribution channel, sports assets, product features, places where consumers play, etc.

Each category is a **different "field of play",** where producers compete to win the hearts of each category consumers. It was much easier to respond to consumer needs and to grow distinctive category markets when the organisation reflected the category approach. Each sports category division includes footwear, apparel and equipment, but has also a team to manage category marketing, retail, visual merchandising, product development, and so on.

Nike's organisational evolution from a business unit organisation to sports category set up is a great example of how a company can adjust to meet consumer needs better and grow business at a very fast pace.

Such an approach helped Nike become number one globally and in each sport "field of play". The transformation from footwear to BU divisions took several years, but the reorganisation from BU to categories was executed within 1 year.

Nike's mission to serve and inspire athletes from all over the world ("if you have a body, you are an athlete") helped the company make the right organisational decisions and redefine a service model in the industry.

The competition followed by doing the same but was unable to regain strategic initiative.

Geographic expansion: an example of CEMEA region

Nike was established in Oregon, USA. It soon expanded to all other states and then started the business in Western Europe and on other continents. For CEMEA region (Central Europe, Russia, Turkey, Israel, Middle East and Africa), Nike picked Poland as the first, test country for the region.

With the help of shared services in Nike's European headquarters in Holland and central warehouse for Europe in Belgium, Nike Poland was opened as their own, buy-sell subsidiary. After one year of tests, the country's opening pattern was applied for other countries of CEMEA region, one after another.

Poland was treated as a training and knowledge centre for other countries' teams. Before Nike's rollout of its own subsidiaries, these markets were serviced by **ineffective, exclusive distributors** who were not able to promote Nike brand and grow revenues the Nike way.

Each CEMEA country had its own customer service in the European headquarters, CEMEA functional and category teams and centralized supply chain model.

With its **own subsidiaries** in each CEMEA county, Nike was able to offer better commercial terms to its retail partners, start marketing activities to position the brand properly, grow revenues (for example, with the impressive CARG of 19% during 13 years in Poland).

The big organisational restructuring innovation was the **European headquarters as a service centre** for all European countries which enable countries to be less staffed, more focused on sales and with less headcount needed to cover all functional departments in each country.

Nike worked as a **matrix**, where all functional and category positions are represented at all levels (global, geography, country). Marketing activities were integrated across all departments (sales, marketing and retail) and executed in each country, according to **global guidelines**, and with **local adjustments**.

Supply chain: centralization of deliveries

After Nike expanded to Europe and started in some countries with traditional logistics in the first couple of years, instead of having warehouses in each country, **one central warehouse** was built in Laakdal, Belgium, to supply **all European customers from one place**.

All Nike global factories shipped their products to Laakdal, and then, outsourced logistics companies delivered seasonal orders to the doors of Nike European customers. In the 90s, opening a huge warehouse facility in the middle of nowhere in Belgium, but close to the sea ports was a huge supply chain innovation, which simplified logistics and was a **labor and operational cost saving** compared to having warehouses in each country.

The system did not work perfectly from day one, but gradually, Nike made it very functional and partly automated.

From “prop” to “futures” orders

In the early stage of its development, Nike met the demand by collecting orders from customers, ordering production at factories and delivering products to customers.

The idea of making customers order products, with the help of **product samples and catalogues, 6 months before each of 4 seasons** was revolutionary. It enabled better demand-based, supply planning, with less cash and logistics constraints. This system called **“futures” ordering**, as opposed to **on-demand “prop” system**, has changed Nike’s organisation dramatically.

Instead of collecting orders by Nike’s sales force during visits to customers, Nike built a network of **unified showrooms in each country**. Nike’s sales force presented new seasonal collections to customers in a similar way, with similar visual merchandising support, and well ahead of their delivery to the market.

From a wholesale model to direct-to-consumer

Any success in business depends on good interaction with consumers and a high gross margin. As the founder of Nike, Phil Knight, used to say: “Once gross margin is good, everything else can be fixed”.

In the past, the main business partners for Nike were: **key accounts** like Footlocker, Intersport, Decathlon, El Corte Ingles, Sports Direct, JD Sport, Go Sport, Bata, mid-size **“field” accounts** and **Small Value Accounts**. Nike sales departments clearly reflected that approach.

In a way, Nike was partly dependent on the customer experience that their partners offered. Many of them were far from being brand enhancers and frequently decreased prices through aggressive discounting. The company did not have its own retail, except for a few Nike Towns or factory outlet stores.

With the growing role of e-commerce and periodic market overstocking due to the aggressive strategic goals, Nike decided to strengthen its direct-to-consumer presence on the global market by opening **Nike-only stores**, its own online store **www.nike.com**, its own **factory outlet stores** and by introducing **category shop-in-shop concept** with key accounts.

These actions required considerable restructuring of Nike organisation to cope with new tasks like channel and space planning, category directive assortments for its own stores, product differentiation in retail, return logistics, among a number of other challenges.

Although the direct-to-consumer approach is continuous learning for Nike, earning double wholesale and retail margins from their own, a brand-enhancing retail stores network was a huge gain for Nike’s P&L.

Selected cost optimization restructuring initiatives

“Shared services” is a concept introduced by Nike to reduce employment by offering 1 central or regional service centre for many countries. It was applied for a group of smaller countries or the whole Nike regions.

The shared services were applied to HR, customer service, logistics, IT, procurement, etc. It is nothing new these days, but 20 years ago, it was a very innovative solution.

Global or regional **headcount reduction** is a bit primitive type of reorganisation to reduce labour cost. Nike executed it when the organisation gained excessive “fat” while revenues and gross margin did not grow as planned. When the top line went back to normal and headcount limits were eased, the total number of headcount usually came back to the number from the previous level or more.

“10 per cent cut in costs” was Nike’s initiative to reduce excessive operational costs at country’s or regional level. This task was surprisingly easy to execute by Nike countries, despite their initial resistance, as long as the exercise was not repeated in the following year.

Conclusion

When you find out about some of Nike’s internal slogans like **“Evolve immediately”**, **“Nike is about to change”**, **“There is no finish line”**, you will understand that evolution or prompt reorganisations were and are an **ordinary practice** at Nike.

The company made several mistakes on its way, but constant product and systems innovation as part of a bold strategic plan gave Nike a permanent, competitive advantage in the market. Nike always behaved like a market leader and was able to quickly adjust its organisation to serve consumers better than its competition.

Reorganisation is a necessary process to respond to external market developments or to take any company to the next, higher level.

It is the company’s friend if executed properly.

How to Increase the Net Worth of Your Business

1. Financial Management, Planning, and Analysis. ...
2. Developing and Executing a Marketing Strategy. ...
3. Boosting Customer Service Excellence to Increase the Business's Net Worth. ...
4. Streamlining Supply Networks. ...
5. Workers and Talent Management. ...
6. A Technical World. ...
7. Things You Can Do Today.

The end goal for any investor or company owner is always to increase their net worth. For many investors and entrepreneurs, building a self-supporting business portfolio with substantial returns is the primary challenge.

Many financial analysts argue that there is little correlation between technology and the company's improved financial performance.

However, they also argue that if well-utilized technology and business applications can help improve its net worth. Improved financial performance in many technology firms is centered around the exploitation of innovative services and products which push them to make a strong investment in research and development. Business applications are also sometimes used in the company's operations.

95Visual has established itself as a leading provider of custom websites and Drupal development. We offer unique custom Drupal themes to give a fresh look and to fully customize your business's website.

Additionally, 95Visual provides custom web applications to help optimize and streamline your business operations. 95Visual also provides custom business software which helps in redefining the company's operations. This helps in avoiding redundancy and unnecessary tasks. But how are these technologies and applications essential in improving a business's net worth?

Financial Management, Planning, and Analysis

Some business applications and software are used to control costs. A company's workflow depends on how fast decisions are made. Financial management and planning software help managers make decisions and plan quickly based on real-time financial data.

These applications are used for strategic planning, forecasting, budgeting, analyzing financial information, and enterprise performance management among others. These help the company in increasing tracking and checking on costs, improving its profitability and aligning its operations in line with its strategy.

Developing and Executing a Marketing Strategy

Some business applications and software help companies tailor their energy and resources towards a single marketing strategy. They do this by assisting in managing expenses and budgets as well as make real-time adjustments to their sales strategies and also increasing their pitching capacity.

These applications also enable companies to quickly react to opportunities in the market, improve transparency and evaluate performance. Companies can effectively align demand against sales by generating and nurturing leads and converting them into sales.

The business software enables companies to design and manage marketing campaigns and swiftly adopt strategic decisions basing on Return on Investment (RoI) and performance. By increasing partnerships with agencies, vendors, and partners, a company can share ideas and crowd source the best ideas and tips.

Boosting Customer Service Excellence to Increase the Business's Net Worth

Digital applications enable companies to understand their customers and to solve their problems in a quick and efficient way. This way, businesses can go beyond customer expectations, offer added value and win their loyalty. This, in turn, translates to additional revenue and increases the business's net worth.
Tailoring Production to Customer Needs

By using business applications, a company is able to engage customers with relevant information and offers meant to boost the refined sectors. The company can understand market niches and produce according to demand and schedule.

Streamlining Supply Networks

The company is also able to optimize its supply channels which helps strengthen the partnership with the suppliers and enforce compliance. The company can shorten planning cycles, reduce inventory levels, and beef up the quality of service to supply.

This way, the company operates on a consumer-driven, scalable, flexible and cost-effective platform. All of this translates to improved efficiency, increased production and cost-cutting, and improved business's net worth. Business supply applications enable companies to keep in touch with suppliers as well as outsourced manufacturers from several supply networks.

The company also has seamless collaborations across demand, supply, as well as inventory replenishment processes. By keeping in touch with suppliers and consumers, the company is able to actively react to change in demand and supply shortages. In short, the company proactively plays the intermediary role linking between the supplier and consumers.

Workers and Talent Management

By using the right applications and software, a company is able to hire, train, and develop the right talents. Additionally, the company is able to improve the level of engagement among its employees as well as business outcomes by retaining only the right skills and talents on board.

These pieces of software offer HR managers the right tools to easily measure, proactively act, and clearly communicate ability results as well as impacts to the business.

Companies are also able to accelerate and automate workforce attendance and time management.

Employees are empowered to effectively and efficiently manage time-related information even on mobile devices. Managers can also access information from team members, and quickly approve requests for time off.

Time, record planning, and absence planning are efficiently taken care of using business software. Human capital analysis applications enable the manager to improve employee results as well as reduce risks.

A Technical World

Today's world is largely based in the technical realm. Even those who have businesses centered around the arts need to invest in tech and business applications to be noticed by the world. Not investing in these things can make your business standstill, and even fail, while the rest of the world quickly leaves you behind. Things like custom business applications and project management software doesn't need to be confusing. Let's take a look at the most important things you need to do in order to grow.

Project Management Software

Nearly sixty percent of business executives in one survey replied that "having a strong project management system in place was essential for business growth." In addition, according to the Economist Intelligence Unit survey "Ninety percent of global senior executives ranked project management methods as either critical or somewhat important to their ability to deliver successful projects and remain competitive."

Project management software offers many advantages. It is the best way to make sure your projects stay on track, which creates dependability in the eyes of your customers. Such a system keeps you from wasting time, overspending, and being able to manage several of the aspects of a project all in one place.

Build a Brand

People don't only need to be able to find you but they also need to be able to remember you. Building a strong brand puts you ahead of the competition in that it is you and your company that comes to mind first when people are in the market for what you have to offer.

Your business's net worth is strongly dependent upon not only the money you make but also the ability you have to bring customers back to you time after time. By developing a strong brand, you help let people know that you exist, and you build trust, which is absolutely necessary for a successful business. This will cement the idea that you are connected to your product or service in people's minds. Building a brand is something you need to do, now.

Increase Assets

Increasing assets involves increasing the money-making aspects of your business so they can exceed your costs. Increasing assets can vary from hiring more highly-trained employees to utilizing custom created software that helps put you ahead of the competition by helping your employees work faster and more efficiently.

Specialize

Too often you see companies that want to spread their knowledge over many different areas in order to reach a wider audience. This is actually a mistake. By spreading your efforts, you are unable to give the full attention to any one aspect of the business and this creates a mediocre product or service. By specializing, you are able to perfect that one thing to the point where no competition can compare. This creates a situation where you are the go-to person because you gain a reputation for quality.

Things You Can Do Today

Increasing your business's net worth is something that won't take place overnight. There are things you can do now, however, that will set you on the correct road. Today, you can start increasing your net worth by:

1. Investing in a decent project management system.
2. Finding out where custom software can help improve production and working on that.
3. Take time to set up social media accounts and start strengthening your brand.
4. Update your website so that it’s optimized for search results and has enough pull to convert visitors into buyers.

Owing or investing in a business can be done for many reasons, but ultimately the goal is to increase the business's net worth in order to realize an increasing profit. The Internet is full of information meant to help you do this, but weeding through all the information to find the things that can be applied to your particular situation is often time-consuming and frustrating. It is our hope that this will help make your quest to increase your business's net worth easier.

Company Accounts

A company is a voluntary association of people who contribute money for a common purpose. A company is an artificial person and a separate legal entity. Let us now understand the basic concepts of company accounts. The contribution of money by people forms the capital of the company and the contributors are its members. Hence, the capital of a company is known as share capital and the contributors as shareholders. Indian Companies Act, 2013 governs all companies and provides guidelines for them to adhere to.

Basic Concepts of Company Accounts

Meaning of Shares

Section 2(84) of the Companies Act, 2013 defines share as a share in the share capital of a company and it includes stock. The share capital of a company is divided into units of smaller denominations. Each such unit is called a Share. It entitles the holder to ownership in the company.

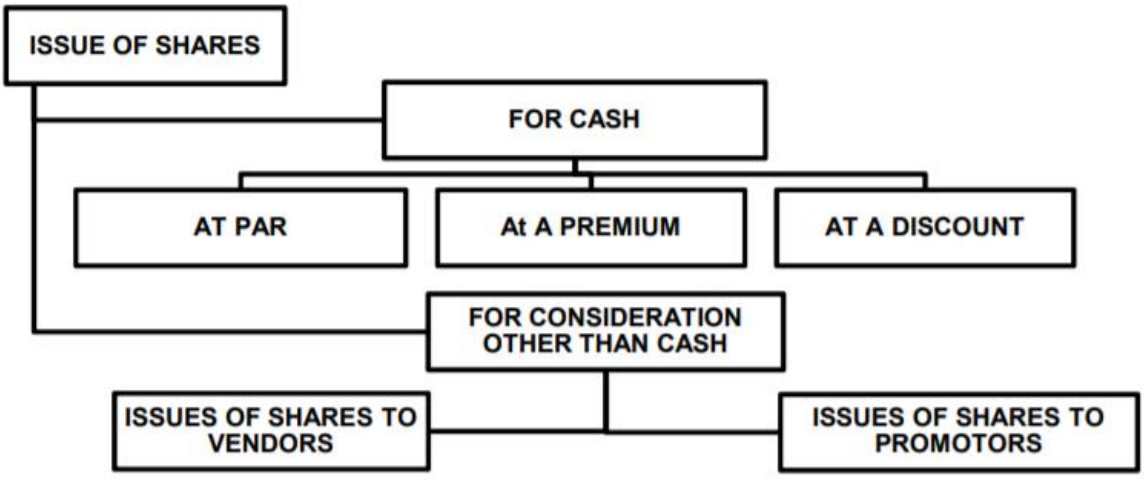
Browse more Topics under Introduction To Company Accounts

- Issue of Shares for Cash
- Issue of Shares for Consideration
- Under and Over Subscription
- Calls-in-Advance
- Calls-in-Arrears
- Issue of Shares to Promoters
- Forfeiture of Shares
- Reissue of Shares
- Issue of Debentures
- Issue of Debentures as Security
- Issue of Preference Shares
- Capital Redemption Reserve Account

Types of share capital

As per Section 43 of the Companies Act, 2013 Share Capital of a company can be of two types:

1. Equity Share Capital
2. Preference Share Capital



(source – icai)

Equity Share Capital

It consists of equity shares. Equity Shares are shares which are not Preference Shares. These carry maximum 'risks and rewards' of the business. In the case of high profits, they receive a payment of higher dividends and appreciation in the market value of the shares.

While, in the case of loss, there exists a higher risk of losing part or all the shares. Equity Share Capital may be with the voting rights or with the differential rights related to dividend, voting or any other right.

Preference Share Capital

Preference Share Capital consists of preference shares. As per Section 43(b) of the Companies Act, 2013, preference shares are shares which carry preferential rights. The preferential rights of preference shares are:

1. Preferential right to receive dividend: This implies that the company will first make payment to a person holding preference shares at fixed rate or amount and then to the equity shareholders. Thus, they receive dividend before Equity Shareholders.
2. Preferential right to repayment of capital: On the winding up of the company they receive the repayment of capital before paying the equity shareholders.

Deemed Preference Share Capital

The capital will be deemed to be preference share capital when it has either or both of the following rights:

1. In addition to the preferential right to payment of dividend, it possesses a right to participate. However, the right to participate may be fully or to a limited extent.
2. In addition to the preferential right to repayment of capital, it possesses a right to participate. However, the right to participate may be fully or to a limited extent.

(source – novojurislegal)

Types of Share Capital shown in the Balance Sheet

Authorized or Nominal Capital

It is the amount of capital with which a company registers itself and also states this amount in the Memorandum of Association. It is the maximum amount of capital beyond which a company cannot issue shares to the public.

However, a company may issue shares of an amount more than the Nominal Capital, if it increases the Nominal Capital by altering the Capital clause in the Memorandum of Association.

Issued Capital

It is the amount of capital which a company offers to the public for subscription. Also, it includes the shares that a company allotted to the vendors or promoters of the company for consideration other than cash.

In the Balance Sheet, under the head Issued Capital, a company needs to state the different classes of share capital including the sub-classes of the preference shares, the date and the terms of the redemption or conversion of redeemable preference shares and any option on un-issued share capital.

Subscribed Capital

It is the amount of capital for which the company receives the subscription from the public and makes the allotment to them. It can be equal to or less than the Issued Capital.

Called-up Capital

It is the amount which the company calls from the shareholders to pay on the shares. Usually, a company does not call the full amount at once from the shareholders.

Hence, the portion that the company calls is called-up capital and the remaining portion is un-called capital.

Paid-up Capital

It is the amount that is paid by the shareholders. This is the amount that we include in the Balance Sheet total. It may be less than or equal to the paid-up capital.

Solved Example For You

Explain the various classes of preference shares.

Ans. The various classes of Preference shares are:

1. *Cumulative Preference Shares:* These are Preference Shares which carry right to receive arrears of dividend before the company makes payment to Equity Shareholders.
2. *Non- Cumulative Preference Shares:* These are Preference Shares which do not carry the right to receive arrears of dividend.
3. *Participating Preference Shares:* The Articles of Association may provide that after paying the dividend to the Equity Shareholders, the Preference shareholders will also have a right to participate in the remaining profits. Thus, the Preference Shares carrying this right are Participating Preference Shares.
4. *Non-Participating Preference Shares:* These are Preference Shares which do not carry the right to participate in the profits remaining after paying the Equity Shareholders.
5. *Convertible Preference Shares:* These Preference Shares have a right to conversion into Equity Shares.
6. *Non-Convertible Preference Shares:* These Preference Shares do have a right to conversion into Equity Shares.
7. *Redeemable Preference Shares:* These Preference Shares are redeemable by the company at a specific time (not exceeding 20 years from the date of issue) for the repayment.
8. *Irredeemable Preference Shares*: These are not redeemable and thus, the company pays the amount only at the time of the winding up of the company.

COMPANY SECRETARIAL PRACTICE IN BANGLADESH :The word 'Secretary' is derived from the Late Latin 'secretarius' meaning 'confident' one on whom secrets are entrusted'. It indicates one aspect of duties of such post "The profession of secretary is one of the oldest in governance that wherever there a man or entity of action, there too was a man of pen to record the deeds[a manual of secretarial practice]

Legal status

ording to The Companies Act, 1994, Section 2(u) - �Secretary�means- �any individual possessing prescribed qualifications appointed to perform the duties which may be performed by the secretary r this act and any other ministerial or administrative duties�

Scope of work of a Company Secretary

1. Company Secretaries works at the centre point of the decision making process in an organisation, which is a powerful position of influence.
2. Generally the Company Secretary assists and guides the directors in their quest of profit and growth but also act with integrity and independence to protect the interests of the company, its shareholders and employees.
3. Today's Company Secretary plays a pro-active and central role in the governance of the company. This requires excellent communication skills, a thorough knowledge of the company's business and applicable regulations, strength of character, integrity, and above all a professional approach.
4. The appointment of Company Secretary is the responsibility of the board of directors; yet despite this legal requirement, the law, whether in the form of the Companies Acts, does not state overtly what the Company Secretary should do once appointed.
5. The limited number of references to the Company Secretary in the Companies Acts and in some circular by Securities and Exchange Commission (SEC) might lead a person newly appointed to the post to underestimate the scope of the responsibilities acquired.
6. All directors should have access to the advice and services of the Company Secretary, who is responsible to the board for ensuring that Board procedures are followed and that applicable rules and regulations are complied with.
7. Any question of the removal of the Company Secretary should be a matter for the board as a whole. Company Secretary is the key to the efficiency and effectiveness of the board and to the smooth running of the company. To fulfill the role, the Company Secretary must not only keep up to date with relevant legal, statutory and regulatory requirements but also be able to give impartial advice and support to directors (in particular, non-executive directors who might not have such detailed knowledge of the company as the executive directors).
8. To distinguish between the duties which all Company Secretaries should perform (core duties) and those which they often perform (additional duties).Core duties are defined as those for which the Company Secretary is responsible as an officer of the company and those undertaken by the Company Secretary as a matter of established and best practice. The list of core duties is therefore a refinement of statute, common law and good practice.
9. There has been an increasing need over the recent years for the Company Secretaries in the corporate sectors.
10. Since long the role of Company secretary is recognized by the developed countries but in Bangladesh there are so many invisible obstacles to get the Chartered Secretaries Act approved/passed by the parliament. As we know that it is better if we can set one or more

control points in business houses to check every unlawful activity by the other professional services or management of a company.

11. This type of control points can help Government to check whether the company comply every legal obligation, Owner to check if there is any malpractice or fund defalcation, employees to get their wages paid appropriately and shareholders to have their dividend on timely and in terms of amount actually.
12. As the secretary is an officer of the company, they may be criminally liable for defaults committed by the company. The liability could include failure to file: in the time allowed; any change in the details of the company's directors and secretary; and the company's annual return.

The company secretary generally performs following duties

1. To maintain statutory registers of members, directors and directors' interests
2. To ensure statutory forms to file & submit promptly & properly
3. To Send the Registrar copies of resolutions and agreements
4. Tosafeguard and protect such interests of the company at all levels viz. legal, statutory, administrative, arbitrational and in other policy matter
5. On approval of Board-
   i. To convene Board or Shareholders meetings in time
   ii. To sign notices of such meetings
   iii. To send annual and half yearly accounts to shareholders
   iv. To prepare minutes of the meeting timely and correctly
   v. To make sure that the quorum requisite is present in the meeting etc.
6. Before execution to verify all agreements/deeds/contracts are properly framed & worded.
7. To work as public relations officer of the company etc.

Role of the Company Secretary

The three main areas, a Company Secretary has the role to play viz. to the Board, to the Company and to the Shareholder. Within each, the Company Secretary’s role can be very diverse.

i. **To the Board**

A Company Secretary must ensure that the procedure for the appointment of directors is properly carried out and assist in the proper induction of Directors, including assessing the specific training needs of directors/executive management. Secretary needs also to be available to provide comprehensive practical support and guidance to directors both as individuals and as a collective with particular emphasis on supporting the non-executive directors. He/she should also facilitate the acquisition of information by all board and committee members so that they can make best use of their ability to have a say to board meetings, discussions etc. Further to these tasks, he/she needs to assist in the compilation of board papers and to filter them to ensure compliance with the required standards of good governance. It may also be part of the Company Secretary’s role to raise matters which may warrant the attention of the board

ii. **To the Company**

Secretary ensures compliance with all relevant statutory and regulatory requirements and that due regard is paid to the specific business interests of the company, for example, a manufacturing company may require a different approach from that of a bank or a financial services company or from that of a charitable company. Secretary also need to assist in the implementation of corporate strategies by ensuring that the board's decisions and instructions are appropriately carried out and communicated. Further to this, he/she should be available to provide a central source of guidance and advice within the company on matters of business ethics and good governance.

iii. **To the Shareholder**

The Company Secretary needs to communicate with the shareholders as appropriate and to ensure that due regard is paid to their interests. He/she also need to act as a primary point of contact for institutional and other shareholders, especially with regard to matters of Corporate Governance.

iv. **Duties as an Administrative Officer**

The Companies Act 1994 imposes numerous obligations on companies regarding, the conduct of their affairs. As an officer of the company, the Company Secretary can be prosecuted for most of these offences. Responsibility for ensuring compliance with these matters ultimately rests with the directors. However, by making the Company Secretary liable, the Act not only recognizes that the directors usually rely on the Company Secretary in this regard, but also provides a strong indication that they should give the Company Secretary responsibility for (or an involvement in) these matters. This is reinforced in the case of public companies by the requirement that the directors appoint as Company Secretary someone they believe is capable of performing the functions. Indeed, a director will often escape personal liability if they are able to show that the breach was not caused by their own acts or omissions and that the board had appointed a suitably qualified Company Secretary with responsibility for these matters. It is clear that, in view of their potential liabilities, Company Secretaries should not close their eyes to cases of non-compliance even if the directors have purported to make someone else responsible for those matters. Company Secretary should draw such cases to the attention of the directors and advise on the company's duties and obligations. It can therefore be argued that the Company Secretary has a duty as an officer of the company to keep an eye on these matters, regardless of the terms of their employment control. Company Secretaries should also ensure that where certain of their responsibilities are delegated, such tasks are properly executed, since they can still be held accountable in law for any failure by the company to comply. The fiduciary duties of directors can apply equally to executives occupying senior management positions in the company and authorized to act on its behalf. This usually includes the Company Secretary who, in any occasion, as an officer of the company has the following fundamental duties:• act in good faith in the interests of the company;• not to act for any collateral purpose• to avoid conflicts of interest• not to make secret profits from dealings for or on behalf of the company.

Core Duties of the Company Secretary

Below mentioned duties includes both those duties which are legal obligations as well as those which result from best practice. Besides, a Secretary may have to use his/her inventiveness to ensure that all core duties are fulfilled.

i. **Meetings of the Board of Directors**
ii. **General Meetings**
iii. **Memorandum and Articles of Association**
iv. **Requirements of Stock Exchanges & Regulatory bodies**
v. **Maintenance of Statutory Registers**
vi. **Statistical Books**

Company Secretary has to maintain the following statistical books also-

a. Application and allotment register
b. Register of share transfer
c. Attendance record book
d. Agenda book
e. Proxy register
f. Index cards for maintaining specimen signatures of members
g. Share certificate and debenture book. etc.

vii. **Submission of Statutory Returns**

Following periodic statutory returns required to file with certain changes, to RJSC, like :

a. **Annual returns (Schedule X):** within 21 days of general meeting
b. Filing of **Audited Accounts :** within 30 days of general meeting with the annual return
c. **Return of Allotment (Form XV):** within 60 days of allotment of shares
d. Amended Memorandum and Articles of Association
e. **Notices of appointment, removal and resignation of directors (Form XII):** within 14 days of any change therein
f. **Consent of Directors to act (Form IX) :** at the time of appointment of director
g. **List of persons consenting to be Directors** : at the time of appointment of director
h. Agreement to take qualification shares in a proposed company (Form XI)
i. Notices of appointment, removal or resignation of auditors
j. Change of registered office (Form VI), within 28 days of incorporation or of any change thereon
k. Special resolution (Form XIII) within 15 days of passing resolution thereof
l. Increase of Authorize Capital (form IV), within 15 days of passing resolution thereof etc

viii. **Report and Accounts**

A Company Secretary has also to co-coordinate the publication and distribution of the company's annual report , accounts and interim statements, in consultation with the company's internal and external advisers, in particular, when preparing the directors' report.

ix. **Registration of Shares**

He/she has to maintain the company's register of members; dealing with transfers and other matters affecting share-holdings; dealing with queries and requests from shareholders and different stakeholders.

x. **Communications to and from Shareholder**

Communicating with the shareholders (e.g. through circulars); arranging payment of dividends, interest; issuing documentation regarding rights issues and capitalization issues; maintaining good shareholder relations; maintaining good relations with institutional shareholders and their investment committees.

xi. **Shareholder Monitoring**

Monitoring movements on the register of members to identify any apparent 'stake-building' in the company's shares by potential take-over bidders; making appropriate inquiries of members as to beneficial ownership of holdings.

Present performers In Bangladesh

Company Secretarial practice are being performed by professionals of � Chartered Secretary (ACS / FCS) Chartered Accountants (ACA/FCA) Cost Management Accountants (ACMA/FCMA) and Experienced Officials of different Disciplines.

Duties of CompS

to work as a Custodian to safeguard interest of the company to work for share issue, transfer to work for deed finalisation & execution to work as a PRO

Responsibilities of CompS

responsible for all lapses, frauds or wrong doing in legal works

responsible for meeting convening different statutory meetings

responsible for maintaining strict secrecy on company info

responsible for filing various statutory returns

responsible for maintaining various statutory registers

responsible for compliance with different authorities like RJSC, BOI, SEC etc

responsible for maintaining statutory time requisite for shareholders notice etc

(Info source : Muqtadir�s Handbook for Company Secretary & www.scribd.com)

Of Audit

An audit is **an examination of the financial statements of a company**, such as the income statement, cash flow statement, and balance sheet. Audits provide investors and regulators with confidence in the accuracy of a corporation's financial reporting.

An audit refers to an examination of the financial statements of a company. Audits are conducted to provide investors and other stakeholders with confidence that a company's financial reports are accurate. Audits also provide regulators with the assurance that a company is adhering to the appropriate legal and regulatory standards.

It's easy to think of an audit as a financial investigation, where a company's financial statements are scrutinized by an external or internal auditor to ensure it is accurate and free of errors. After an audit, the auditor will provide an opinion on whether the financial statements accurately reflect the financial position of the company.

Summary

- **An audit is an examination of the financial statements of a company, such as the income statement, cash flow statement, and balance sheet.**
- **Audits provide investors and regulators with confidence in the accuracy of a corporation's financial reporting.**
- **Once completed, the auditor will provide an opinion on whether the financial statements accurately reflect the financial position of the corporation.**

How It Works

Although there are many types of audits, in the context of corporate finance, an audit typically refers to those conducted on public or private corporations. Government agencies, such as the Securities and Exchange Commission (SEC), require publicly listed companies to conduct an independent audit to validate their annual financial reporting.

For private companies, audits are not legally required but are still conducted to provide investors, banks, and other stakeholders with confidence in the company's financial position. During an audit, different financial statements are examined, such as the income statement, cash flow statement, and balance sheet.

The audit provides stakeholders and regulatory agencies with information on how money is earned and spent throughout the fiscal year. Depending on the size of the company, an audit can span a few months to an entire year. At the end of the engagement, the auditor provides a professional opinion on the accuracy of the financial reporting done.

Internal vs. External Audits

Internal audits are performed by employees within the company. The audits tend to focus less on the financial statements, and greater emphasis is placed on a company's operations and corporate governance.

Internal audit reports are not available to the public but are provided to a company's executives and audit committee to provide an overview of the organization's performance across different areas. The areas can include risk management, internal controls, and compliance.

External audits involve independent auditors hired to express an opinion on the accuracy of a corporation's financial reporting. For public companies, the results of an external audit are reported to the public and are conducted following the Generally Accepted Audit Standards (GAAS).

Most large companies engage with one of the Big Four accounting firms to conduct an audit of their financial statements. To put it into perspective, the Big Four firms audit more than 99% of the S&P 500 companies.

Stages of an Audit

How an audit is conducted can differ depending on the size of the corporation and the complexity of the case. However, an audit usually has four main stages:

- The first stage is the **planning stage**. In this stage, a corporation engages with the auditing firm to establish details, such as the level of engagement, procedures, and objectives.
- The second stage is the **internal controls stage**. In this stage, auditors gather financial records and any other information necessary to conduct their audits. The information is necessary to evaluate the accuracy of the financial statements.
- The third stage is the **testing stage**. In this stage, auditors examine the accuracy of the financial statements using various tests. It may involve verifying transactions, overseeing procedures, or requesting more information.
- The fourth stage is the **reporting stage**. After completing all the tests, the auditors prepare a report that expresses an opinion on the accuracy of the financial statements.

Levels of Audit Engagement

Many companies choose to engage with internal and external auditors in the preparation of their year-end financial statements. However, the depth of the auditor's investigation may vary depending on the type of engagement and the assertion level required.

In a full audit engagement, the auditor conducts a complete and thorough investigation of the financial statements, including verifications of income sources and operating expenses. For example, the auditor may compare reported account receivables with receipts from actual customer orders.

At the end of the engagement, the auditor will provide an opinion on the accuracy of the financial statements. A full audit engagement also provides investors, regulators, and other stakeholders with confidence in a corporation's financial position.

In a review engagement, an auditor only conducts limited examinations to ensure the plausibility of the financial statements. In contrast with an audit, the review engagement only assures that the financial statements are fairly stated, and no further examinations are conducted to verify the accuracy of the statements. Therefore, a review engagement does not provide the same level of confidence in the accuracy of the financial reporting relative to an audit.

In a notice to reader engagement, the role of the auditor is solely to help a company compile its financial information into presentable financial statements. No further examinations are performed, and no opinions are expressed on the accuracy of the financial reporting. Notice to reader engagements is typically only utilized by small corporations without any obligations to external stakeholders.

Of Dividents:

Dividends can be paid in cash or in additional shares of stock. Here's the difference between the two types

Sharon Chin
Apr 13, 2022, 6:42 PM

The majority of shareholder dividends are paid in cash. Alyssa Powell/Insider

- Cash dividends are the most common type of dividend and provide investors with a steady stream of income.
- Stock dividends are when companies issue new shares to distribute to investors, who can hold them or sell them for cash.
- Each type has different income-tax and risk factors to consider.
- Read more stories from Personal Finance Insider.

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Dividends are a way companies distribute a portion of their earnings to shareholders. Stocks that pay dividends are particularly attractive to investors looking for assets that produce regular income for their portfolios.

There are two main ways companies issue dividends.

Cash dividends vs. stock dividends: At a glance

- **Cash dividends** are payments made in cash to shareholders based on the number of shares they hold.
- **Stock dividends** are payments to shareholders made in the form of additional shares of stock.

What is a cash dividend?

Most companies pay dividends in cash. When a company declares a dividend, shareholders who own stock as of a date specified in the announcement are entitled to the payment. The payments are made on a per-share basis. For example, if a company you owned 1,000 shares declared a dividend of 50 cents per share, you would be paid $500.

If you are looking for income from your stock on a regular basis, cash dividends are among the best sources. Dividends are normally declared quarterly, and investors will receive quarterly cash payments. This can be seen as a sort of reward for investing in the company. However, not every company issues cash dividends.

Cash dividend pros and cons

Pros	Cons
• Regular source of income • Can use cash to buy additional shares, providing compounding returns • Dividend-paying companies tend to be more established and stable	• Distributions received are taxable • Cash paid out cannot be used to grow the business • Not as reliable a source of income as interest-paying securities because dividends can be canceled

Example of a cash dividend

Let's look at a real example of a cash dividend. Lowe's board of directors declared a quarterly cash dividend of 80 cents per share, payable on May 4, 2022, to shareholders of record as of April 20, 2022. The ex-dividend date is April 19, 2022, which means you have to own the shares of the company before then.

Let's say you own 50 shares of Lowe's and you bought them for $200 apiece for a total of $10,000 prior to April 19. Since the company declared an 80 cents per share dividend, you will receive a $40 cash dividend (50 shares x $0.80), which will be paid to all shareholders of record on May 4. If the company declares the same quarterly cash dividend each quarter, that equates to a $160 cash dividend received for the year, assuming you still owned only 50 shares of the company.

What is a stock dividend?

This is when the company pays the shareholders with additional shares of stock. This kind of dividend is uncommon. If you don't need income or immediate cash, you can defer the income by selling the stock later. The best scenario is that the stock appreciates in value over this time. The risk is that the stock declines in value.

Stock dividends are typically issued by smaller companies looking to increase liquidity and the number of shares in the market, says George Metrou, an equity portfolio manager at Morningstar Investment Management.

"However, a company paying a stock dividend could be a sign of financial distress and it may signal they are trying to conserve cash," Metrou says. "This is especially true if they were paying a cash dividend and switched to a stock dividend."

Stock dividend pros and cons

Pros	Cons
• Not taxable until you sell the shares • Provides greater portion of ownership of the company • Provides the option to hold onto the stock or to sell it	• Riskier, as it's based on stock performance • Behavioral risk, as investor must decide when to sell • Could be a sign of financial distress

Quick tip: Metrou points out that if the dividend is a hybrid, part stock and part cash, or you have an option between the two, the stock dividend is treated as cash for tax purposes.

Example of a stock dividend

If a company issued a 5% stock dividend, your shares would increase by 5%. If you previously had 1,000 shares in the company, you would now have 1,050 shares.

However, this doesn't increase the value of the company or your stock. Since the dividend is paid in newly created stock, it dilutes the value of the pre-existing shares. This is similar to what happens after a stock split .

Let's say a company had 1 million shares at $20 per share, making its market value $20 million. When it issues more shares, the market value remains the same but each individual share is worth less.

Note: Whether a cash dividend or stock dividend is better depends on the investor's point of view: cash now or later, income tax considerations, and behavioral risk.

"My preference is a cash dividend," says Metrou. "The financial goal is to generate large, reliable and growing streams of income that's the most efficient and direct method. Looking for companies that have a competitive advantage, profitable, sound financials and fundamentals, and a lot of cash. Companies that have a cash dividend is one good method of screening companies to invest in."

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How and When Are Stock Dividends Paid Out?

By

Brian Beers

Updated March 05, 2022

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If a company has excess earnings and decides to pay a dividend to common shareholders, then an amount is declared, in addition to the date when this amount will be paid out to the shareholders. Usually, both the date and the amount is determined on a quarterly basis, after a company finalizes its income statement and the board of directors meets to review the company's financials.

Key Takeaways

- A dividend is the distribution of some of a company's earnings to a class of its shareholders.
- If a company elects to distribute dividends, usually, both the date and the amount is determined on a quarterly basis, after a company finalizes its income statement and the board of directors meets to review the company's financials.
- On the declaration date, the Board of Directors announces the dividend, the size of the dividend, the record date, and the payment date.
- The record date is the day by which you must be on the company's books as a shareholder so as to receive the declared dividend.
- Buy the stock before the ex-dividend date and you get the dividend; buy it on or after the ex-date, and you don't—the seller of the stock gets it.
- The payment date is when the company pays the declared dividend only to shareholders who own the stock before the ex-date.

How And Why Do Companies Pay Dividends?

How Dividends Are Paid Out

A dividend is the distribution of some of a company's earnings to a class of its shareholders. Dividends are usually paid in the form of a dividend check. However, they may also be paid in additional shares of stock. The standard practice for the payment of dividends is a check that is mailed to stockholders a few days after the ex-dividend date, which is the date on which the stock starts trading without the previously declared dividend.

The alternative method of paying dividends is in the form of additional shares of stock. This practice is known as dividend reinvestment; it is commonly offered as a dividend reinvestment plan (DRIP) option by individual companies and mutual funds. Dividends are always considered taxable income by the Internal Revenue System (IRS) (regardless of the form in which they are paid).1

Key Dividend Dates

If a dividend is declared, all qualified shareholders of the company are notified via a press release; the information is usually reported through major stock quoting services for easy reference. The key dates that an investor should look for are:

- The date that the dividend is declared is called the declaration date.
- At the time of declaration, a record date, or date of record, is set. This means that all shareholders on record on that date are entitled to the dividend payment.
- The day preceding the record date is called the ex-date, or the date the stock begins trading ex-dividend. This means that a buyer on ex-date is purchasing shares that are not entitled to receive the most recent dividend payment.

- The payment date is usually about one month after the record date.

On the payment date, the company deposits the funds for disbursement to shareholders with the Depository Trust Company (DTC). Cash payments are then disbursed by the DTC to brokerage firms around the world where shareholders hold the company's shares. The recipient firms appropriately apply cash dividends to client accounts, or process reinvestment transactions, as per a client's instructions.

Tax implications for the dividend payments vary depending on the type of dividend declared, account type where the shareholder owns the shares, and how long the shareholder has owned the shares. Dividend payments are summarized for each tax year on Form 1099-DIV for tax purposes.1

Once a dividend is declared on the declaration date, the company has a legal responsibility to pay it.

Dividend Reinvestment Plan (DRIP)

A dividend reinvestment plan (DRIP) offers a number of advantages to investors. If the investor prefers to simply add to their current equity holdings with any additional funds from dividend payments, automatic dividend reinvestment simplifies this process (as opposed to receiving the dividend payment in cash and then using the cash to purchase additional shares). Company-operated DRIPs are usually commission-free, since they bypass using a broker. This feature is particularly appealing to small investors since commission fees are proportionately larger for smaller purchases of stock.

Another potential benefit of DRIPs is that some companies offer stockholders the option to purchase additional shares in cash at a discount. With a discount from 1% to 10%, plus the added benefit of not paying commission fees, investors can acquire additional stock holdings at an advantageous price (over investors who purchase shares in cash through a brokerage firm).

The Bottom Line

Dividends are a way for companies to distribute profits to shareholders, but not all companies pay dividends. Some companies decide to retain their earnings to re-invest for growth opportunities instead. If dividends are paid, a company will declare the amount of the dividend, and all holders of the stock (by the ex-date) will be paid accordingly on the subsequent payment date. Investors who receive dividends may decide to keep them as cash or reinvest them in order to accumulate more shares.

Related Terms

Dividends: A Complete Guide

A dividend is the distribution of some of a company's earnings to a class of its shareholders, as determined by the company's board of directors.

more

What Is a Spillover Dividend?

A spillover dividend is one in which the year that the shareholder receives payment and the year that the payment is taxable are different.

more

What Is a Dividend Rollover Plan?

A dividend rollover plan is an investment strategy in which the investor purchases a dividend-paying stock shortly before its ex-dividend date.

more

Dividend Reinvestment Plan (DRIP)

A dividend reinvestment plan (DRIP) is an arrangement that allows shareholders to automatically reinvest a stock's cash dividends into additional or fractional shares of the underlying company.

more

What Is Ex-Dividend?

Ex-dividend is a classification in stock trading that indicates when a declared dividend belongs to the seller rather than the buyer.

more

Cum Dividend Is When a Company Is Gearing up to Pay a Dividend

Cum dividend is when a buyer of a security will receive a dividend that a company has declared but

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Saturday, May 14, 2022

Business

BSEC clamps down on unjustified dividend declaration by cos

Staff Correspondent | Published: 22:24, Sep 07,2021 | Updated: 23:08, Sep 07,2021

A file photo shows the Bangladesh Securities and Exchange Commission building in Dhaka. The Bangladesh Securities and Exchange Commission has clamped down on unjustified dividend declaration by the listed companies as many companies have recently declared no dividend while many others declared bonus dividend without proper reasons. — New Age photo

The Bangladesh Securities and Exchange Commission has clamped down on unjustified dividend declaration by the listed companies as many companies have recently declared no dividend while many others declared bonus dividend without proper reasons.

On August 5, the BSEC barred the companies which do not require any business expansion for a particular year from declaring bonus dividend.

The BSEC issued a notification on Sunday in this regard.

Besides, the BSEC has sought explanations from the companies which did not declare any dividend for their shareholders in the past financial year.

BSEC commissioner Shaikh Shamsuddin Ahmed told New Age that the regulator would make the companies accountable for their failure to declare dividend for shareholders.

Companies must not deceive shareholders by declaring bonus dividend or no dividend, he said.

The commission observed that a number of companies made profits in the past financial year but declared no dividend while many others declared bonus dividend even though they did not require any expansion, BSEC officials said.

According to the new notification, a company which is listed on any stock exchange by raising capital through any public offer but has not completed three years of operation from the date of listing with the stock exchange(s) cannot declare bonus dividend without prior approval of the BSEC.

The company must complete three years after raising funds through rights issue or repeat IPO and must fully utilise the funds raised through IPO or rights issue to declare bonus dividend.

The company which has failed to declare at least 10 per cent cash dividend for a period of two consecutive years from the date of listing with the stock exchange(s) or from the date of declaration of last dividend after listing with any stock exchange cannot declare bonus dividend, it said.

The company which is not in operation for a period of minimum one year excluding any such period for renovation and the company whose shares have been trading under the ‘Z’ category or trading at the over-the-counter platform cannot declare dividend without the BSEC consent.

According to the rules, the companies must declared stock dividend or bonus shares out of the accumulated profit or retained earnings.

The dividend must not be declared out of the capital reserve account or the revaluation reserve account or any unrealised gain or out of profit earned prior to the incorporation of the companies.

The companies must not declare dividend through reducing paid-up capital or through doing anything so that the post-dividend retained earnings become negative or a debit balance, it said.

Despite several initiatives taken by the regulator, the companies continue declaring bonus dividends and no dividends that frustrated the general investors, market operators said.

Besides, some companies provide concocted financial statements to declare irrational dividend for their own purpose, they said.

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Business Law

Rules Regarding Declaration and Payment of Dividend

Rules Regarding Declaration and Payment of Dividend

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Rules Regarding Dividend

The Companies Act provides various rules regarding the declaration and payment of dividend. They are summarized below:

Rules regarding declaration and payment of dividend

1. Right to Recommend the Dividend

The right to recommend a dividend lies with the Board of directors. Only when the Board recommends a dividend, the shareholders can declare a dividend in the general meeting. However, the shareholders cannot insist the directors to recommend. Even if there are sufficient profits, but the directors feel that a distribution of dividend is undesirable in the interests of the financial stability of the company, they can refuse to recommend a dividend.

2. Right to Declare a Dividend

Only the shareholders in the Annual General Meeting can declare the dividend. The Board of Directors determines the rate of dividend to be declared and recommends it to the shareholders. The shareholders, by passing a resolution in the general meeting, can declare the dividend. The shareholders can either accept the same rate of dividend or they can even reduce the rate. However, they cannot enhance the rate of dividend recommended by the directors.

3. Payable out of Profits Only

The company can declare and pay a dividend only where there is a profit. In other words, dividend is payable only out of profits. If there is no profit, there can be no distribution of dividend. The Companies Act provides that a dividend can be paid only:

1. Out of the profits of the Current financial year, or

2. Out of the profits of the previous years, or

3. Out of moneys provided by the Central or State Governments for the purpose of paying a dividend.

Therefore, if a dividend is paid out of capital, it amounts to a breach of trust. It amounts to an unauthorized reduction of capital and is ultra vires. Hence, void. The directors shall become jointly and severally liable.

4. Provision for Depreciation

It is already stated that a dividend can be declared only out of profits. The profits should be arrived only after providing for depreciation for the current year and also for all the arrears of depreciation or loss in any previous year [Sec. 205 of Companies Act]. However, the Central Government can exempt any company from this obligation in the interest of the public.

5. Setting off the Previous Losses

If any loss is incurred in any previous year after 1960, such loss should be set off against the profits of the current year before declaring a dividend [Sec. 205(1)(b)].

6. Payable Only in Cash

The dividend is payable only in cash. However, a company is not prohibited from capitalizing its profits or reserves by the issue of bonus shares or by making partly paid up shares into fully paid up shares.

7. Transfer to Reserves

It is also provided in the Companies Act that every company before declaring any dividend should transfer a certain percentage not exceeding 10% of the profit, to the reserves of the company. The percentage shall be prescribed by the Central Government.

Separate rates are prescribed if the company declares the dividend out of the current year's profits. The Table below shows the percentages of profits to be transferred compulsorily to reserves before declaration of any dividend as per the provision of the Companies (Transfer of Profits to Reserves) Rules, 1975.

Proposed Rate of Dividend	Percentage of Profit to be transferred to reserves
1. Above 10% but below 12.5% of the paid up capital	Not less than 2.5% of the current profits

Proposed Rate of Dividend	Percentage of Profit to be transferred to reserves
2. Above 12.5% but below 15%	Not less than 5% of the current profits
3. Above 15% but below 20%	Not less than 7.5% of the current profits
4. Above 20%	Not less than 10% of the current profits

TABLE: Percentage of Profits transferred to Reserves before declaring Dividend

However, the companies are at liberty to transfer a higher percentage of profit to the reserves. The Companies Amendment Act introduced this provision only in the year 1974 by incorporating Sec. 205 A in it.

8. Time Limit for Payment

When a dividend is declared, it should be paid within 42 days from the date of declaration. The dividend when declared shall become a debt due from the company. If the company does not pay the dividend within the period, every person who is a party to the default is punishable with simple imprisonment up to seven days and also with a fine.

9. Unpaid Dividend Account

If a dividend is declared but not paid within 7 days from the date of expiry of the 42 days, should transfer the amount of unpaid dividend to a separate account with any Scheduled Bank opened under the style "***Unpaid Dividend Account of………Company Ltd***".

10. Transfer to General Revenue Account

Any amount transferred to the Unpaid Dividend Account, which remains unpaid or unclaimed for a period of three years, should be transferred by the company to the General Reserve Account of the Central Government. However, the person to whom the dividend is payable can claim the money from the Central Government. The company which transfers any amount to the General Reserve Account, should furnish a statement furnishing the nature of amount, names of the persons entitled to receive the amount, their addresses, amount due to them, etc.

Company Accounts Cannot Be Retrospectively Adjusted for Convenience

14 December 2021

A company's accounts cannot be retrospectively adjusted to meet the convenience of its directors. The High Court made that point in ruling that the reclassification of a director's loan account just before a company entered liquidation was of no legal effect.

The sole director of the intermittently profitable company blamed its insolvency on third-party bookkeeping failures. At the last minute before the company entered liquidation, the six-figure balance of her director's loan account was reclassified as 'drawings'. That was on the basis that she had taken the money from the company as salary, rather than as loans. The company's liquidators launched proceedings against her with a view to recovering the sum concerned.

The crux of her defence to the claim was that she was paid £6,000 a year in salary, a sum that was not commensurate with a director who often worked 15 hours a day for a company with an approximate annual turnover of £500,000, eight staff and hundreds of clients. Payments from the erstwhile director's loan account should have been recorded as drawings of salary and she was entitled to retain them.

Ruling on the matter, the Court found that the reality of the situation was that it was at all times intended or hoped that the company would ultimately make enough money to declare dividends that would be used to cancel out the sum due on the loan account. Money had been withdrawn from the company as payments on account of future anticipated dividends and was never intended to be salary.

The purported reclassification of the payments as drawings could not alter the basis on which they had been paid or received during the company's prior trading periods. Were such retrospective accounting adjustments possible, the Court had little doubt that most company owners or directors would adopt a similar practice. They would simply approve salary payments to themselves below the Income Tax threshold and then make additional drawings in the hope of earning sufficient dividends by the end of the year to pay off any debt arising to the company.

The sums that had been advanced to the director, and not accounted for as either salary or dividends, came to £286,421. Notwithstanding her attempts, on advice, to re-characterise those payments as drawings, they remained due and owing to the company as a debt. She was ordered to repay the total sum to the company, together with interest.

The contents of this article are intended for general information purposes only and shall not be deemed to be, or constitute legal advice. We cannot accept responsibility for any loss as a result of acts or omissions taken in respect of this article. [To be Continued:

Nonbanking financial institution

A nonbank financial institution (NBFI) is a financial institution that does not have a full banking license and cannot accept deposits from the public. However, NBFIs do facilitate alternative financial services, such as investment (both collective and individual), risk pooling, financial consulting, brokering, money transmission, and check cashing. NBFIs are a source of consumer credit (along with licensed banks). Examples of nonbank financial institutions include insurance firms, venture capitalists, currency exchanges, some microloan organizations, and pawn shops. These non-bank financial institutions provide services that are not necessarily suited to banks, serve as competition to banks, and specialize in sectors or groups.

Risk pooling institutions

Insurance companies underwrite economic risks associated with death, illness, damage to or loss of property, and other risk of loss. They provide a contingent promise of economic protection in the case of loss. There are two main types of insurance companies: life insurance and general insurance. General insurance tends to be short-term, while life insurance is a longer contract, ending at the death of the insured. Both types of insurance, life and property, are available to all sectors of the community. Because of the nature of the insurance industry (companies must access a plethora of information to assess the risk in each individual case), insurance companies enjoy a high level of information efficiency.

Life insurance companies insure against economic loss of the insured's premature death. The insured will pay a fixed sum as an insurance premium every term. Because the probability of death increases with age while premiums remain constant, the insured overpays in the earlier stages and underpays in the later years. The overpayment in the early years of the agreement is the cash value of the insurance policy.

General insurance is further divided into two categories: market and social insurance. Social insurance is against the risk of loss of income due to sudden unemployment, disability, illness, and natural disasters. Because of the unpredictability of these risks, the ease at which the insured can hide pertinent information from the insurer, and the presence of moral hazard, private insurance companies frequently do not provide social insurance, a gap in the insurance industry which government usually fills. Social insurance is more prevalent in industrialized Western societies where family networks and other organic social support groups are not as prevalent.

Market insurance is privatized insurance for damage or loss of property. General insurance companies take a single premium payment. In return, the companies will make a specified payment contingent on the event that it is being insured against. Examples include theft, fire, damage, natural disaster, etc.

Contractual savings institutions

Contractual savings institutions (also called institutional investors) provide the opportunity for individuals to invest in collective investment vehicles in a fiduciary rather than a principle role. Collective investment vehicles invest the pooled resources of the individuals and firms into numerous equity, debt, and derivatives promises. The individual, however, holds equity in the CIV itself rather what the CIV invests in specifically. The two most popular examples of contractual savings institutions are mutual funds and private pension plans.

The two two main types of mutual funds are open-end and closed-end funds. Open-end funds generate new investments by allowing the public buy new shares at any time. Shareholders can liquidate their shares by selling them back to the open-end fund at the net asset value. Closed-end funds issue a fixed number of shares in an IPO. The shareholders capitalize on the value of their assets by selling their shares in a stock exchange.

Mutual funds can be delineated along the nature of their investments. For example, some funds make high-risk, high return investments, while others focus on tax-exempt securities. Still others specialize in speculative trading (i.e. hedge funds), a specific sector, or cross-border investments.

Pension funds are mutual funds that limit the investor’s ability to access their investment until after a certain date. In return, pension funds are granted large tax breaks in order to incentivize the working public to set aside a percentage of their current income for a later date when they are no longer amongst the labor force (retirement income).

Other nonbank financial institutions

Market makers are broker-dealer institutions that quote both a buy and sell price for an asset held in inventory. Such assets include equities, government and corporate debt, derivatives, and foreign currencies. Once an order is received, the market maker immediately sells from its inventory or makes a purchase to offset the loss in inventory. The difference in the buying and selling quotes, or the bid-offer spread, is how the market-maker makes profit. Market makers improve the liquidity of any asset in their inventory.

Specialized sectoral financiers provide a limited range of financial services to a targeted sector. For example, leasing companies provide financing for equipment, while real estate financiers channel capital to prospective homeowners. Leasing companies generally have two unique advantages over other specialized sectoral financiers. They are somewhat insulated against the risk of default because they own the leased equipment as part of their collateral agreement. Additionally, leasing companies enjoy the preferential tax treatment on equipment investment.

Other financial service providers include brokers (both securities and mortgage), management consultants, and financial advisors. They operate on a fee-for-service basis. For the most part, financial service providers improve informational efficiency for the investor. However, in the case of brokers, they do offer a transactions service by which an investor can liquidate existing assets.

Role in financial system

NBFIs supplement banks in providing financial services to individuals and firms. They can provide competition for banks in the provision of these services. While banks may offer a set of financial services as a package deal, NBFIs unbundle these services, tailoring their services to particular groups. Additionally, individual NBFIs may specialize in a particular sector, gaining an informational advantage. By this unbundling, targeting, and specializing, NBFIs promote competition within the financial services industry.

Having a multi-faceted financial system, which includes non-bank financial institutions, can protect economies from financial shocks and recover from those shocks. NBFIs provide multiple alternatives to transform an economy's savings into capital investment, which act as backup facilities should the primary form of intermediation fail.

However, in countries that lack effective regulations, non-bank financial institutions can exacerbate the fragility of the financial system. While not all NBFIs are lightly regulated, the NBFIs that comprise the shadow banking system are. In the runup to the recent global financial crisis, institutions such as hedge funds and structured investment vehicles, were largely overlooked by regulators, who focused NBFI supervision on pension funds and insurance companies. If a large share of the financial system is in NBFIs that operate largely unsupervised by government regulators and anybody else, it can put the stability of the entire system at risk. Weaknesses in NBFI regulation can fuel a credit bubble and asset overpricing, followed by asset price collapse and loan defaults.

Bank/non-bank integration and supervisory integration

The banking, securities, and insurance markets have become increasingly integrated, with linkages across the markets rapidly increasing. In response, one of the most notable developments in financial sector regulation in the past 20 years has been a shift from the traditional sector-by-sector approach to supervision (with separate supervisors for banks, securities markets, and insurance companies) toward a greater cross-sector integration of financial supervision (Čihák and Podpiera 2008). This had an important impact on the practice of supervision and regulation around the globe.

Three broad models are being used around the world: a three-pillar or "sectoral" model (banking, insurance, and securities); a two-pillar or "twin peak" model (prudential and business conduct); and an integrated model (all types of supervision under one roof). One of the arguably most remarkable developments of the past 10 years, confirmed by the World Bank's Bank Regulation and Supervision Survey, has been a trend from the three-pillar model toward either the two-pillar model or the integrated model (with the twin peak model gaining traction in the early 2000s). In a recent study, Melecky and Podpiera (2012) examined the drivers of supervisory structures for prudential and business conduct supervision over the past decade in 98 countries, finding among other things that countries advancing to a higher stage of economic development tend to integrate their supervisory structures, small open economies tend to opt for more integrated supervisory structures, financial deepening makes countries integrate supervision progressively more, and the lobbying power of the concentrated and highly profitable banking sector acts as a negative force against business conduct integration. (The related data on the structure of supervision are available on this website, https://www.worldbank.org/en/publication/gfdr.)

How do these various institutional structures compare in terms of crisis frequency and the limiting of the crisis impact? Cross-country regressions using data for a wide set of developing and developed economies provide some evidence in favor of the twin peak model and against the sectoral model (ˇCihák and Podpiera 2008). Indeed, during the global financial crisis, some of the twin peak jurisdictions (particularly Australia and Canada) have been relatively unaffected, while the United States, a jurisdiction with a fractionalized sectoral approach to supervision, has been at the crisis epicenter. However, the crisis experience is far from black and white, with the Netherlands, one of the examples of the twin peaks model, being involved in the Fortis failure, one of the major European bank failures. It is still early to make a firm overall conclusion, and isolating the effects of supervisory architecture from other effects is notoriously hard.

Report of Inquiry Committee of Peoples Leasing to be placed before the Board of Directors by the MD of the company for consideration, if there is an agenda.

An Inquiry Committee was formed under the direction of the Mr. Kamal ul Alam,Bar-at Law, the Chairman of the Board of Directors of this company formed by the Company Bench of the High Court Division.

Two sittings were made but the meetings were not attended by the important Members so thee as no real inquiry. The matter is mainly of Audit but te member conversant with audit never sat in meeting, so we couldn't go into deep of the problem.

Everyone more or less knows as it was in renowned print media that the company was running well. Then there was a Hostile Takeover by Uzzal Kamar Nandi and his men and Sami Huda became MD/CEO. The company went bankrupt and a liquidation process began. A Provisional Liquidator was appointed who ran the affairs before this Board was appointed by High Court. The present Board and the MD are separately appointed.

The present MD did not submit any Inception Report to the Board called 'White-Paper' in corporate culture and kept everybody in dark. It is well known that the capital was drained away by illegal loans violating Bangladesh Bank Circulars relating to Non Banking Financial Institutions. Nor the MD call for any report from outgoing Chairman and the MD to know their opinions. The Provisional Liquidator also did not submit any report on the status of the company what he got when took charge and what he handed over at departure, as the company went liquidated but went for Court Directed Restructuring to give a Fresh Start.

It can be mentioned here that there is no alternative of loan recovery other than Artharin Adalat Ain.In this case the Boar did not go for Court Case in Original Court. Instead it submitted list of borrowers for taking actions against them. At one stage it was found that MD and his officers were reluctant in sending notices to the borrowers. No general notice was published in newspapers! At one point it was discovered that several Directors had taken huge amount of loan illegally but the MD did not take any action though repeated request by me [MD is not bound by any request of any Member]. Later I pointed out that there are time barred loans and execution cases and it was found that there are huge amount of time-barred loans due to deliberate mismanagement by former and present management. Non participation by vital Board Members in the Inquiry Committee Meetings made the whole task difficult and I am unable to come to conclusion who are actually liable unless the MD comes with a comprehensive report on the Status of Loans barred by law. It was suggested that the coadunation of delay be prayed for the time barred loans and execution cases. It was also found out that all the cases which were pending in Artharin Courts were transferred to High Court but the Liquidator could not show any Court Order and state of affairs of the cases. I think this was done as a tactics to avoid Court-Decree in Original Courts.

Under such circumstances the Inquiry couldn't be proceeded with full strength and no definite conclusion could be arrived upon as to the specific liability of any person. Hasan Shaheed Ferdous, Chairman Inquiry Committee.

Brokerage Company

A brokerage company's main duty is to act as a middleman that connects buyers and sellers to facilitate a transaction. Brokerage companies typically receive compensation by means of commissions or fees that are charged once the transaction has successfully completed. Nowadays these might be paid by the exchange or by the customer, or in some cases both.

Because many discount brokerages have instituted zero-commission trading, they make up for this loss of revenue in other areas, including getting paid by the exchanges for larger quantities of order flow. For example, when a trade order for a stock is executed, an investor pays a transaction fee for the brokerage company's efforts to complete the trade.

The real estate industry also functions using a brokerage company format, as it is customary for real estate brokers to collaborate, with each company representing one party of the transaction to make a sale. In this case, both brokerage companies divide the commission.

A brokerage company may also be called a brokerage firm, or simply a brokerage.

Key Takeaways

- A brokerage company primarily acts as a middleman to connect buyers and sellers to facilitate a transaction.
- Brokerage companies typically receive one of two types of commission: a flat fee or a percentage of the transaction amount.
- Brokerage companies come in several types, offering a range of products and services at a range of costs and fees.

Understanding Brokerage Companies

In a perfect market, where everybody had full information and could act quickly and correctly on that information, there would be no need for brokerage firms. In reality, however, there is less than perfect information, opacity, and asymmetric knowledge. As a result, buyers don't always know who the sellers are and which is offering the best price. Likewise, sellers are in the same position. Brokerage companies exist to help their clients match the other side of a trade, bringing together buyers and sellers at the best price possible for each, and extracting a commission for their services.

Brokers may work for brokerage companies or operate as independent agents.

In the financial markets, several different types of brokerage firms offer a wide range of products and services. Here is a brief description of the three major types, starting with the most expensive option. We will go into greater detail on each below.

- **Full-service brokerage:** A full-service brokerage company provides a professional financial adviser who manages all investment decisions and provides ongoing advice and support. Such brokerages, with their high-touch services, are the most expensive option.

- **Discount brokerages:** Discount brokers were once brick-and-mortar operations, but are now most often online platforms that allow do-it-yourself (or self-directed) investors to make their own trading decisions for lower commissions. Recently, there has been a push toward zero trading commissions for ETFs or even all products on several self-directed online platforms. These brokerage companies may tout relatively low flat fees for trades in television, internet, and radio advertising.
- **Robo-advisors:** Automated investment advisory platforms, or robo-advisors, are a relatively new form of a digital financial advisor that offers investment management services carried out by algorithms with minimal human intervention at a very low cost. Several robo-advisors offer zero commissions or fees, and you can start with as little as $5 in many cases.

Investors have a range of options when choosing a brokerage company. The type of services a person requires depends on their level of market knowledge, sophistication, risk tolerance, and comfort in trusting others to manage their money.

Brokerage commissions erode returns over time, so investors should select a company that provides the most economical fees for services provided. Before opening an investment account, a customer should compare fees, products, benefits, customer service, reputation, and the quality of services provided.

Types of Brokerages

The amount you will pay depends on the level of services you receive, how personalized they are, and whether they involve human beings rather than computer algorithms.

Full-Service Brokerage

Full-service brokerages, also known as traditional brokerages, offer a range of products and services including money management, estate planning, tax advice, and financial consultation.

Some traditional, full-service brokerage companies also offer discount brokerage services and robo-advisor platforms. The difference is the breadth of services and cost.

These companies also offer up-to-date stock quotes, research on economic conditions, and market analysis. Highly trained and credentialed professional brokers and financial advisers work at these firms and may form personal relationships with their clients. Some traditional, full-service brokerage companies also offer discount brokerage services or robo-advisor platforms.

Traditional brokerages charge a fee, commission, or both. For regular stock orders, full-service brokers may charge up to $10 to $20 per trade, but many advisors are switching to a wrap-fee business model, in which all trades and advice come under an all-inclusive annual fee—typically 1% to 2% of assets under management (AUM). Many full-service brokers seek out affluent clients and establish minimum account balances required to obtain their services, often starting at six figures or more.

Discount Brokerage

A discount brokerage charges less than a traditional brokerage but may provide fewer comprehensive services and products, and lack the personal relationship found with a full-service advisor; the depth and quality of discount brokers' advice often depend on the size of an investor's account.

Several full-service companies do offer a lower-cost discount brokerage arm, as well. These types of companies are able to charge a lower commission by having their clients conduct their own research and trades via computerized trading systems, either web-based or through a mobile app.

The first discount brokerage is often attributed to Charles Schwab in the 1970s and 1980s. Since the advent of online trading in the late 1990s, commissions for discount brokers have become drastically lower than full-service brokers due to fierce competition. Today, most discount brokerage customers go online or use Smartphone apps. in 2019, Charles Schwab joined Robinhood in their initiative to offer zero commissions on all equities trades. This sparked a similar reaction from the majority of online brokerage firms to adjust their pricing similarly.

Robo-Advisors

Starting in the 2010s, robo-advisors are a class of digital-only online investment platform that uses algorithms to implement trading strategies on behalf of clients in an automatic manner. Most robo-advisors subscribe to long-term passive index strategies that follow the rules of modern portfolio theory (MPT), although several robo-advisors now allow clients to modify their investment strategy somewhat if they want more active management.

The allure of robo-advisors is not only the automation but also the very low fees and low account balances needed to get started. In many cases, robo-advisors actually charge no annual fee, zero commissions, and you can start with just a few dollars.

Some robo-advisors have now started employing human advisors whom clients can consult, but these advisors often are unable to actually change the recommended portfolio allocation generated by their algorithms. Furthermore, access to an advisor will come with a higher fee, typically 0.25% to 0.50% of AUM per year—which is still far less than that of a traditional broker.

Independent versus Captive Brokerage

It's also important to know whether your broker is affiliated only with certain companies or can sell you the full range of choices. You should also find out whether they hold to the fiduciary standard or the suitability standard.

Independent Brokerage

Independent brokerages are not affiliated with any mutual fund company, but function similarly to a full-service brokerage. Typically, these brokers can recommend and sell clients products that are more likely to be in their best interests because they are not tied to one company. Registered investment advisors (RIAs) are the most common type of independent broker found today.

They are required to hold to the fiduciary standard, meaning that they must recommend the investments most in the client's best interest—and not their own (meaning, a fund with an especially good commission for the broker who sells it). It's best to choose an advisor who upholds the fiduciary standard and not the lesser suitability standard.

Captive Brokerage

Captive brokerages are affiliated with a specific mutual fund or insurance company and have contracts with specific providers to sell only their products. These brokers are employed to recommend and sell the range of products that the mutual or insurance company owns. Such products may not be in the client's very best interest compared with other options.

Related Terms

Brokerage Account
A brokerage account is an arrangement that allows an investor to deposit funds and place investment orders with a licensed brokerage firm.
more
Independent Agent
An independent agent can sell the insurance or financial products of several carriers and is not captive to just their direct employer's products.
more
Registered Representative (RR)
A registered representative (RR) is a financial professional who works with clients who are trading investments such as stocks and bonds.
more
What Is a Deep Discount Broker?
A deep discount broker handles buys and sales of securities for customers on exchanges at even lower commission rates than regular discount brokers.
more
What Is a Fiduciary?
A fiduciary is a person or organization that acts on behalf of a person or persons and is legally bound to act solely in their best interests.
more
Do-It-Yourself (DIY) Investing
Do-it-yourself (DIY) investing is an investment strategy where individual investors choose to build and manage their own investment portfolios.
more
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Blue sky law
The emptiness of blue sky was a metaphor for the fraudulent basis of some securities that laws named after it sought to prevent by requiring disclosures to investors.

A **blue sky law** is a state law in the United States that regulates the offering and sale of securities ostensibly to protect the public from fraud. Though the specific provisions of these laws vary among states, they all require the registration of all securities offerings and sales, as well as of stockbrokers and brokerage firms. Each state's blue sky law is administered by its appropriate regulatory agency, and most also provide private causes of action for private investors who have been injured by securities fraud.

The first blue sky law was enacted in Kansas in 1911 at the urging of its banking commissioner, Joseph Norman Dolley, and served as a model for similar statutes in other states. Between 1911 and 1933, 47 states adopted blue-sky statutes (Nevada was the lone holdout[1]). Today, the blue sky laws of 40 of the 50 states are patterned after the Uniform Securities Act of 1956. Historically, the federal securities laws and the state blue sky laws complemented and often duplicated one another. Much of the duplication, especially with regards to registration of securities and the regulation of brokers and advisors, was largely preempted by the Securities and Exchange Commission with the National Securities Markets Improvement Act of 1996 (NSMIA). This act, however, left some regulation of investment advisors and much of the fraud litigation under state jurisdiction. In 1998, state law securities fraud claims were expressly preempted by the Securities Litigation Uniform Standards Act from being raised in lawsuits that were effectively class actions by investors, even if not filed as class actions.

Origin of term in securities context

Its earliest cited use by the US Supreme Court was in an opinion by Justice Joseph McKenna in *Hall v. Geiger-Jones Co.*, 242 U.S. 539 (1917), a case that addressed the constitutionality of state securities laws. Oddly, McKenna is frequently and erroneously given credit for inventing the term even though J. N. Dolley used the term when he was plumping for passage of the Kansas statute in 1910, and McKenna's own opinion in *Hall* itself attributes the term to an unnamed earlier source:

The name that is given to the law indicates the evil at which it is aimed, that is, to use the language of a cited case, "speculative schemes which have no more basis than so many feet of 'blue sky'"; or, as stated by counsel in another case, "to stop the sale of stock in fly-by-night concerns, visionary oil wells, distant gold mines and other like fraudulent exploitations." Even if the descriptions be regarded as rhetorical, the existence of evil is indicated, and a belief of its detriment; and we shall not pause to do more than state that the prevention of deception is within the competency of government and that the appreciation of the consequences of it is not open for our review.

Kansas Banking Commissioner Dolley, railing against "blue sky merchants" while he pushed for passage of the Kansas statute in 1910, observed that certain fraudulent investments were backed by nothing but the blue skies of Kansas. The *Oxford English Dictionary* has a cited use dating to 1906. Also, *The New York Times* (and other national newspapers) frequently reported on the blue sky laws as various states began to enact them between 1911 and 1916. The newspapers expressly used the term *blue sky* to describe such law pithiness of blue sky was a metaphor for the fraudulent basis of some securities that laws named after it sought to prevent by requiring disclosures to investors.

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What happens when a stock trading is halted?

When trading is halted, **the particular security will no longer be able to trade in the stock exchanges**. It has been listed till the time the halt is lifted back. It means brokers and retail investors. ... read more will not be able to trade in that particular stock, i.e., buy or sell the securities for a specific period.

Why does trading halt on a stock?
Can a trading halt be good?
Is it legal to halt trading on a stock?
Securities exchanges, such as the New York Stock Exchange (NYSE) as well as the Nasdaq Stock Market, **have the authority to halt and delay trading in a security**. ... The most common regulatory halt and delay happen when a company has pending news that may affect the security's price (a "news pending" halt or delay)

Can Share Price be Zero?

It can't drop to zero. If there is a transaction, the price is above zero. It can drop to nothing only when it is not traded on any market. When that happens, for the most part the shares simply become part of history, a future entry on your tax return, or if in certificate form, a historical artifact that can be sold on eBay if it has a neat picture.

No. If the stock vale drops to zero it means the equity value of the company is zero.

Equity = Assets - Liabilities

So if the equity is zero, either liabilities are greater than assets therefore company is bankrupt or assets have shrunk and cannot maintain liabilities The company will still have staff, plant and machinery, premises etc but its financial condition means that its unlikely to pay for staff, will have to sell assets to pay liabilities and so on. It will function for a short while but will quickly grind to a halt as the company's cash flow, its life blood, dries up.

Capital Injection Non Banking Financial Intuitions in Bangladesh:

Hasan Shaheed Ferdous, Chairman Peoples' Leasing, People's Investment [Bangladesh]

Bangladesh is in take-off period in economic emancipation and role of banks and non banking financial institutions like lease financing to provide capital- power is crucial.

The banks and financial institutions are the main sources for flow of capital but their underperforming in primary role to bring about significant change of the country would require 'plugging the holes' to reduce the capital drain and minimum ability to infuse New Normal Financial Reality to increase capacities of stakeholders. The need for increase of youth capital users is significant to increase investment and lowering unemployment or under employment.

3 sources of capital
Most businesses distinguish between **working capital, equity capital, and debt capital**, although they overlap. Working capital is the money needed to meet the day-to-day operation of the business and pay its obligations in a timely manner.
A capital injection is an investment of capital into a project, company, or investment, typically in the form of cash, equity, or debt. Oftentimes, the word *injection* implies that the company or organization receiving funding may be in financial distress. However, the term may also refer more broadly to all types of one-off capital investments, including those made in a startup or a growing company. What are capital injections?

A capital injection is **an investment of capital into a project, company, or investment, typically in the form of cash, equity, or debt**. Oftentimes, the word injection implies that the company or organization receiving funding may be in financial distress.

Main Points:

A capital injection is a lump-sum investment, typically in the form of cash, but may also consist of equity or debt.

- Capital injections can be obtained for a variety of purposes including startup funding, growth, initial public offerings, distress, or bailout funding.
- When the government offers a capital injection bailout it provides capital to an ailing industry or prominent companies with tax dollars to pay for the investment but the funding is typically structured as either a loan or equity investment which provides a return over the long-term.

Capital Injection Explained

Capital injections in the private sector are usually in exchange for an equity stake in the company from which the investor is investing. Capital injections can occur throughout the various life cycles of a business. For example, financing in the form of a capital injection may open a seed round from friends, family, and hand-selected angel investors.

In return, the investors receive a portion of the company's ownership. If a private company in a growth phase wants to fund its momentum, that company can open a series A investment round, or it can assume debt, both of which are capital injections. If a mature company decides to go public, the money earned through the issuance of shares is also a capital injection.

There are other ways that a company or organization can receive a capital injection. Sometimes, governments will inject capital into struggling sectors to stabilize them for the public good. The government may negotiate an equity stake in recipient companies or institutions, or it may treat the capital injection as a debt obligation.

Examples of Capital Injections

For example, following the financial crisis of 2008, the U.S. government, as well as other governments around the world, injected hundreds of billions of dollars into their financial sectors. These capital injections were an attempt to halt the conflagration that was threatening to engulf the global economy.

We examine the effect of government capital injection on a distressed bank and its borrowing firm.

- Government capital injection produces greater safety for the bank, but greater default risk for the borrowing firm.
- The bank significantly benefits from government capital injection when its borrowing firm has inferior performance.
-

Government capital injection is significantly harmful to the borrowing firm with inferior performance.

- Ignore bank-dependent borrower health state underestimated the effect of government capital injection on bank safety.

We examine the impacts on bank interest margin, bank default risk, and bank-dependent borrower default risk from changes in the bailout program of government capital injections. This paper focuses on the capped credit risk, the risk of default related to borrower health states. We show that government capital injection helps to reduce default risk for the bank, but indirectly increases the default risk for the borrowing firm. Government capital injection is more likely to produce greater safety for the bank when the borrowing firm is in a distressed situation (e.g., a high-risk and low-return one). The capital effect on bank safety is underestimated when the capped credit risk is ignored. We conclude that a government capital injection program stabilizes the bank, but deteriorates the borrowing firm.

Capital –Injection: Need for Law:

By the end of this year due strain on the banks and other financial institution like Leasing companies will require a strong and unshakably competitive financial system should be rebuilt, including regional finance. To achieve this objective, financial institutions should basically complete the disposal of bad debts and subsequently ensure sufficient capital. Basically taking the same approach as in the cases for the banks, the Financial Reconstruction Commission (FRC) is required which will have to make a Report which will make use of the capital injection scheme under the Financial Function Early Strengthening Law as early as possible

Basic Viewpoints

- Capital injections must be commensurate with local conditions. Sufficient consideration will be given to the provision of funds to local corporations in medium and small size.

- Capital injections must promote smooth flows of credit, thereby contributing to revitalization of the regional economy, i.e., improvements in business activity and employment.

- Capital injections must contribute to greater efficiency for the financial system by triggering new realignments of regional financial institutions.

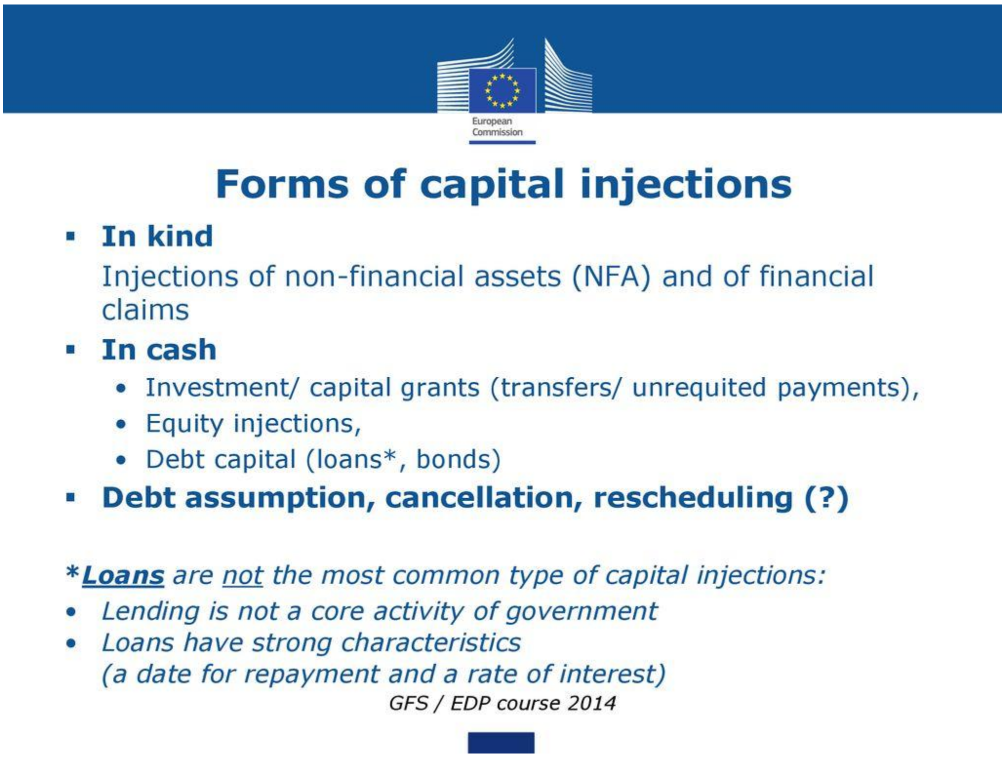
- Financial institutions which meet the following will be given preferential treatment regarding the size of and conditions on the capital injections:

- those playing a major role in the provision of credit in the region;

- those necessary for assuring appropriate competition in the local financial market;

- Those adapting to financial realignment in the region.

- The specific contents of the plan for restoring sound management will correspond with the conditions of country’s financial institutions. Applications will be examined in a timely manner whenever received.



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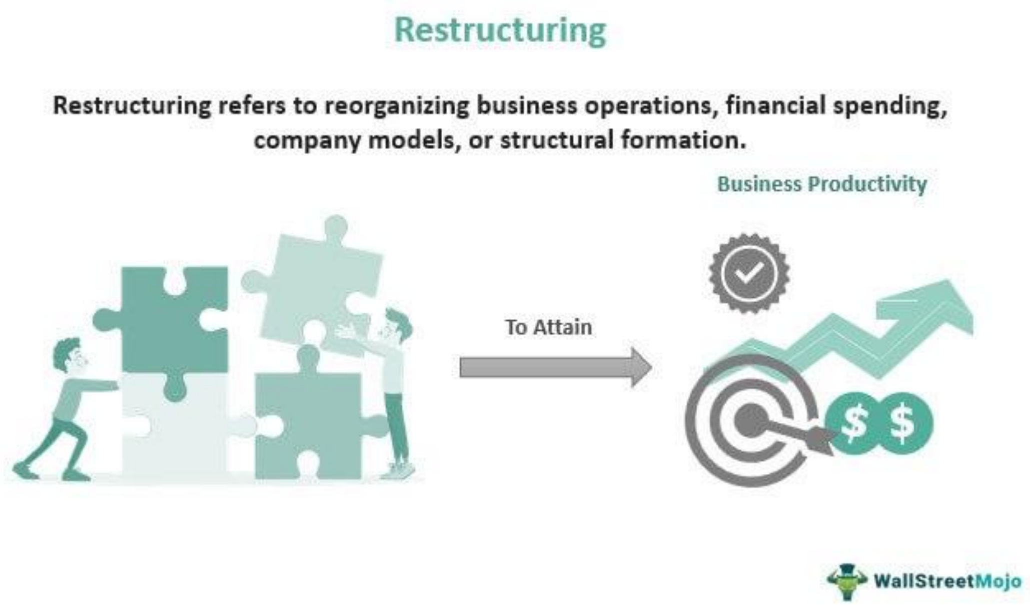
Restructuring in the case of heavy loss-generating business units

Bottom of Form

Restructuring

Restructuring is the corporate activity to reform the firm’s operational strategy for successful goal accomplishment. It helps soar the efficacy in commercial activities, facilitating the economic status of the corporation. Moreover, there are two critical types of **corporate restructuring** in a company, namely, organizational and financial.



Please note that it can incorporate reconfigurations or other ground-level makeovers like dividing, attaching, disintegrating, or shifting business units not impacting the surface structure. Also, its benefits comprise increased communication, improvement in organizational finances, matching with competitors, and enhanced employee productivity.

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Key Takeaways

- Restructuring is a method to execute the organizational redesigning program for its financial condition advancement. Additionally, it assists in boosting the operational efficacy resulting in successful outputs.
- This entails surface-level adjustments like splitting, adding, dissolving, or transferring non-productive business sectors or deeper financial refurbishments.
- It is categorized into two major types, namely, organizational and **financial restructuring**. While the former aims at functional alterations, the latter is focused on economic changes.
- Its benefits are enhanced interaction, refined company funds, equalizing the competition with rivals, and better employee productiveness.

Restructuring Explained

Restructuring can happen following insolvency, continue changing markets, or upon approving further structural improvements such as merging with another enterprise. Additionally, the business possibly comprises arrears management in the reorganization scheme accompanying functional and structural changes.

Determined by the severity of the institution's situation, it may transpire formally (lawful **corporate restructuring** actions) or informally (behind the scenes). Please note that undertaking this action can be complicated and hard. Therefore, the Board of Directors (BOD) typically takes this decision which may include hiring underwriters.

To clarify, the establishment must contemplate reorganizing itself if it,

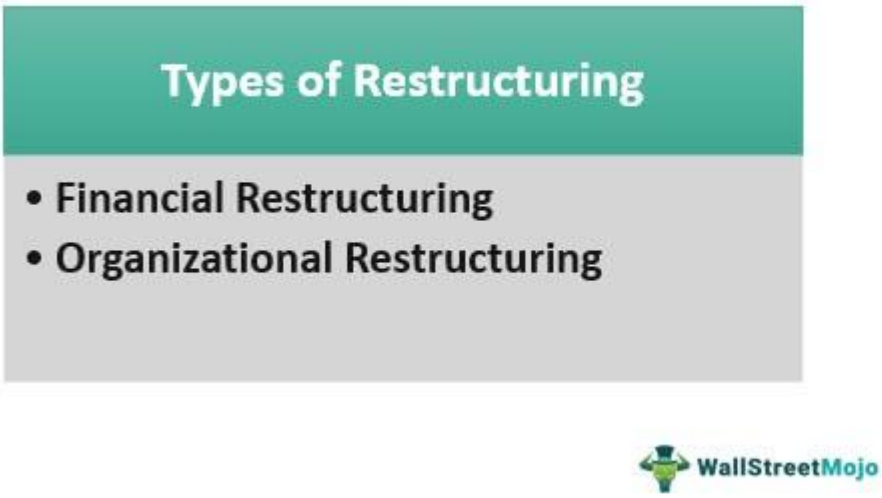
1. Is documenting a logically substandard business outcome
2. Couldn't reimburse short-term or long-term debt repayment
3. Fails to make a profit that fulfills the stockholders' expectations
4. Has experienced an incomparable severe case like a slump in major clients leading to financial hardship
5. Is thriving in some divisions and is lagging in others

Most importantly, company reorganization is advantageous only if problem-solving can assist it in dealing productively in the foreseeable future. It can also encompass refinancing bank services, staffing cutbacks or readjustments, rationalizing goods or utilities, or initiating new venture capital.

The firm restructures itself (through mergers and acquisitions, divestment, or cost modifications) to attain synergy advantages via a beneficial strategy.

Types Of Restructuring

In other words, the following are two pivotal kinds of **company restructuring**:



1. Financial Restructuring

This can occur owing to a steep decline in the total sales caused by drastic financial situations. Moreover, the business entity can modify its equity holdings and pattern, cross-holding pattern, and debt-servicing arrangement. It assists in maintaining the market and profitability of the business.

2. Organizational Restructuring

It implicates modifications in the firm's organizational structure like its hierarchy level reduction, downsizing the workers, redeveloping job profiles, and altering the reporting relations. Hence, **organizational restructuring** helps cut back the expenses and settle the outstanding dues for continuance with commercial activities.

Examples

Here are a few examples of the same.

Example#1

1. Say the BOD discovers the acquisition of irrelevant businesses in ABC Co. aimed at increasing the salary of its Chief Executive Officer (CEO). Therefore, it might choose capital restructuring to sell off the unrelated acquisition, diminishing the CEO's salary while making the firm cash-rich.
2. Suppose a corporation, XYZ Co., may restructure itself after successfully launching the latest service or product in case of insufficient debt payment and payroll coverage revenues. Therefore, it may sell the assets, issue equity to reduce debt, reorganize the fiscal arrangements, or file for foreclosure as the company sustains operations.

Example#2

Atos SE is planning the spinoff of the Big Data and cybersecurity business into an individual entity leading to the resignation of its CEO Rodolphe Belmer. The resignation comes after he disagrees with the firm about the restructuring proposal.

Moreover, this plan will list the current data unit before 2023's second half with Evidian as the afflicted legacy IT solutions will go ahead as Atos. Both firms will possess different management.

As per the estimates by Atos, 1.6 billion euros of total finances is required for 2022-2023, with gains anticipated from selling 700 million euros of non-essential assets. As a result, Atos stakeholders will completely possess the restructured firm with 70% ownership in Evidian. To clarify, Atos will hold the remaining 30% share.

Benefits Of Restructuring

Above all, here are the benefits of **company restructuring**:

1. Boosts Communication

While reorganizing business activities or organizational elements, corporate leaders may probably boost interaction between corporate branch locations or divisions. Also, it affects the working process of departments toward organizational goals and their collaboration with each other.

2. Sustains Or Refines Company Funds

This helps enterprises maximize revenue streams, debt reduction, or sustenance of operations throughout financial downturns.

3. Equalizes Firms with Rivals

It permits the organizations to facilitate their functional structure and funds or adjust to industry changes. Therefore, corporations can match market rivals and maintain a robust business image.

4. Enhances Employee Productiveness

The reorganization of divisions or a complete firm lets the organizational leaders redesign commercial affairs and roles in a manner that benefits employees. To clarify, this comprises the workers' movement into distinctive teams or parts and executing systems to boost functionalities.

Frequently Asked Questions (FAQs)

What Is Corporate Restructuring?

Corporate restructuring is a business activity involving relevant modification of the firm's debt, functions, or arrangement. Furthermore, it aids in restricting fiscal harms and business improvements. Please note that it has two types, financial and organizational restructuring.

What Is Financial Restructuring?

Financial restructuring is a corporate reconstitution technique conveying issues and disorganizations due to the firm's unsuitable economic structure. Moreover, it can entail matters like transforming preference shares to ordinary shares or current dues to equity, and debt comprises debt subordination.

To clarify, this may also involve the transferral or sale of current equity or liabilities to more encouraging new owners.

What Are the Problems with Restructuring?

Here are the problems with restructuring,

1. Probable negative public image
2. 2. Employee anxiety
3. Unpredictable investor reactions
4. Losing assets
5. Reduction in employee morale
6. Re-training efforts and expenses
7. Possibly adverse effect on Return on Investment (ROI)

CEO Worldwide offers companies the experience of seasoned top managers who have a successful track record in the carrying out of several restructuring programs for heavy loss-generating business entities. And in this field, like in a number of others, experience is a (probably even the) major success factor.

No one wants to talk about it, but there are numerous instances where a company or a group come to realise one day that a given business unit, a subsidiary, or worse, a group of subsidiaries, has become a source of recurrent, permanent losses, and does not respond to the efforts made to turn its situation around, or, at least, bring it under effective control.

This kind of situation appears very often when the money-loosing entity is located in a foreign country, where language problems as well as different ways of doing business add to the usual difficulties of finding the appropriate solutions and restructuring measures to cope with an ailing business entity.

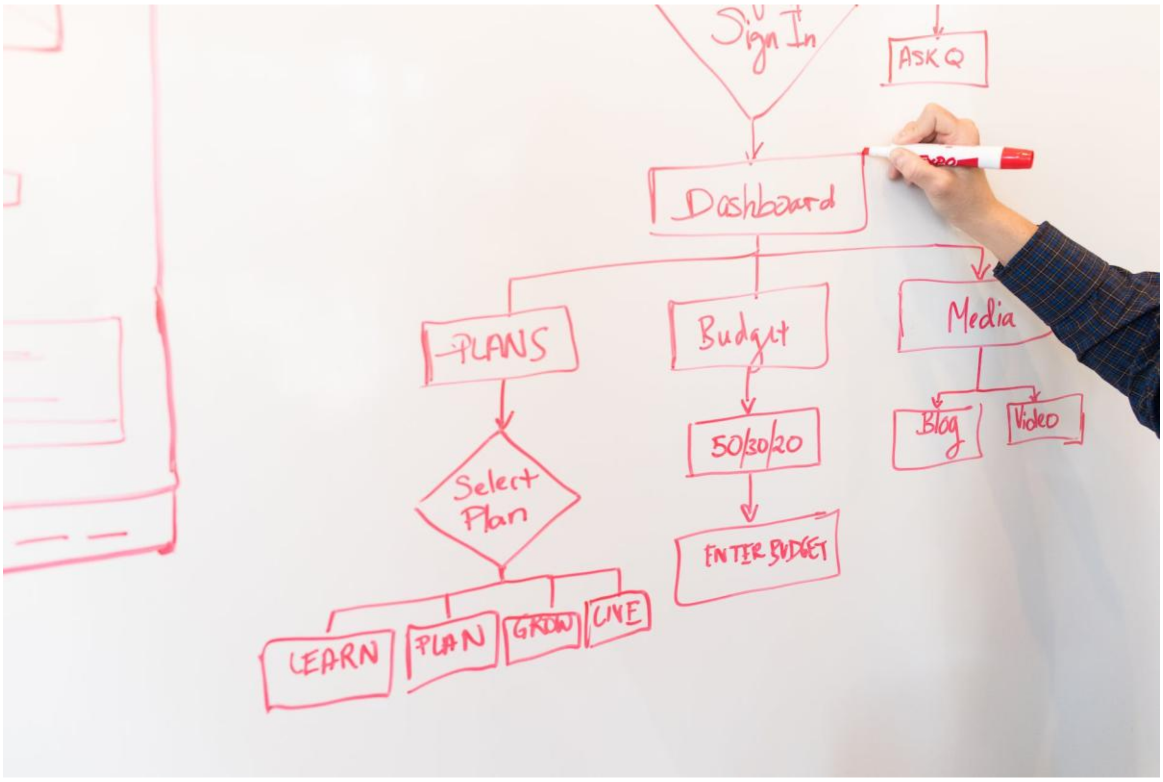
A) Identifying the problem

When a business unit has lost money for some time and does not seem to react positively to whatever corrective actions have been decided upon and implemented, the usual reaction is to question the measures and/or the management team responsible for their implementation. However, when this line of thought does not lead to some fairly obvious explanation, it is necessary to look closer into the matter.

The requisite in-depth study of what is actually happening is very often postponed if the losses generated by the business unit remain limited in comparison to the consolidated result of the shareholding entity, and/or if, in addition, the reasons for the poor performance of the business unit seem obscure and difficult to identify. The problem then remains unsolved, losses keep accumulating, and conventional wisdom, within both the ailing business unit and its shareholding entity, soon begins to vehicle the idea that there is no good solution whatsoever.

B) Where to start

The first decisive step must be the decision by the top management of the shareholding structure to put an end, one way or the other, to the never-ending losses of the business unit, and to follow up on that decision. The top manager in charge must clearly be backed by the CEO. He should be chosen amongst the top collaborators who have had no responsibility in connection with the ailing unit, his final objective(s) should be clearly expressed and the corresponding deadline to achieve his objective(s) clearly defined.



C) The key factors for a successful solution through restructuring

Considering the fact that the situation at hand has remained unattended or at least unresolved despite various attempts to deal with it, or at least to mitigate its consequences, it must be obvious to all that the problem is indeed serious and that the main reasons for its occurrence have not been properly identified and fully understood.

Consequently, the top manager in charge will first select and appoint a chief operating officer (COO) who will work full-time to solve the problem(s) of the ailing business unit, or to dispose of the unit through sale(s) or closure(s). Under the direct supervision of the top manager in charge, the COO should be given all powers to instruct and direct the ailing entity as he deems appropriate to carry out his assignment within the imposed time frame, in the best interest of the shareholding structure.

The COO will be given a limited but adequate amount of time to study the situation in depth and propose a strategy as well as an action plan to solve the problem(s) in due time. The top manager in charge will review the strategy and the action plan, make whatever changes and modifications deemed necessary (in liaison with the COO), and obtain the green light and full support of the CEO (or the Executive Committee as the case may be). He will then formally send to the COO the precise objectives, constraints, and levels of financial and human resources corresponding to the implementation phase of his assignment.

C1) Sponsorship

To ensure success of the action plan to be carried out by the COO, it must be clear to all, within the ailing unit but also within the shareholding entity, that the restructuring process is fully supported (and monitored) by the top management at the highest level. It is essential to have all collaborators involved be aware of the fact that the COO's assignment has high priority for top management, that the necessary resources will be made available in due time, and that the key collaborators involved in the process will be accountable and rewarded for performance.

C2) Decision-making at the shareholder's level

A key factor to the success or failure of the process is the ability of the manager in charge to swiftly make the decisions which must be made at the shareholder's level in response to the questions and requests coming from the COO. All too often, because of insufficient availability, delayed access to the CEO, other priorities and so on, the top manager in charge is in no position to give the answers which the COO requests and which he needs to move on. As a result, the whole process is at best slowed down, its credibility damaged and its outcome jeopardised. No matter how competent and diligent the COO is, he can only succeed if the top management is prepared and organised to react and decide promptly.

C3) Communication

As the restructuring/cleaning up action plan often implies carrying out social plans, reductions of the labour force, closure of some plants, disposal of assets, etc…, it generates strong emotional reactions at all levels within the company and around it. It is therefore necessary to communicate and explain both internally and externally what is happening and what is coming and why, in order to give to all stakeholders a fair, even though often simplified, understanding of the process and to reduce inasmuch as possible all sources of anxiety. Communication is therefore of the utmost importance and should be handled very carefully with a strong involvement of the COO and the top manager in charge.

D) To conclude: nothing replaces experience

If there are any rules to successfully carry out a restructuring process of an ailing business unit, experience is the crucial factor. There are so many variables involved that no business administration operating manual can give all the answers; besides, the human factor plays a major role (either in a positive or in a negative way or both at the same time) in the response of the business entity to the restructuring process itself. This is why experience is so very important.

Needs Assessment, Analysis,discovery,etc:

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SWOT Analysis: How To With Table and Example

What Is SWOT Analysis?

SWOT (strengths, weaknesses, opportunities, and threats) analysis is a framework used to evaluate a company's competitive position and to develop strategic planning. SWOT analysis assesses internal and external factors, as well as current and future potential.

A SWOT analysis is designed to facilitate a realistic, fact-based, data-driven look at the strengths and weaknesses of an organization, initiatives, or within its industry. The organization needs to keep the analysis accurate by avoiding pre-conceived beliefs or gray areas and instead focusing on real-life contexts. Companies should use it as a guide and not necessarily as a prescription.

Key Takeaways

- SWOT analysis is a strategic planning technique that provides assessment tools.
- Identifying core strengths, weaknesses, opportunities, and threats leads to fact-based analysis, fresh perspectives, and new ideas.
- A SWOT analysis pulls information internal sources (strengths of weaknesses of the specific company) as well as external forces that may have uncontrollable impacts to decisions (opportunities and threats).
- SWOT analysis works best when diverse groups or voices within an organization are free to provide realistic data points rather than prescribed messaging.
- Findings of a SWOT analysis are often synthesized to support a single objective or decision that a company is facing.

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SWOT Analysis

Understanding SWOT Analysis

SWOT analysis is a technique for assessing the performance, competition, risk, and potential of a business, as well as part of a business such as a product line or division, an industry, or other entity.

Using internal and external data, the technique can guide businesses toward strategies more likely to be successful, and away from those in which they have been, or are likely to be, less successful. Independent SWOT analysts, investors, or competitors can also guide them on whether a company, product line, or industry might be strong or weak and why.

SWOT analysis was first used to analyze businesses. Now, it's often used by governments, nonprofits, and individuals, including investors and entrepreneurs. There is seemingly limitless applications to the SWOT analysis.

Components of SWOT Analysis

Every SWOT analysis will include the following four categories. Though the elements and discoveries within these categories will vary from company to company, a SWOT analysis is not complete without each of these elements:

Strengths

Strengths describe what an organization excels at and what separates it from the competition: a strong brand, loyal customer base, a strong balance sheet, unique technology, and so on. For example, a hedge fund may have developed a proprietary trading strategy that returns market-beating results. It must then decide how to use those results to attract new investors.

Weaknesses

Weaknesses stop an organization from performing at its optimum level. They are areas where the business needs to improve to remain competitive: a weak brand, higher-than-average turnover, high levels of debt, an inadequate supply chain, or lack of capital.

Opportunities

Opportunities refer to favorable external factors that could give an organization a competitive advantage. For example, if a country cuts tariffs, a car manufacturer can export its cars into a new market, increasing sales and market share.

Threats

Threats refer to factors that have the potential to harm an organization. For example, a drought is a threat to a wheat-producing company, as it may destroy or reduce the crop yield. Other common threats include things like rising costs for materials, increasing competition, tight labor supply. and so on.

SWOT Table

Analysts present a SWOT analysis as a square segmented into four quadrants, each dedicated to an element of SWOT. This visual arrangement provides a quick overview of the company's position. Although all the points under a particular heading may not be of equal importance, they all should represent key insights into the balance of opportunities and threats, advantages and disadvantages, and so forth.

The SWOT table is often laid out with the internal factors on the top row and the external factors on the bottom row. In addition, the items on the left side of the table are more positive/favorable aspects, while the items on the right are more concerning/negative elements.

How to Do a SWOT Analysis

A SWOT analysis can be broken into several steps with actionable items before and after analyzing the four components. In general, a SWOT analysis will involve the following steps.

Step 1: Determine Your Objective

A SWOT analysis can be broad, though more value will likely be generated if the analysis is pointed directly at an objective. For example, the objective of a SWOT analysis may focused only on whether or not to perform a new product rollout. With an objective in mind, a company will have guidance on what they hope to achieve at the end of the process. In this example, the SWOT analysis should help determine whether or not the product should be introduced.

Step 2: Gather Resources

Every SWOT analysis will vary, and a company may need different data sets to support pulling together different SWOT analysis tables. A company should begin by understanding what information it has access to, what data limitations it faces, and how reliable its external data sources are.

In addition to data, a company should understand the right combination of personnel to have involved in the analysis. Some staff may be more connected with external forces, while various staff within the manufacturing or sales departments may have a better grasp of what is going on internally. Having a broad set of perspectives is also more likely to yield diverse, value-adding contributions.

Step 3: Compile Ideas

For each of the four components of the SWOT analysis, the group of people assigned to performing the analysis should begin listing ideas within each category. Examples of questions to ask or consider for each group are in the table below.

Internal Factors

What occurs within the company serves as a great source of information for the strengths and weaknesses categories of the SWOT analysis. Examples of internal factors include financial and human resources, tangible and intangible (brand name) assets, and operational efficiencies.

Potential questions to list internal factors are:

- (Strength) What are we doing well?
- (Strength) What is our strongest asset?
- (Weakness) What are our detractors?
- (Weakness) What are our lowest-performing product lines?

External Factors

What happens outside of the company is equally as important to the success of a company as internal factors. External influences, such as monetary policies, market changes, and access to suppliers, are categories to pull from to create a list of opportunities and weaknesses.1

Potential questions to list external factors are:

- (Opportunity) What trends are evident in the marketplace?
- (Opportunity) What demographics are we not targeting?
- (Threat) How many competitors exist, and what is their market share?
- (Threat) Are there new regulations that potentially could harm our operations or products?

Strengths	**Weaknesses**
1. What is our competitive advantage?	1. Where can we improve?
2. What resources do we have?	2. What products are underperforming?
3. What products are performing well?	3. Where are we lacking resources?
Opportunities	**Threats**
1. What new technology can we use?	1. What regulations are changing?
2. Can we expand our operations?	2. What are competitors doing?
3. What new segments can we test?	3. How are consumer trends changing?

Companies may consider performing this step as a "white-boarding" or "sticky note" session. The idea is there is no right or wrong answer; all participants should be encouraged to share whatever thoughts they have. These ideas can later be discarded; in the meantime, the goal should be to come up with as many items as possible to invoke creativity and inspiration in others.

Step 4: Refine Findings

With the list of ideas within each category, it is now time to clean-up the ideas. By refining the thoughts that everyone had, a company can focus on only the best ideas or largest risks to the company. This stage may require substantial debate among analysis participants, including bringing in upper management to help rank priorities.

Step 5: Develop the Strategy

Armed with the ranked list of strengths, weaknesses, opportunities, and threats, it is time to convert the SWOT analysis into a strategic plan. Members of the analysis team take the bulleted list of items within each category and create a synthesized plan that provides guidance on the original objective.

For example, the company debating whether to release a new product may have identified that it is the market leader for its existing product and there is the opportunity to expand to new markets. However, increased material costs, strained distribution lines, the need for additional staff, and unpredictable product demand may outweigh the strengths and opportunities. The analysis team develops the strategy to revisit the decision in six months in hopes of costs declining and market demand becoming more transparent.

Use a SWOT analysis to identify challenges affecting your business and opportunities that can enhance it. However, note that it is one of many techniques, not a prescription.

Benefits of SWOT Analysis

A SWOT analysis won't solve every major question a company has. However, there's a number of benefits to a SWOT analysis that make strategic decision-making easier.

- **A SWOT analysis makes complex problems more manageable.** There may be an overwhelming amount of data to analyze and relevant points to consider when making a complex decision. In general, a SWOT analysis that has been prepared by paring down all ideas and ranking bullets by importance will aggregate a large, potentially overwhelming problem into a more digestible report.
- **A SWOT analysis requires external consider.** Too often, a company may be tempted to only consider internal factors when making decisions. However, there are often items out of the company's control that may influence the outcome of a business decision. A SWOT analysis covers both the internal factors a company can manage and the external factors that may be more difficult to control.
- **A SWOT analysis can be applied to almost every business question.** The analysis can relate to an organization, team, or individual. It can also analyze a full product line, changes to brand, geographical expansion, or an acquisition. The SWOT analysis is a versatile tool that has many applications.
- **A SWOT analysis leverages different data sources.** A company will likely use internal information for strengths and weaknesses. The company will also need to gather external information relating to broad markets, competitors, or macroeconomic forces for opportunities and threats. Instead of relying on a single, potentially biased source, a good SWOT analysis compiles various angles.
- **A SWOT analysis may not be overly costly to prepare.** Some SWOT reports do not need to be overly technical; therefore, many different staff members can contribute to its preparation without training or external consulting.

SWOT Analysis Example

In 2015, a Value Line SWOT analysis of The Coca-Cola Company noted strengths such as its globally famous brand name, vast distribution network, and opportunities in emerging markets. However, it also noted weaknesses and threats such as foreign currency fluctuations, growing public interest in "healthy" beverages, and competition from healthy beverage providers.2

Its SWOT analysis prompted Value Line to pose some tough questions about Coca-Cola's strategy, but also to note that the company "will probably remain a top-tier beverage provider" that offered conservative investors "a reliable source of income and a bit of capital gains exposure."

Five years later, the Value Line SWOT analysis proved effective as Coca-Cola remains the 6th strongest brand in the world (as it was then). Coca-Cola's shares (traded under ticker symbol KO) have increased in value by over 60% during the five years after the analysis was completed.

To get a better picture of a SWOT analysis, consider the example of a fictitious organic smoothie company. To better understand how it competes within the smoothie market and what it can do better, it conducted a SWOT analysis. Through this analysis, it identified that its strengths were good sourcing of ingredients, personalized customer service, and a strong relationship with suppliers. Peering within its operations, it identified a few areas of weakness: little product diversification, high turnover rates, and outdated equipment.

Examining how the external environment affects its business, it identified opportunities in emerging technology, untapped demographics, and a culture shift towards healthy living. It also found threats, such as a winter freeze damaging crops, a global pandemic, and kinks in the supply chain. In conjunction with other planning techniques, the company used the SWOT analysis to leverage its strengths and external opportunities to eliminate threats and strengthen areas where it is weak.

What Is SWOT Analysis?

SWOT (strengths, weaknesses, opportunities, and threats) analysis is a method for identifying and analyzing internal strengths and weaknesses and external opportunities and threats that shape current and future operations and help develop strategic goals. SWOT analyses are not limited to companies. Individuals can also use SWOT analysis to engage in constructive introspection and form personal improvement goals.

What Is an Example of SWOT Analysis?

Home Depot conducted a SWOT analysis, creating a balanced list of its internal advantages and disadvantages and external factors threatening its market position and growth strategy. High-quality customer service, strong brand recognition, and positive relationships with suppliers were some of its notable strengths; whereas, a constricted supply chain, interdependence on the U.S. market, and a replicable business model were listed as its weaknesses.

Closely related to its weaknesses, Home Depot's threats were the presence of close rivals, available substitutes, and the condition of the U.S. market. It found from this study and other analysis that expanding its supply chain and global footprint would be key to its growth.3

What Are the 4 Steps of SWOT Analysis?

The four steps of SWOT analysis comprise the acronym SWOT: strengths, weaknesses, opportunities, and threats. These four aspects can be broken into two analytical steps. First, a company assesses its internal capabilities and determines its strengths and weaknesses. Then, a company looks outward and evaluates external factors that impact its business. These external factors may create opportunities or threaten existing operations.

How Do You Write a Good SWOT Analysis?

Creating a SWOT analysis involves identifying and analyzing the strengths, weaknesses, opportunities, and threats of a company. It is recommended to first create a list of questions to answer for each element. The questions serve as a guide for completing the SWOT analysis and creating a balanced list. The SWOT framework can be constructed in list format, as free text, or, most commonly, as a 4-cell table, with quadrants dedicated to each element. Strengths and weaknesses are listed first, followed by opportunities and threats.

Why Is SWOT Analysis Used?

A SWOT analysis is used to strategically identify areas of improvement or competitive advantages for a company. In addition to analyzing thing that a company does well, SWOT analysis takes a look at more detrimental, negative elements of a business. Using this information, a company can make smarter decisions to preserve what it does well, capitalize on its strengths, mitigate risk regarding weaknesses, and plan for events that may adversely affect the company in the future.

The Bottom Line

A SWOT analysis is a great way to guide business-strategy meetings. It's powerful to have everyone in the room discuss the company's core strengths and weaknesses, define the opportunities and threats, and brainstorm ideas. Oftentimes, the SWOT analysis you envision before the session changes throughout to reflect factors you were unaware of and would never have captured if not for the group’s input.

A company can use a SWOT for overall business strategy sessions or for a specific segment such as marketing, production, or sales. This way, you can see how the overall strategy developed from the SWOT analysis will filter down to the segments below before committing to it. You can also work in reverse with a segment-specific SWOT analysis that feeds into an overall SWOT analysis.

Although a useful planning tool, SWOT has limitations. It is one of several business planning techniques to consider and should not be used alone. Also, each point listed within the categories is not prioritized the same. SWOT does not account for the differences in weight. Therefore, a deeper analysis is needed, using another planning technique.

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Six Forces Model: Definition, What It Is, and How It Works

By

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Updated April 01, 2023

Reviewed by Margaret James

Fact checked by

Vikki Velasquez

What Is the Six Forces Model?

The six forces model is a strategic business tool that helps businesses evaluate the competitiveness and attractiveness of a market. It provides a view or outlook by analyzing six key areas of business activity and competitive forces that shape any industry. The purpose of the model is to identify the structure of the industry—including strengths and weaknesses—to help formulate a corporate strategy.

Key Takeaways

- The six forces model is used to evaluate a firm's strategic position in a particular marketplace.
- The model emerged in the mid-1990s and built on the original five forces model.1
- The five forces model considers how potential new market entrants, suppliers, customers, substitute products, and rivalry can influence a company's profitability.2
- The sixth force of Porter's model is complementary products—the tech industry was impacted by intense competition due to the proliferation of new products and services in the 1990s.31
- The six forces model can also be used to determine the market's overall attractiveness in relation to profitability and competition.

How the Six Forces Model Works

The five forces model was originally developed by Michael E. Porter of Harvard Business School. It was used as a framework to analyze a company's competitive environment. As a means of analysis, there were certain limitations in that original model. Among those limitations was that the model was more applicable to simple and static markets rather than the complex and dynamic markets that exist today.4

Furthermore, the five forces model did not account for factors and influences from outside of the market or industry itself. The pace of change in business has increased and new business models continue to emerge that do not follow the same patterns as incumbent, older businesses.

Complementary products was added as a component to the model and the updated version includes six forces.5

Power of Buyers/Users

The power of buyers is one of the forces that affect the competitiveness of an industry, and there are several factors that impact the power of buyers or customers. First, industry competition depends on the number of buyers in the market. Markets with few customers may face strong price, preference changes, or sensitive customer theory implications as each individual buyer has more power compared to more saturated markets.

The competitive nature of a market also depends on the size of the users. Large buyers have more power than smaller buyers as they represent a larger share of the market, have the ability to make large purchases, and have greater resources to sway change in their favor.

Buyers may also have more or less power based on the product being offered. For instance, as discussed below, buyers may have more bargaining power if there are suitable substitutes they can buy instead. On the other hand, if products are more important, customers may not have any negotiation power (i.e. medication).

Power of Suppliers

The power of suppliers refers to the bargaining power that suppliers hold over an industry or market. Suppliers can have a significant impact on an industry or market when they are the only source of a critical input. For example, if a supplier can manufacture a highly technical or specialized part of a larger manufactured unit, that supplier may hold more power in the process and development of the good.

Suppliers can also have significant control over the price and quality of that input should they leverage their position to their benefit. Manufacturers may not be able to dictate their own prices or profit margins, as their supplier may impose upon them the prices that need to be paid for raw materials. On the other hand, industries with lower power for suppliers may allow for greater profit profitability.

The power of suppliers and buyers are constantly changing. The six force model must be continually revised to reflect the latest changes in the market.

Risk New Entrants

The risk of new entrants refers to the threat that new competitors will enter an industry and disrupt the existing competitive landscape. When the barriers to entry for an industry are low, new competitors can easily enter the market, compete with existing firms, and steal market share. This can lead to lower prices for consumers and reduced profitability for firms as they compete for business.

On the other hand, when the barriers to entry are high, it is more difficult for new competitors to enter the market. This can help protect not only the profits but the existing client relationships a company has formed. Companies who are able to enter the industry and maintain a presence are more likely to be rewarded in the long-term as not as many companies may be able to do the same.

There are several factors that can impact the risk of new entrants in an industry. Most often, there may be a financial hurdle that prevent a new market participant from easily being able to start a new company (i.e. consider the capital needed to start an oil drilling company). Other industries may already have competitor with very strong brand recognition (i.e. consider starting a new company to compete with Coca-Cola). Last, some industries are heavily regulated and may make it legislatively difficult to join or exist (i.e. consider trying to start your own bank).

Risk Substitutes

The risk of substitutes refers to the threat of alternative products or services that can satisfy the same customer needs. Whereas companies may not be able to enter the exact same industry or offer the same exact product, competitors may be able to offer a similar good that steals market share from a different product.

When the risk of substitutes is high, customers have more options to choose from, which can lead to decreased demand for the products or services offered by firms within an industry. This can result in reduced profitability and market share for firms within the industry. Consider two competing farmers, one which grows apples and the other that grows oranges. Should the apple farmer price his goods too high, consumers may consider buying oranges instead because they are a similar type good.

There are several factors that can impact the risk of substitutes in an industry. One of the primary factors is the availability and price of substitute products. If a customer simply can't access or afford one type of good, they may seek out a comparable. In addition, customers may or may not be loyal to a specific brand. Imagine how many different types of cell phones there are; for many Apple users, there is no suitable substitute.

Rivalry/Competition

The force of rivalry refers to the intensity of competition among existing players in the industry. Depending on how intense the competition is, certain industries may experience more narrow profitability or long-term potential sustainability.

Rivalry and competition are all defined by the factors discussed above; this force is also defined by the risk of complementary products below. In general, companies face risk based on other market participants. Whether its companies with stronger strengths, better relationships, more recognizable brand awareness, or superior products, the nature of other companies impact a company's ability to compete effectively and succeed in an industry.

Risk of Complimentary Products

Complimentary products are those that are used in conjunction with a particular product or service. Companies strategically devise complimentary products such as accessories, add-ons, or services that enhance the experience of a different product. A classic example of complimentary products is the interoperability and communication between Apple products such as an iPhone, iPad, and MacBook.

The risk of complementary products arises when a competitor has a comparable good but has a stronger set of complementary goods. These complementary goods, especially when they enhance the quality and usability of the primary product, may make the primary product more desirable.

There are also pricing elasticity considerations when comparing how one good may be compared to another.

In another example, consider all of the potential accessories related to a smartphone such as earbuds, chargers, or cases. Should a company decide to embrace these complementary goods, the company may be able to increase profitability and market share by having more related products in a given industry. If competitors were to choose to not embrace these complementary goods, these companies may be at a disadvantage by only having one primary product to sell.

Though this article emphasizes complementary goods in technology, complementary goods exist in almost every industry. Consider how a meal at your favorite hamburger restaurant often contains multiple types of goods along with a beverage.

Six Forces Model vs. Five Forces Model

There are a few reasons why a company would want to choose the six forces model over the traditional five forces model. It may be more strategic to consider the added force of complementary goods if the industry in question is highly volatile or changes rapidly. This sixth force allows companies to consider multiple revenue streams where the company can still collect profit in one line as others evolve.

As technology advances, it may continue to become easier and more natural for complementary products to exist. When cell phones were invented, smartwatches did not exist. Today, it's incredibly prevalent to sync a cell phone with a watch. As new products evolve and capabilities expand, the Porter's Five Force model may fail to consider how technological advancements may influence the ways companies can pair products.

Last, the six forces model holds the advantage of simply consider more relevant variables. Companies must consider all risks and elements of competition when evaluating strategy, and adding one additional force may make all the difference when evaluating long-term product implications. In some cases, additional models specifically add even more forces such as risks of government regulations or risks specific to technology.

Advantages and Disadvantages of the Six Forces Model

Pros of the Six Forces Model

The advantages of the six forces model are very similar to that of Porter's Five Force model. The key takeaway is that the six force model helps to identify potential areas of competition. The model is structured in a way where a company can analyze the competitive environment of an industry ranging from the buyers, suppliers, and other market forces. This level of analysis can help companies identify areas of potential competition and opportunities for differentiation.

The six force model can also help companies think more strategically about their industry, competitors, and customers. Though the company must be armed with relevant and appropriate data, the conclusions drawn from the six forces model may lead to better decision-making and a more focused approach to business. It may also lead to a more refined, appropriate delegation of where to deploy capital.

Last, the primary goal of the model is to provide a framework for analyzing the key factors that influence the competitiveness of an industry. This structure enhances the governance of a company and sets some rules on how the company should be considering running its business. Without this framework, it is much more difficult to contemplate the external factors that may be more challenging to monitor.

Cons of the Six Forces Model

Also like the Porter's Five Forces model, there are some drawbacks to the six forces model. The six forces model focuses primarily on the external environment and does not account for internal factors such as a company's own strengths and weaknesses. A company may have excellent positioning in the market but may lack oversight into severe weaknesses such as not have the appropriate level or talent of staff needed to succeed.

The six forces model can oversimplify complex situations, as is the case with many other risk frameworks. The model assumes that the competitive environment is relatively stable and that the industry structure is easily defined, which is usually never the case. In addition, the model requires constant refinement in industries that are continually evolving, making this framework at risk to be outdated as the industry changes and new risks arise. The six forces model may also not take into account industry-specific factors that can affect competitiveness.

Last, the six forces model relies on management input and assumptions. In some cases, management may simply not know risks exist. In other cases, poor management may simple fail to recognize risks or choose not to address them. The six forces model is only as strong as the opinions contributed to the framework, so it is up to management on how valuable the six forces model can be.

Pros

- Often helps identify the competitive environment outside of a company
- Enhances strategic thinking of a company and the forces it faces
- Provides guidance to management on how to consider external risks
- May cause management to consider factors that were not previously being considered

Cons

- May exclude internal forces that dictate many aspects of success
- May oversimplify complicated situations
- May downplay risks, especially if management does not consider them
- Is often less dynamic than other frameworks

Example of the Six Forces Model

In June 2011, Apple Inc. introduced a breakthrough technology of cloud services called iCloud.6 Used extensively today, the service allowed applications on one's iPhone, iPad, iPod touch, Mac, or PC to automatically and wireless store content to be pushed across all devices. In this situation, owning one product across this product line lends itself to potentially buying complementary goods. For example, if you already own a MacBook and need a new phone, there may be substantial benefits to buying across the Apple line.

This strategic approach to building out a product line is now being emulated across the technology industry. As of April 2023, consider how Google's Pixel line now contain or will contain cell phones, premium earbuds, smartwatches, and tablets.7 Regarding the six forces model, companies must consider how once a customer has committed to one of these product lines, it may become very difficult to sway them to invest in a new product line.

What Is the Sixth Force in the Six Forces Model?

The six forces model takes Porter's Five Forces model and adds the force of complementary goods. Complementary goods are those that consumers buy in addition to a primary product to enhance or supplement the experience.

What Is the Risk of Complementary Goods?

The risk of complementary goods is it may become difficult is not prohibitively expensive to convert a customer from one complementary product line to another. In the example discussed above, Apple customers may have commit thousands of dollars to building out their portfolio of Apple products. The risk to Google and their Pixel line is these customers may never be able to be captured because the complementary line of goods is too strong for those who have already bought in.

What Is the Purpose of Force Analysis?

The purpose of any force analysis framework is mainly to identify the external circumstances that may impact how a company is able to strategically plan for the future. These forces, such as buyers, suppliers, or competing products, may inherently shape the way a company must operate. In many cases, these forces can not be easily changed, so they are simply inherent forces a company must work around and work with to build a viable business strategy.

What Is a Primary Criticism of the Six Forces Model?

Both Porter's Five Forces Model and the six forces model are criticized for being too static. These frameworks have a rigid set of rules which may be helpful to management to guide how to analyze an industry. On the other hand, the framework isn't really customized to a specific industry or set of circumstances which may cause risks or problems to be oversimplified.

The Bottom Line

The six forces model is an extension of Porter's Five Forces model which identifies various external forces that influence how an industry operates. The model adds one more force to consider the risk of complementary goods. The six forces model can be helpful to assess risks and enhance long-term strategic planning, though it does have the downside of needing constant refinement to be relevant and not being a more dynamic tool.

Article Sources

Related Terms

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V Bank Restructuring

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The three crisis countries and Malaysia implemented comprehensive bank restructuring strategies. This section discusses selected issues related to the design and implementation of these strategies. It reviews broad principles and policies underlying such strategies and discusses operational issues related to the restructuring, such as institutional arrangements, issues in valuing financial institutions, the speed of recapitalization, methods to deal with troubled institutions, management of value-impaired assets, the cost of the restructuring, institutional constraints, and linkages with corporate restructuring.

Broad Principles and Policies

A broad-based restructuring strategy should achieve the following economic objectives: (1) restore the viability of the financial system as soon as possible so that it can efficiently mobilize and allocate funds (a core banking system must be in place to preserve the integrity of payment systems, capture financial savings, and ensure essential credit flows to the economy); (2) throughout the process, provide an appropriate incentive structure to ensure effectiveness and, as far as possible, avoid moral hazard for all market participants, including bank owners and managers, borrowers, depositors and creditors, asset managers, and government agents involved in bank restructuring and supervision; and (3) minimize the cost to the government by managing the process efficiently and ensuring an appropriate burden sharing (by distributing losses to existing shareholders). To achieve these objectives, governments had to ensure effective governance of intervened banks, application of appropriate resolution procedures, maximization of the value of nonperforming assets, and optimal involvement of private investors. While all the crisis countries followed these broad objectives, strategies varied according to local circumstances, government preferences, and the depth of the crisis.

Systemic bank restructuring requires strong government leadership because the restructuring seeks to preserve an essential economic infrastructure and entails major macroeconomic and wealth distribution effects, even if in essence it is a microeconomic process. Key steps include decisions on institutional arrangements to deal with the crisis; criteria for evaluating institutions; a strategy to deal with nonviable institutions and to restructure the viable ones consistent with macroeconomic goals; the extent and modalities of public sector support for restructuring; the arrangements for loan recovery and workouts and asset management; arrangements to ensure operational restructuring; and the pace of restructuring and compliance with prudential norms (see Box 9). Experience also indicates that clear information to the public on the steps to be undertaken is a crucial part of the strategy; a nontransparent restructuring process may fail to restore the public's confidence in the government and the financial system.

Box 9.

Principal Issues in Devising a Bank Restructuring Strategy

The following issues need due attention in developing a strategy for restructuring banks.

- Institutional and legal frameworks for the restructuring, including the allocation of qualified human resources;
- Criteria for discriminating between those institutions that are sound and need no public support, those that are viable but require public support, and those that should exit the system;
- Modalities to assess the financial condition of institutions (deciding on who will do the valuation, and on the valuation rules to be applied, including loan classification, loan-loss provisioning, and collateral valuation);
- Methods for dealing with troubled institutions (liquidation, mergers, nationalization, use of bridge banks, or purchase and assumption operations);
- Treatment of existing and new shareholders;
- Role of government and private (domestic and foreign) sectors in contributing equity and subordinated debt;
- Financing arrangements, including target level of recapitalization, types of instruments, terms and conditions for the government's support of restructuring (guided by the principle of minimizing the government's contribution);
- Arrangements for loan recovery and workouts and management of problem assets;
- Appropriate linkages with corporate restructuring;
- Operational restructuring of banks;
- Timeframe for the different steps in bank restructuring;
- Information campaign and transparency on the restructuring strategy to ensure credibility and public confidence;
- Exit strategy from government ownership of banks; and

- Exit strategy from blanket guarantee.

The strategies adopted by the crisis countries have been broadly similar, in that they all have aimed at removing nonviable institutions and requiring strict compliance with international best practices for capital adequacy, loan classification, and loan-loss provisioning by the end of the restructuring period (Table 6). All countries aimed at maximizing (domestic and foreign) private sector involvement in the recapitalization process. In the event, the extent of private sector involvement has depended on country-specific circumstances, such as the depth of the crisis, the availability of domestic private funds amidst a deteriorating macroeconomic situation, and the legal framework for attracting foreign investors.

Table 6.

Summary of Measures to Address the Financial Sector Turmoil

Measure	Indonesia	Korea	Malaysia	Philippines	Thailand
Emergency measures					
Liquidity support	Yes	Yes	Yes	Yes	Yes
Introduction of a blanket guarantee	Yes	Yes	Yes	No	Yes
Institutional measures					
Establishment of an overarching restructuring authority	Yes	Yes	Yes[1]	No	No
Establishment of a separate bank restructuring authority	Yes	No	Yes	No	No
Establishment of a centralized asset management corporation	Yes	Yes[2]	Yes	No	No[3]
Adoption of a special corporate debt restructuring framework	Yes	Yes	Yes	No	Yes
Operational autonomy of restructuring agencies	Limited	Yes	Yes	n.a.	n.a.
Restructuring measures					
Intervention in financial institutions that were weak or insolvent.	Yes	Yes	Yes	Yes	Yes
This would include:					
Mergers of weak institutions	Yes[4]	Yes	Yes	Yes	Yes[4]
Closure of insolvent institutions	Yes	Yes	No	Yes	Yes
Use of public funds to purchase nonperforming assets	Yes	Yes	Yes	No	No
Use of public funds to recapitalize institutions, including:	Yes	Yes	Yes	No	Yes
State intervention in banks	Yes	Yes	Yes	No	Yes
Elimination or dilution of current shareholder stakes of insolvent banks	Yes	Yes	Yes	Yes	Yes
New direct foreign investment	Yes	Yes	Limited[5]	Yes	Yes
Other measures					
Measures to encourage corporate restructuring	Yes	Yes	Yes	Yes	Yes
Steps to improve prudential supervision and regulation	Yes	Yes	Yes	Yes	Yes

Source: IMF.

[1]Steering committee chaired by the central bank.

[2]The powers and resources of a preexisting asset management company were substantially increased.

[3]The Financial Sector Restructuring Agency (FRA) was established to liquidate 56 closed finance companies, and the asset management company to deal with residual FRA assets.

[4]Between government-owned intervened institutions.

[5]Foreign banks are allowed to purchase up to a 30 percent stake.

Malaysia and the Philippines never experienced a full–blown crisis and applied different restructuring strategies from those in the three crisis countries. In Malaysia, the emergency measures assisted in containing pressures on the system and were followed by a package of proposals that focused on recapitalizing banks that were expected to become undercapitalized in the course of 1998; strengthening the finance company sector through consolidation (mergers); establishing a strong institutional framework to manage the restructuring; and strengthening of regulatory and supervisory frameworks. Faced with the threat of a crisis, the Philippines adopted a financial sector reform program in early 1998 to strengthen the ability of the system to withstand shocks. The main ingredients were a streamlining of the resolution procedures of troubled banks, encouragement of mergers, the privatization of the remaining government equity stake in the Philippine National Bank (the second largest bank in the country), now planned for mid-2000, and an enhancement of the prudential and supervisory frameworks.[34]

The cost of restructuring the financial sector is typically high and largely falls on the public sector. This reflects a severe lack of equity capital in the banking system and the corporate sector at the outset of a crisis. In the crisis countries, seeking efficient ways to restructure objectives at the least fiscal cost was a key concern of the authorities. A poor fiscal situation could severely constrain the public sector's capacity to absorb the cost of the restructure. This was not the case in Indonesia, Korea, and Thailand, which all had relatively sound fiscal positions at the onset of the crisis.[35] However, the immense scale of public support needed will most likely require special efforts to preserve medium-term fiscal sustainability.

Institutional Arrangements

The allocation of responsibilities for handling the restructuring was a crucial first step in the strategy. Taking into account not only technical considerations but also political circumstances and institutional and legal frameworks already in place, governments put in place a variety of institutional structures:

- In Indonesia, no institution was in charge of restructuring until the Indonesian Bank Restructuring Agency (IBRA) was established in January 1998 under the auspices of the ministry of finance. Initial problems in providing adequate legal and regulatory powers to the IBRA delayed the effective start of bank restructuring and asset management. Bank Indonesia remained the principal supervisory authority, though its powers vis-à-vis state-owned banks and IBRA had not been clearly defined.
- In Korea, responsibility for restructuring was given to the newly established Financial Supervisory Commission. The Financial Supervisory Commission also coordinated the work of the other agencies involved in addressing the crisis, including the Korean Asset Management Corporation (KAMCO), a bridge bank (Hanaerum Merchant Bank), and the Korean Deposit Insurance Company (KDIC).
- In Malaysia, a well-designed institutional framework supported by strong legislation was already in place. The restructuring has been coordinated by an overarching steering committee chaired by Bank Negara Malaysia, which is also the supervisory authority, and includes managers of the three other agencies involved, that is, Danaharta (the asset management company), Danamodal (the bank recapitalization company), and the Corporate Debt Restructuring Committee (the corporate restructuring agency).
- In Thailand, no new agency was set up with specific responsibilities for bank restructuring. The Financial Institutions Development Fund, a legal entity within the Bank of Thailand, which is also the supervisory authority, has been in charge of managing liquidity and solvency support to intervened banks. However, most decision making has been left with the Ministry of Finance. The Financial Institutions Development Fund has been hampered by a lack of clear legal powers. The Financial Sector Restructuring

Agency (FRA) was set up to assess the viability of the 58 suspended finance companies and to liquidate the assets of the 56 companies that were closed. A public asset management company was established to purchase residual assets from FRA. Moreover, the Corporate Debt Restructuring Advisory Committee was set up to facilitate corporate debt restructuring.

- In the Philippines, no new institutional arrangements were introduced. The central bank's role in bank restructuring has been based on its role as regulator and supervisor. The Philippines Deposit Insurance Corporation (established in 1963) has continued to be involved with the resolution of insolvent banks; problems of weak but solvent banks have been addressed by encouraging mergers.

Issues in Valuing Bank Assets

Realistic valuation of banks' assets is an important factor in establishing the viability of individual banks, but it is difficult during a crisis. In fact, in these circumstances there is no precise method for valuing nonperforming loans.[36] There are no market prices for nonperforming loans. Valuation based on appropriately discounted present values becomes less reliable as estimates of cash flows, interest rates, and underlying business conditions become volatile. The valuation can be particularly difficult when the viability and repayment capacity of borrowers is in doubt. Also, it is hard to value collateral, not only because of uncertain prices and a limited market, but because of uncertainty as to whether, and when, the bank can seize the collateral.

Differing approaches to valuation were used to improve self-assessments by banks in the three crisis countries. While banks continued to be responsible for valuing their assets and making provisions for losses, they were also subject to intensified on-site examinations by supervisors and assessments by external auditors. These on-site examinations and external audits generally revealed situations that were worse than those reported by the banks. In Indonesia and Korea, these assessments were further supplemented with audits by internationally recognized accounting firms. In Thailand, the authorities questioned the value of additional assessments by international auditors of banks meeting all prudential and regulatory requirements. Each approach has advantages and drawbacks. Self-assessments are often biased due to conflicts of interests; external audits by local firms and supervisory evaluations may not carry sufficient credibility in the market; and foreign assessors may have a limited understanding of a borrower's repayment capacity and other local circumstances. In addition, international auditors might be too cautious in their valuations, perhaps to limit their potential liability in case they overvalued assets. Resorting to international audits, however, seems essential for credibility purposes in cases of pervasive government interference or insider lending.

The information collected through either of these valuation methods serves as a basic input for the restructuring authority's decisions on the viability of financial institutions. Thus, regardless of the valuation methods used, the end result must allow the restructuring agency to compare banks, based on uniform and transparent criteria.[37] This implies that the restructuring agency or the bank supervisor has to choose the valuation procedures, including the possible use of external valuation boards. It also implies that the agency be able to issue regulations on how banks should assess the value of their assets, but be prepared (and have the power) to overrule valuations by others where deemed appropriate. This power to overrule needs to be used judiciously, particularly in cases where the assessment has been done by independent outsiders. Moreover, valuations should be subject to revisions as economic conditions change. In any event, most prospective private investors will undertake their own due diligence valuations prior to any investment in or acquisition of assets or financial institutions.[38]

Speed of Recapitalization

In all countries, the bank restructuring strategy relied on a tightening of rules for loan-loss provisioning and the observance of minimum capital requirements.[39] This gave banks a basis for recognizing their losses based on international best practices, identifying their capital shortfalls, and putting forward recapitalization plans. The tightening of regulations was gradual, however.[40] On the one hand, markets were demanding more information about banks' financial conditions and strengthened regulation and supervision. Meeting those demands was viewed as necessary for investors to restore the flow of funds to the affected countries and resume lending and provide capital to domestic financial institutions. On the other hand, insufficient resources (e.g., capital funds to meet minimum capital adequacy requirements or long-term foreign financing to eliminate maturity mismatches) made it impossible for banks to meet strict prudential standards in the short run. Requiring banks to meet international standards for capital adequacy requirements and loan-loss provisions in a very short timeframe would have forced them to shrink their balance sheets drastically. This would have further reduced credit to the private sector and aggravated the recession. Thus, a gradual approach was used. Moreover, it would have been impossible for banks to effect a reduction in their outstanding loans sufficient to meet the capital adequacy requirement.

Gradualism for achieving compliance with international standards can apply to loan-loss provisioning or capital adequacy. The former overstates capital adequacy while the latter shows a capital adequacy requirement below the regulatory minimum. Countries have used both approaches. IMF staff has emphasized that full transparency of the policy considerations behind the decisions should be assured to enable investors to make educated decisions.[41] In Indonesia and Korea, banks have been given time to meet their normal capital adequacy requirements. The minimum capital adequacy requirement is currently at 4 percent in Indonesia, but is to increase to 8 percent by the end of 2001. In Korea, commercial banks were required to meet a capital adequacy requirement of 6 percent by March 1999 and 8 percent by March 2000 (a different schedule was applied to merchant banks). In Thailand, an 8.5 percent capital adequacy requirement for commercial banks (8 percent for nonbank financial institutions) applies in full while the loan-loss provisioning requirements are increased each semester until the end of year 2000.[42] In Malaysia, valuation and provisioning rules were strengthened, but some gradualism was allowed with respect to public disclosure of nonperforming loans. In the Philippines, higher minimum capital requirements were phased in gradually, aiming at full compliance by the end of 2000.

Dealing with Troubled Institutions

Once nonviable banks were separated from viable ones, governments in all crisis countries and Malaysia devised strategies to rehabilitate those institutions deemed viable. To minimize the fiscal cost for the government and to preserve private ownership of banks, each government encouraged banks to rehabilitate themselves. In cases where market-based solutions were not forthcoming, governments sought to assist in forging such solutions. In case of insolvency, governments intervened. The degree of government involvement largely related to the degree of insolvency of the banks.

The main vehicle for seeking private-sector-based resolutions was for the respective governments to request recapitalization and rehabilitation plans from existing shareholders. In all countries, owners of undercapitalized banks were requested to provide timetables to raise the banks' capital adequacy requirements to prescribed levels and to show their viability.[43] In Korea, the government requested from banks with capital adequacy requirements below 8 percent self-improvement plans to reach that threshold, including contributions of new capital from existing or new shareholders. Approval of those plans was a requirement for banks to keep their license and for them to receive public sector support through the sale of nonperforming loans to KAMCO or in the form of equity. The precise content of individual plans varied depending on the circumstances and the size and significance of the institution. Memoranda of understanding between the banks and supervisory agencies were used to document the approval of the plans and the conditions attached to them. The conditions typically included operational improvement benchmarks on matters such as cost reduction, labor shedding, and rate of return on assets. Likewise, the Bank of Thailand requested half-yearly capitalization plans from all undercapitalized institutions, spelling out how they would bring in equity (domestic and foreign) to meet their capital adequacy requirements. These plans were agreed upon under binding memoranda of understanding with the Bank of Thailand.

The initial lack of private capital in the three crisis countries forced the governments to promote plans whereby new private capital contributions would be matched in varying proportions by the government. Under Indonesia's joint recapitalization program, for banks with a capital adequacy requirement between +4 percent and -25 percent, owners have to submit a business plan demonstrating medium-term viability, in addition to passing a fit-and-proper test. Schedules to eliminate excess connected lending also had to be agreed upon. Owners had to provide 20 percent of the capital shortfall and the government the remaining 80 percent.[44] Korea followed a case-by-case approach, under which the government was prepared to arrange for KAMCO purchases of nonperforming loans, purchase subordinated debt, or subscribe new capital, to assist private banks' recapitalization efforts. In Thailand, the government will match any amount of capital injected by private investors, provided (1) the bank has brought forward and fully implemented the end of year 2000 loan classification and provisioning rules; (2) the new capital (public and private) is injected with preferred status; (3) the government and the new investor have the right to change management; and (4) an acceptable operational restructuring plan has been presented to the authorities, including procedures for dealing with nonperforming loans and for improving internal control and risk management systems.[45] This scheme has contributed to restoring confidence in the Thai banking system, and hence, inducing private banks to find private investors with or without the public matching funds.

To facilitate foreign participation in the restructuring process, governments have liberalized regulations on foreign ownership of financial institutions. In addition to bringing in foreign capital, these measures have also aimed at introducing international banking expertise into the domestic financial system to enhance competition. All countries have allowed foreign investment in existing financial institutions. In Indonesia, two sizeable private banks have recently been bought by foreign banks and further purchases are expected. In Korea, the banking law has been changed to allow foreigners to acquire a controlling interest in domestic banks, including full ownership, and the government is seeking to sell a controlling interest to foreign investors in two of the largest commercial banks. In addition, foreign investors have contributed capital to other major commercial banks and have started negotiations to invest in other segments of the financial sector, such as in insurance companies. In Malaysia, foreign shareholders are allowed to take a stake in domestic banking institutions to up to 30 percent. In Thailand, foreign ownership in excess of 49 percent in existing banks has been allowed to help restructure the system. Strategic foreign investors have taken a majority stake in two small private banks, and foreign ownership in some large banks is approaching 50 percent. Malaysia has indicated that foreign banks with operations in the country will be allowed to buy finance companies. The Philippines has not yet been fully opened to new foreign ownership of existing banks, but further liberalization is planned. Recently drafted legislation has been submitted to allow 100 percent ownership of distressed banks, but this is to be reduced to 70 percent over 10 years.

When self-rehabilitation was beyond reach, governments resorted to a variety of bank resolution methods to deal with troubled institutions. Such methods included interventions, nationalizations, mergers, purchase and assumption operations, and the use of bridge banks.

A general principle in resolving troubled institutions is that existing shareholders should bear losses until their capital has been fully written off. This principle was generally applied in the crisis countries, although in some countries shareholders were left with nominal stakes to take into account legal restrictions on a full write-down or to avoid costly legal challenges by the old shareholders. In Indonesia, for example, the shareholders in the largest bank taken over in April 1998 were diluted to 1 percent of total equity. In Korea, until amended in mid-1998, legislation prevented shareholder stakes from being written down below the minimum capital required for a bank to operate. In Thailand, the shares of owners in intervened banks have been written down to token values.[46] Furthermore, in Indonesia, the authorities are pursuing former shareholders of failed banks for personal indemnification for past central bank liquidity support in those cases where banks have been in violation of prudential regulations, especially for connected lending.

The contribution of new shareholders is of key importance to help strengthen bank finances and governance. All countries have revised the rules and regulations governing new shareholders. Existing shareholders are required to meet fit-and-proper tests to remain eligible, and rules regarding conflicts of interest for shareholders have been strengthened. A key issue is the maximum size of the equity share of each individual shareholder: concentration of equity may facilitate governance and capital injections, but concentration may also lead to excessive connected lending and large exposure risks. New or amended banking laws in Indonesia and Korea address this trade-off. In Korea, for instance, the law limits the maximum shareholding stake of domestic residents in commercial banks unless that stake is matched by a foreigner's stake.

In the three crisis countries, deep insolvency of private banks led to the nationalization of a significant part of the private bank sector. In Indonesia, IBRA has acquired control of 12 banks, representing 20 percent of the banking sector. The authorities continue to distinguish between the "banks taken over," however, and the seven state banks existing before the crisis, because the aim is to resolve the former through privatization, mergers, or closures within a relatively short period. In Korea, public equity support was very extensive because the limits on single ownership of commercial banks meant that there were no significant strategic shareholders that could be called upon to inject funds into the banks. Thus, five of the six major corporate lending banks have ended up with government shareholdings in excess of 90 percent. In Thailand, public equity support has mainly been provided to the institutions that were state-owned at the outset of the crisis, to the six commercial banks and 12 finance companies that have been intervened, and to match private equity contributions in a few private banks.[47] All the governments have expressed their commitment to privatize their state-owned banks as soon as feasible, Korea and Thailand have already made some progress in this direction.

Closures, mergers, purchase and assumption operations, and bridge banks were useful techniques to consolidate the financial sectors in most countries, and governments adopted them flexibly under the circumstances. As mentioned before, closures were an important measure in all three crisis countries, as indicated by the proportion of the closed entities in the sector. Government-assisted mergers were used in all countries to consolidate the banking system. In Korea and

Malaysia, mergers involved private sector banks, but in Indonesia and Thailand such operations were limited mostly to the state-owned sector. In Indonesia, four of the seven state banks are in the process of being merged into a single bank. In Thailand, the authorities are merging the intervened banks and finance companies into three new banks. The 56 closed finance companies are being liquidated by FRA through public auctions; the liquidation continued through the end of 1999. Mergers, purchase and assumption operations, and bridge banks have been used in Korea.[48] The strategy in Malaysia was different for commercial banks and finance companies. For the commercial banks, a recapitalization strategy was set up for 14 banks that were identified as undercapitalized, or projected to become undercapitalized in the course of 1998; in addition, four banks would be merged into two. One such operation, involving two banks, has been completed. For the finance companies, the government initially aimed at consolidating the 39 companies to less than half that number through mergers. As of August 15, 1999, 15 had been absorbed or merged.[49] In the Philippines, private-sector-led mergers were encouraged through easing of accounting and prudential regulations.

In the event, governments used a wide variety of resolution strategies. In a deep systemic crisis, no standard solution can be prescribed within the broad overall restructuring strategy. Governments had to deal with troubled institutions on a case-by-case basis. The final solution for each institution had to take into account the interest of the parties involved (existing shareholders, potential domestic or foreign investors, the government, and creditors) as well as the legal and regulatory framework, and, often, the political situation. As a result, the outcome for the sector as a whole necessarily varied from country to country (Table 7).

Table 7.

Mergers, Closures, and State Interventions of Financial Institutions

(June 1997 to June 1999)

Source: IMF. Note: Figures in parentheses refer to percentage of total banking system assets held by the corresponding group of institutions

[1]Banks with over 90 percent government ownership. The government owns varying amounts of shares in seven other commercial banks.

[2]Closures of a number of rural banks and small thrifts are not included. Such closures are routine operations in the Philippines.

[3]In Thailand, most of the intervened institutions were later merged. Thus, columns one and three include the same institutions.

Dealing with Impaired Assets

Proper management and disposition of nonperforming assets is one of the most critical and complex aspects of successful and speedy bank restructuring. The government's overarching objective should be to maximize the value of the impaired assets in the system, minimize fiscal costs, and prevent credit discipline of borrowers from deteriorating. Various approaches can be adopted to achieve those objectives. Impaired assets may either be held and dealt with by the financial institutions themselves or sold to special companies or agencies created to handle bad assets. The likelihood that the borrower will be able to honor his loan contract should determine whether the asset should be handled as a loan subject to collection or as a case for liquidation, including collateral. The more likely that the borrower will honor the loan contract, possibly after renegotiation, the more reason there is to keep it in a bank. If the borrower is bankrupt, or otherwise unlikely to repay, and the bank has to seek recovery of collateral— which often takes the form of real estate or other physical assets—a separate institution with special knowledge in asset resolution techniques most likely should undertake the recovery.

The optimal strategy for managing and disposing of impaired assets has many variations, depending on factors such as the nature of the problem assets, their overall size and distribution, the structure of the banking system, the legal framework, and available management capacity in the banks and in the public sector. There is no single optimal solution but rather a combination of solutions for each country that may vary over time and for each bank. The strategy will need to consider the speed of disposition of the assets and whether to use a centralized or decentralized process and institutional framework (Table 8).

Table 8.

Framework for Managing Impaired Assets

Speed of disposition is determined by the quantity, quality, and type of assets; market demand for such assets; and whether the assets belong to a bank that has been closed or to one in operation. While economic recovery requires some asset sales or liquidations to help markets find new price levels, the markets may be extremely thin and care needs to be taken not to destroy values for the entire banking system through "fire-sale" liquidations. This is of particular concern in a systemic crisis when the amount of problem assets typically is very large. The value of impaired assets may be better preserved through careful management and gradual sales by specialized institutions (in this paper all such units located outside banks are referred to as asset management companies). At the same time, it is important not to "park" severely impaired assets for years in asset management companies while waiting for an economic upturn. Such an approach may result in accrual of carrying costs and ultimately bigger losses. Moreover, poor management of the assets may deteriorate their value. In the case of failed banks, it is important to move the better quality loans to other operating institutions as fast as possible to preserve value. In Korea this was done through bridge banks, while in Thailand most of the assets of the 56 closed finance companies have been sold to the private sector through public auctions carried out by the FRA.[50]

Each country considered the advantages and disadvantages of dealing with impaired assets in a centralized or decentralized asset management company structure and related ownership issues in its own circumstances (Table 9). Centralized asset management companies, which typically need to be state-owned, have been used in Korea and Malaysia, and more recently in Indonesia. Advantages and disadvantages of state-owned, centralized asset management companies are shown in Box 10. A key objective of a state-owned centralized asset management company is to buy nonperforming loans from banks and thus help banks clean up their balance sheets as fast as possible. It is also useful in cases of mergers or bank sales when the merging or purchasing party may not wish to get a large amount of nonperforming loans as part of the deal. Thailand has chosen a decentralized process, encouraging each commercial bank to establish its own separate asset management company. However, a public asset management company was established to purchase residual assets from FRA. In Indonesia private asset management companies to deal with failed banks were ruled out due to governance concerns.[51] The sale of banks'assets to an asset management company forces immediate recognition of the value of the loan. This may deter such sales in cases where banks have been carrying these loans at inflated values.

Table 9.

Public Asset Management Companies in the Asian Crisis Countries

Source: IMF.

[1]KAMCO existed before the crisis

[2]End of June 1999.

[3]This 4 percent is included in the 17.5 percent

Box 10.

Advantages and Disadvantages of a Centralized Public Asset Management Company

The crisis countries considered the following when deciding whether to adopt a centralized, public asset management company.

Advantages

- Serves as a vehicle for getting nonperforming loans out of troubled banks, based on uniform valuation criteria.
- Allows government to attach conditions to purchases of nonperforming loans in terms of bank restructuring.
- Centralizes scarce human resources (domestic and foreign).
- Centralizes ownership of collateral, thus providing more leverage over debtors and more effective management.
- Serves as a third party for insider loans (Indonesia).
- Can better force operational restructuring of troubled banks.
- Can be given special legal powers to expedite loan recovery and bank restructuring.

Disadvantages

- Management is often weaker than in private structures, reducing the efficiency and effectiveness of its operations.
- Such agencies are often subject to political pressure.
- Values of acquired assets erode faster when they are outside a banking structure.
- Nonperforming loans and collaterals are often "parked" long-term in an asset management company, not liquidated.
- If not actively managed, the existence of a public asset management company could lead to a general deterioration of credit discipline in financial system.

- Cost involved in operating an asset management company may be higher than a private arrangement.
- If dealing with private banks, determining transfer prices is difficult.

Pricing is the most difficult issue for a public asset management company purchasing assets from private banks. The issue is less severe for a public asset management company buying assets from a state-owned bank or a private asset management company buying assets from a private bank.[52] This is due to the valuation difficulties for impaired assets discussed earlier. Purchases of a bank's assets at inflated values by an asset management company amount to a back-door recapitalization of the bank and a bailout of the bank's shareholders.[53] The impossibility of determining an unambiguously fair market price for nonperforming loans has so far deterred the Thai authorities from setting up a public, centralized asset management company and they have instead opted for a decentralized approach. Proper transfer pricing is also of key importance for the incentive structures for both the asset management company and the banks—there is a need to set up a system that provides the right balance. Excessive prices for nonperforming loans may also induce banks to reduce their recovery efforts, which could lead to a general deterioration of credit discipline and loan values throughout the banking system.

A decentralized approach that encourages each bank to set up its own asset management company allows arrangements to suit each bank's conditions (see Table 10). Thailand followed such a route, encouraging banks to set up their own asset management companies to which they can transfer assets at market value. Five private banks are in the process of setting up asset management companies and other banks (including state-owned ones) are expected to follow. Until recently, however, this process has been held up due to capital scarcity.

Table 10.

Pros and Cons of Decentralized Asset Management

The final results of the various strategies will only be known when the process of recovering impaired assets has been completed. This process will take time. As noted earlier, it would be unwise to undertake massive sales of assets in the midst of the crisis. Also, practical problems—such as the need to acquire proper legal title to collateral and to prepare an inventory of the assets—require time to be solved. Nonetheless, sales of impaired assets have begun in Korea, Malaysia, and Thailand.

Cost of Restructuring

Estimating the cost of financial restructuring is one of the more challenging issues. There are costs both in the private and public sectors to cover losses and contribute new capital. The private sector outlays will not be considered here. The government's *gross costs* for the restructuring arise from paying out guaranteed bank liabilities; providing liquidity support; assisting in meeting capital adequacy requirements; and purchasing nonperforming loans. The *net costs* will only be known after proceeds from (re)privatization of banks and recoveries of loans accruing to the government have been taken into account.[54] A more complete picture of the cost would also include the indirect effects of the crisis and subsequent reforms. The magnitude of these costs and the need for political support for the process require transparent accounting rules and disclosure of information.

Gross costs in the three crisis countries and Malaysia are likely to range from 15 percent to 45 percent of GDP (Table 11). Estimating the cost of restructuring is an evolving exercise because loss recognition is still taking place as part of the corporate restructuring process.[55] The cost of restructuring will depend on several factors, including domestic and external macroeconomic conditions, the effectiveness of corporate restructuring, and the efficiency of bank restructuring efforts. As a result, estimates for the cost of restructuring vary widely, with government numbers generally lower than market estimates.[56] While IMF staff has continuously made estimates based on different scenarios to discuss policy options with the authorities, it has refrained from including any estimates in official documents because of their sensitive and crude nature.

Table 11.

Authorities' Estimates for the Gross Cost of Financial Sector Restructuring

Source: National authorities. Note: Gross costs do not include recoveries. The cost will depend on a number of factors, including macroeconomic conditions, effectiveness of corporate restructuring, and the efficiency of the bank restructuring effort. Estimates of these costs are based on different assumptions and methodologies and may therefore not be comparable across countries.

The need for immediate liquidity support at the onset of the crisis meant that the central banks in the crisis countries were the main providers of funds. In Indonesia and Thailand, formal arrangements to allocate costs between the central bank and the government were weak or did not exist. Meanwhile, in Indonesia, the government has issued 150 trillion rupiah (13 percent of GDP) of indexed bonds to the central bank to compensate it for past liquidity support. In Thailand, the government was authorized to issue bonds for 500 billion baht (10 percent of GDP) to cover losses in the Financial Institutions Development Fund, and the government has announced its intention to cover additional losses in a similar way.

Bonds issued or guaranteed by the governments of Indonesia, Korea, and Thailand are the main instruments for financing the government's contribution to the restructuring costs (Table 12). Market interest rates and regular coupon payments are needed, because, as opposed to zero coupon bonds, they help banks'cash flows. Tradable bonds help banks manage their liquidity, as they can sell the bonds if liquidity is needed.[57] Given the large amount of bonds to be issued, making them tradable also assists the development of a government bond market and reduces the cost for the government; thus, the development of an efficient microstructure for government securities markets becomes critically important.[58] Only Korea and Malaysia used a combination of cash and bonds to provide capital, although cash injections in both cases were so minimal that they did not interfere with monetary policy. The government of Indonesia has recently approved the issuance of another 100 trillion rupiah of bonds (9 percent of GDP) to the banks to finance the first wave of bank recapitalization. The interest cost of all the bonds is borne by the budget. In Korea, parliament approved the issuance of 64 trillion won of bonds to finance KAMCO and KDIC (15 percent of GDP).

Instruments Used to Recapitalize and Purchase Non performing Loans

A full and transparent recording of the cost of bank restructuring is important. While the initial support by the central banks was not very transparent, bringing the outlays into the budget would imply more transparency. All of the crisis countries have incorporated into their budgets the interest payments on the governments' recapitalization bonds. However, the cost of earlier liquidity support and the capital cost of government bonds have not yet been accounted for in the budgets. Incorporating the total restructuring costs into the budget is crucial, not only to have a clear overview of the total cost, but also to be in a position to better assess the countries' medium-term fiscal sustainability. This can be achieved through the use of an augmented fiscal balance that would explicitly incorporate all major quantifiable fiscal costs of bank assistance operations (Box 11). For financial programming purposes, however, the carrying costs of financial sector restructuring is a more appropriate concept.

The Augmented Fiscal Balance

The concept of augmented fiscal balance would explicitly incorporate the major quantifiable fiscal costs of bank assistance operations that are not included in the current definitions of the overall balance.[1] The augmented balance is not intended to replace the overall balance, but to present an additional measure of the fiscal stance for countries where bank assistance operations are important. Use of the augmented balance would allow a transparent, comprehensive, and reasonably comparable presentation of government financial assistance for bank restructuring across countries. If not using an augmented balance framework, complete details of the capital cost of bank restructuring operations should be recorded separately, regardless of whether they are budgetary or quasi-fiscal costs.

Institutional Constraints

Restructuring a banking system following a systemic crisis of the magnitude experienced in Asian countries is a complex process that goes far beyond purely technical operations. Restructuring strategies have to take into account local business practices, the availability of human resources, the deficiencies in the legal and judiciary framework, and depend largely on the degree of political support. In the three crisis countries, the changeover in the political regime had a clear positive impact on the pace of restructuring. Full recognition by the new governments of the magnitude of the crisis not only increased their resolve to implement the restructuring strategy, but also made it easier to gather broad-based support for the restructuring.[59]

Bank restructuring requires a large number of people with a wide variety of skills. Countries seldom have such resources readily available because crises are only sporadic occurrences. Governments often had to rely on outside expertise to help develop their strategy and carry out specialized tasks. In addition, the number of people needed was considerable. For instance, approximately 5,000 people (foreign and local experts, officials from different agencies, and security forces) were involved in the final closing of the 56 finance companies in Thailand. Similar numbers were involved in such operations in Indonesia.

Deficiencies in national legal and judicial frameworks have been major obstacles to the restructuring process in the crisis countries. Key issues include the initial lack of proper and tested exit policies for banks (especially insufficient authority to take early action against weak banks and to eliminate shareholders); the lack of legal protection of officials (the absence of immunity from prosecution and civil suits of officials in the exercise of their duties is still a major problem in the Philippines and Thailand); the inadequacy of foreclosure procedures and bankruptcy laws and an appropriate judicial infrastructure to deal with the massive corporate debt restructuring problem; a legal framework that often favored debtors over creditors; and the slowness and inexperience of the courts. Once deficiencies were recognized, it took a considerable amount of time before laws could be changed, and parliaments sometimes introduced counterproductive amendments, further delaying the process.

Linkages to Corporate Sector Restructuring

The severity of the corporate sector crisis in the three crisis countries has affected bank restructuring more than in most other bank crises. In most crisis countries, corporate sector restructuring began slowly and is lagging behind bank restructuring. This stems from the fact that the loss recognition process took longer, legal frameworks for addressing the issues were not or only partially in place, additional skills were needed that were not readily available, and the sector itself is more complex and diversified than the banking sector. Most important, unlike the banking sector, the private, corporate sector is not under the control of one single regulatory and supervisory agency. Moreover, corporate debt restructuring (the part that has a direct bearing on bank restructuring) largely depends on a broader business restructuring, which is usually a slow process. To the extent that corporate restructuring continues to lag behind, bank restructuring might be delayed. Generally, the two processes should proceed as simultaneously as possible, although bank restructuring should take the lead. This is so, not only because it is more feasible because banks are fewer and are already subject to an established supervisory regime, but also because it is necessary to have functioning financial institutions as counterparties to facilitate the corporate restructuring. Several initiatives have been taken to expedite corporate sector restructuring (Box 12.).

Box 12.

Linkage to Corporate Restructuring

Corporate restructuring is lagging behind bank restructuring, and has been hampered by a lack of leverage of most banks vis-à-vis their borrowers. The countries generally lacked frameworks for restructuring failing borrowers, such as coordinating credit committees under the guidance of a lead bank. Moreover, in many countries, the courts have tended to be lenient and provided little support for creditors, at least in the initial stages. Companies have been able to continue to operate under the court's protection, allowing interest to be deferred. This has undermined credit discipline. In some countries, measures have been taken to address this problem: first, through strengthened bankruptcy and foreclosure procedures to lessen the balance in favor of the borrowers, and second, by providing incentives and mechanisms for banks and corporate clients to restructure before reaching the courts. Initiatives also have been taken to improve court procedures.

The speed at which corporate restructuring takes place depends on a variety of factors, including the legal and regulatory framework at the onset of the crisis, the vigor of its enforcement, the structure of the corporate sector, and the nationality of the creditors. Corporate restructuring in Indonesia has so far been slow because new bankruptcy and foreclosure laws have not been enforced, in particular by the state-owned institutions. Korea is more advanced than the others because it adopted new laws fairly rapidly, has a corporate sector concentrated around the chaebols, and has clearly specified its restructuring objectives and provided strong leadership. The legal framework is strongest in Malaysia. Thailand suffered from delays in adopting a new legal framework for bankruptcy and disclosure.

Countries have given a variety of incentives to banks to address and expedite corporate debt restructuring. The "London Approach," which provides a framework whereby creditors would jointly approach the debtor and work out a mutually beneficial (out-of-court) arrangement, has so far been used most aggressively for government-led restructuring in Korea, where a number of medium-sized corporate groups have been dealt with in this way (debt rescheduling with some interest rate reduction, or issuance of convertible bonds and debt/equity swaps). In Thailand, the Corporate Debt Restructuring Advisory Committee (CDRAC) was formed by the Bank of Thailand and representatives from debtor and creditor groups, which agreed upon a framework for corporate debt restructuring based on the London Approach (the "Bangkok Approach"). The CDRAC initially targeted large debt restructuring cases but has recently expanded its coverage to small- and medium-size cases. A scheme that would combine government support for recapitalization with corporate debt settlement (Tier 2 options) has also been in place to encourage corporate debt restructuring. In Indonesia, the government has adopted a four-way classification of delinquent borrowers, based on their degree of cooperation with the workout process and business prospects. The state institutions and Indonesian Bank Restructuring Agency (IBRA) are adopting a coordinated approach vis-àa-vis each major delinquent borrower, beginning with the largest, broadly along the lines of the London Approach (the "Jakarta Initiative"). In Malaysia, the asset management company (Danaharta) has been given very extensive powers in dealing with the borrowers of any loans it buys. These powers seem to have had a significant effect on borrowers, because banks threatened to sell to Danaharta if the borrower failed to resume servicing the debt.

The banking system provides a key lever for corporate restructuring, in particular as regards corporate debt. Tightening and stronger enforcement of prudential regulations can make a major contribution. For instance, in Korea, tighter regulations on maximum exposure limits, connected lending, liquidity mismatches, and cross guarantees have required corporations to seek other sources of finance or shrink their balance sheets. Also, Korean banks—following strong government leadership—have been instrumental in approving and monitoring corporate restructuring plans. International financial institutions, particularly the World Bank, have strongly supported this process, including the banks' heavy involvement as key counterparts.

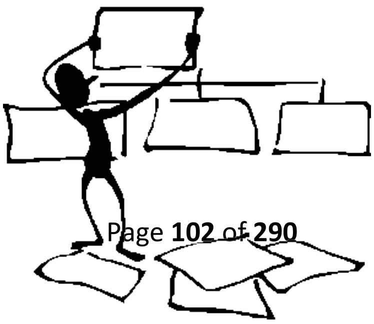
Banks are Restructuring Troubled Loans

- Other Category: Banking / Financing

- December 16, 2015
- Dan
- banks, loans, restructuring

With oil prices the lowest they've ever been in recent memory, business owners and financial analysts are predicting either an economic downturn, or possibly another recession in oil producing states. Bad news for oil and gas companies? Maybe not… Recently, I spoke with several Houston area bankers and learned that there seems to be a general focus on how banks are restructuring troubled loans in the oil and gas industry rather than forcing these companies into a workout situation as in previous downturns. This particularly applies to those companies who were more financially fragile going into the crisis back in July 2014.

Banks are Restructuring Troubled Loans



According to a recent Wall Street Journal article, some analysts and investors say, "The time of reckoning has been pushed back several months as banks prove reluctant to turn off the taps." Despite being in the 15th month since the peak of oil prices in July 2014, banks "have kept flowing, helping the [oil and gas] industry weather the market's collapse."
If you're in any oil producing state or country, you've probably already felt the pinch. Unfortunately for some, the price of oil is predicted to stay at $40 for the next 9-21 months, extending the "crisis" to 24-36 months.
One of the questions that we're dealing with today is to what extent this crisis will spill over to other markets. Companies adjacent to the oil and gas industry will likely be feeling the pain in the near future. The good news is that banks aren't pressuring companies outside of the oil and gas industry to restructure their loans just yet.

(Questions that your banker wants to know the answers to… Click here to read more about it)

What Can I Do Now?

The key is DON'T PANIC! There are steps you can take, so it's time to put on your thinking cap and be the trusted advisor your organization needs.

[box](**NOTE: Want more tips on how you can be a trusted advisor?** Check out our whitepaper How to be a Wingman!)[/box]

Sit back and look at your company as a whole in the market. By taking a wide view, you'll be better able to see where the company is unnecessarily bleeding. Three things are key in protecting yourself in an unstable market:

- Be proactive
- Cut sooner and cut deeper
- Restructure

Be Proactive

If your company is on the "edge" of the oil and gas industry, be proactive! Since we're in the 15th month and are expecting it to last up to 36 months, it's vital that you start preparing now.
First, calculate the how long your company can lose money without running out of cash. If you haven't acted yet (especially if you're in the 5% closest to the oil and gas industry), you'll most likely discover that you'll run out of cash before this crisis is projected to end.
Start analyzing how your market is functioning, how your company is operating, etc. List all of the operating functions that are not necessary or could be dramatically improved. Ask yourself: what are you spending the preciously small amount of cash that you have on?
The advantage of acting now is to prevent panic (i.e. cutting thousands of jobs, angering stock holders, breaking debt covenants, etc.). If you're trained, armed, and ready, then you have a much better chance of surviving this crisis than a company who walks on the battlefield completely unprepared.

Cut Sooner And Cut Deeper

Oftentimes in this twilight zone of a crisis, soft cuts are ideal because they don't hurt as much. This results in further cuts happening down the line when you find yourself scrambling to find a solution.
When we say "cut," we don't always mean cut people. Put on your thinking cap and re-engineer your company. Just because you've done things a certain way for 20 years doesn't mean it should stay that way for the next 20. Times change and so should your company.
Years ago, I had a client who was spending upwards of a quarter of a million dollars on advertising in Yellow Pages. He found himself in a pickle despite the fact that the market was ideal for his company. Even though it hurt, he cut his marketing from $250,000 to $50,000 and allocated the $200,000 to other more vital places within the company. Because of this reallocation of resources, he was able to save his employees and the company.
There are many ways to do more with less. More money spent does not always correlate to higher productivity or efficiency.
Reallocate your resources from the old company to the new.

Restructure

There are two sides to restructuring: either the bank restructures the loan or the company restructures its operations. In simple terms, restructuring is when significant changes are made in the operations, structure, or debt of a company to avoid financial harm and improve the business. This should provide greater efficiency, if done correctly. The strength of your operations can either cause your ship to sink, or deliver you safely to the shore. Managing your cash flow is of the utmost importance. Prioritize what is necessary to continue operations. Analyze what can be and needs to be cut. Improve productivity. Project your cash flows. Manage your cash flows from there. Debt restructuring essentially provides two options: continue operations or liquidate. If you are able to maintain and increase cash flow while reducing expenses, then continue operations. The goal is to at least break even. Ultimately, the company needs to make a decision about when to jump ship. If after researching and analyzing operations, structure, and debt you find that you cannot make $1 profit, then the best case scenario would be to liquidate.

(Be mindful of Expense Restructuring when restructuring your company.)

It's not every day that you're given the opportunity to restructure your company to have higher productivity and higher efficiency, thereby a higher net income. Be proactive, make the necessary cuts now, and live to fight another day.

Case Study: Shilpa Bank:

Report on Bangladesh Shilpa Bank

Report

Introduction:

Bangladesh Shilpa Bank (BSB) established under the Bangladesh Shilpa Bank Order 1972 (Presidential Order No. 129 of 1972) on 31 October 1972, to provide credit facilities and equity support to industrial enterprises in Bangladesh. It is the prime development financing institution

(DFI) in the country for extending financial assistance for industrialisation. Initially, the authorised capital of the bank was Tk 1,000 million in 1972 and the paid up capital was then Tk 750 million, which was subscribed by the government of the People's Republic of Bangladesh. Later, the authorised and paid up capital was enhanced. In 2000, the authorised capital was Tk 2,000 million divided into 2 million shares of Tk 1,000 each. Tk 1,320 million (66%) was subscribed and paid up by the government while the rest were left for subscription by Bangladeshi nationals or by financial institutions at home and abroad.

Bangladesh Shilpa Bank

The bank created a reserve fund of Tk 7 million in its first year of operations. In 1999-2000, the total reserve fund and other reserves of the bank stood at Tk 392.36 million. In 1982, the bank created a special equity fund titled 'Quasi Equity' by converting the 3rd, 5th, 6th and 8th UK credits received by it immediately after independence in 1971. The prime objective of the bank is to accelerate industrial growth in the country by financing industries, by providing advisory services in setting up new projects, and by assisting in balancing, modernisation, replacement and expansion (BMRE) of existing industrial units.

The Bank provides long and medium-term loans both in local and foreign currencies, guarantees repayment of loans raised by investors from other sources, and provides equity support by way of outright purchase of shares and by underwriting the public issue of shares. It also extends short-term bridge financing and working capital loans on a limited scale. BSB provides free technical advice in respect of plant and machinery, product and process, raw materials, market for products, and other related aspects to prospective entrepreneurs. It prepares project profiles for private entrepreneurs. All industrial projects either in the public sector or in the private sector are eligible for financial assistance from the bank. It follows a policy of diversifying its lending portfolio for widespread geographical dispersal of industrial enterprises, especially in less-developed areas of the country. With the view to bringing more dynamism and diversity in its activities, BSB started full-fledged commercial banking in 1993-94. This enables bank-financed projects to obtain commercial banking services including working capital loans, import of raw materials, etc.

On 31 December 2000, the total deposits of the bank were Tk 725.67 million comprising deposits received from banks (Tk 154.67 million), current account (Tk 72.24 million), bills payable (Tk 3.34 million), savings bank accounts (Tk 130.54 million), fixed deposits (Tk 267.01 million), and other deposits (Tk 97.87 million). Rates of interests offered by BSB on different deposit accounts varied between 7.75% and 9.75%, depending upon the duration of deposits. Lending rates of the bank varied between 10% and 18%. Up to end 1999, the bank financed a total of 1,573 industrial projects. The amount loaned to them was Tk 27,342 million. Total loans and advances of the bank (after provision for bad and doubtful debts) were Tk 7,136.26 million in 1999-2000. The distribution of the loans and advances by types were cash credit (Tk 1,121.96 million), long-term loans (Tk 19,242.87 million), overdraft (Tk 140.73 million), bridge loan (Tk 282.11 million), and staff loans (Tk 533.89 million). At the end of 2000, the cumulative amount of the bank's non-performing stuck-up loans stood at Tk 14,195.30 million, and were classified duly as substandard, doubtful, and bad, under the loans classification rules of bangladesh bank.

Shilpa Bank borrowed an amount of Tk 8,604.48 million during 1999-2000 from various internal and external sources. This includes F C Borrowing Accounts (Tk 360.32 million), BSCIC (Tk 3.94 million), Saudi Grant (Tk 11.80 million), KFW Counterpart Fund (Tk 165.93 million), Long-term loan from Bangladesh Bank (Tk 6405.57 million), KFW Loan (Tk 15.38 million), Danish

Credit Counterpart Fund (Tk 7.49 million), and overdue installment interest and exchange risk A/C (Tk 1,634.04 million).

The foreign exchange business handled by Shilpa Bank in 1997-98 was Tk 479 million, but dropped to Tk 25 million in the next year. This business covers export servicing, import financing, and remittance facilities. In 2001, the bank had correspondent relationships with 35 foreign banks and other financial institutions. In June 2000, the BSB investments other than lending stood at Tk 1289.54 million and its investment portfolio comprised short and long term treasury bills and bonds, prize bonds, shares and debentures and equity investments in industrial units. Total assets of the bank were valued at Tk 24,002.90 million in June 2000.

The bank demonstrated a deteriorating trend in profitability since 1994. The cumulative loss of the bank stood at Tk 3,285.60 million in 2000. The main reason for losses is the huge amount of non-performing stuck-up loans for which the bank has to maintain large amount of provision from its profit each year. Borrowed funds constitute a major source of the bank's lending assets and posting of accrued interest in interest suspense account has lowered its net interest income.

The management of the bank is vested in a 9-member board of directors, including the chairman and the managing director appointed by the government. However, there is a provision that non-government shareholders of the bank shall elect 4 directors from amongst themselves. But till now, there is no private subscription in the bank's capital, and all directors are appointed by the government. The managing director is the chief executive officer. The bank has 16 branches. The total number of employees in the bank is 997. The head office of the bank is at dhaka and it has 3 zonal offices, one each at chittagong, rajshahi and khulna. It has six divisions and 23 departments.

The Shareholders of Bangladesh Shilpa Bank

We have audited the accompanying Balance Sheet of Bangladesh Shilpa Bank as of 30 June, 2004 and the related Profit and Loss Account, Cash Flow Statement, Statement of Changes in Equity, Statement of Liquidity and notes to the financial statements for the year then ended. These financial statements are the responsibility of the management of the Bank. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with Bangladesh Standards on Auditing. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatements. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management as well as evaluating the overall financial statements presentation. We believe that our audit provides a reasonable basis for our opinion.

Our audit revealed the following:

i) BSB had made an investment of Tk. 10,000,000 in 100,000 Ordinary Shares @ Tk. 100 each of M/s. Sreepur Textile Mills Ltd. during the year 1993-94. But BSB did not receive any return on such investment till date. The market value of shares of the company has come down to Tk. 12.50 per share (on 28 October 2004). The bank has in turn lost Tk. 8,750,000 (100,000 x Tk. 100- Tk. 12.50) on this investment. But necessary provision has not been made in the accounts.

ii) In line with the requirement of Bangladesh Accounting Standard (BAS)-10; events after the Balance Sheet date necessary provision has not been made against classified loan account and classified equity investment held with M/s. Sreepur Textile Mills Ltd. As per Order of the Honorable 6th District Judge Court the said loanee was treated as unclassified till 30-06-04. But subsequently the order was suspended by the court on 27-09-04. As a result, the total loan of Tk. 29,776,738 should be provided for in the accounts for the period ended 30 June 2004.

iii) Specific provision amounting to Tk. 4,401,871 due to diminution of market value of Shares of various companies has not been made in the accounts.

iv) Provision has not been made against interest accrued on debenture amounting to Tk. 58,000,508 and these amounts appeared to us not realizable.

v) As per BSB book of accounts balance with Bangladesh Bank held by DCBO (Dhaka Commercial Branch Office) as on 30-06-04 amounted to Tk. 68,151,173. Bangladesh Bank confirmed a balance of Tk. 78,431,006. The difference of Tk. 10,279,833 remained unrecognized till the date of our audit.

vi) Other assets of the Bank include Inter Office Adjustment Account Tk. 104,233,782 as on 30-06-04. The said amount could not be reconciled by the bank till the date of our audit. As a result, we could not confirm inter office adjustment account.

vii) Fixed assets include a number of damaged items for which no accounting adjustment has been made regarding deletion of such item from the books of accounts.

viii) Requirement of Section 35 of the Bank Company Act 1991 in respect of transfer of unclaimed amount to inoperative accounts to Bangladesh Bank were not complied with.

In our opinion, if the adjustments relating to (i), (ii) and (iv) are reflected in the accompanying financial statements, the net profit shown in the profit and loss account will be reduced by Tk.100,919,117. Except for the above, the financial statements give a true and fair view of the financial position of the Bank as of 30 June, 2004 and of the results of its operations and its cash flows for the year then ended and comply with the Bank Companies Act 1991, the rules and regulations issued by Bangladesh Bank and the Security Exchange Rules 1987 and the other applicable laws and regulations.

We, except for the matters as mentioned above further report that:

(i) we have obtained all the information and explanations which to the best of our knowledge and belief were necessary for the purpose of our audit and made due verification thereof; (ii) in our opinion, proper books of accounts as required by law have been kept by the Bank so far as it appeared from our examination of those books and proper returns adequate for the purpose of our audit have been received from branches not visited by us;

(iii) the Bank's Balance Sheet and Profit and Loss Account dealt with by the report are in agreement with the books of accounts and returns;

(iv) The financial statements have been drawn-up in conformity with the Bank Company Act, 1991 and in accordance with the applicable rules and regulations issued by the Bangladesh Bank;

(v) adequate provision has been made for advances which are, in our opinion, doubtful of recovery;

(vi) the records and statements submitted by the branches have been properly maintained and consolidated in the financial statements;

(vii) the financial statements conform to the prescribed standards set in the accounting regulations issued by the Bangladesh Bank;

(viii) the information and explanations required by us have been received and found satisfactory;

(ix) we were not aware of any other matters which are required to be brought to the notice of the shareholders.

Most listed banks see rise in profits

In 2020 most of the commercial banks in Bangladesh shoed good profits.Low provisioning was the main driver

Most of the listed banks logged higher profits in the first nine months of 2020 despite a lower net interest income amid the business slowdown caused by the coronavirus pandemic.

Lower provisioning was the main driver behind the higher profits.

All the 30 banks listed with the Dhaka Stock Exchange declared their third quarterly earnings. The financial report of 27 lenders is available on their website.

Eighteen out of the 27 posted a year-on-year rise in profits during the January to September period. They logged 3.49 per cent higher profits of Tk 4,888 crore in the nine months.

Their combined net interest income, the biggest source of revenue, dropped 25 per cent to Tk 10,301 crore thanks to two steps introduced by the central bank -- 9 per cent interest cap in April and a payment holiday after the Covid-19 outbreak.

Provisioning of the listed banks also dipped 47 per cent year-on-year to Tk 2,009 crore.

"The banking sector witnessed higher income because of the policy support on provisioning from the central bank," said Md Abdul Halim Chowdhury, managing director of Pubali Bank.

"The stock market was also vibrant this year, so many banks did not need to keep provision. This ultimately boosted the profits of the banking sector," he added.

On March 19, after the country was struck with the pandemic, the banking regulator asked lenders not to consider businesspeople as defaulters if they fail to repay instalments until June 30.

As the crisis prolonged, the deadline was extended initially to September 30 and then to December this year.

Banks usually keep aside 0.5 per cent to 100 per cent in provisioning. They keep lower provisioning for regular loans but 20 to 100 per cent for default loans.

As the central bank has granted the payment holiday, banks are not compelled to set aside funds to cover future losses although new lending has not come to a halt and there is also non-payment of instalments.

"Banks should be more careful in booking profit this year and paying dividends because if they disburse dividend on unearned profits, they will be in trouble next year," said Syed Mahbubur Rahman, managing director of Mutual Trust Bank.

As the banks' profit rose riding on the lower provisioning and despite experiencing a reduction in the net interest income, they can announce dividend but it should not be much higher, he said.

"We don't know what the real scenario will be next year. Many companies are exporting products now but they might not receive the payment on time due to the Covid-19. Some good companies may even shut operations."

Rahman said keeping an average provision is safe.

"A number of loans might be classified or turn bad next year. So, we should be prepared for that. If banks keep adequate provision. it will boost their books as well."

A managing director of another bank said the profit situation of the banking sector is not the real picture and it would not sustain.

"The main shock would be clear next year when they will need to classify doubtful loans and subsequently keep higher provisioning," the top official said.

The loans that were recouped in the last few months were small loans whereas big loans have largely remained unrealized, he said. "The problem would exacerbate in the upcoming year."

The managing director urged the central bank not to allow banks to give higher cash dividends based on the "artificial profits".

Institutional investors always look for good stocks and prefer to invest in the banks that keep provisioning, said Ershad Hossain, CEO of City Bank Capital, a subsidiary merchant bank of City Bank.

"If banks don't keep the provision, they will face an enormous challenge next year because they will witness a rise in non-performing loans when the loan moratorium is lifted," Hossain said.

"How would they then manage the situation?"

Deposit collection by the listed banks fell about 17 per cent to Tk 677,873 crore at the end of September compared to December. Lending dipped 20 per cent to Tk 606,028 crore.

Trust Bank has the highest annualised return on equity of 21.1 per cent, followed by Jamuna Bank's 16.9 per cent and Dutch-Bangla Bank's 16 per cent, data showed.

Islami Bank Bangladesh posted the highest net profit of Tk 369 crore. Dutch-Bangla Bank took home Tk 345 crore and City Bank Tk 308 crore in the first nine months of the year.

City Bank had the highest year-to-date loan growth of 20.1 per cent, followed by Exim Bank's 12.4 per cent and First Security Islami Bank's 10.8 per cent.

State-run Rupali Bank registered the highest deposit growth of 17.5 per cent, followed by Dutch-Bangla Bank's 15.7 per cent and Islami Bank's 15.6 per cent.

How banks made millions from volatile dollar in 2022-23.

How does Bangladesh Bank affect the economy of Bangladesh?

Bangladesh Bank maintains the foreign exchange reserve of the country in different currencies to minimize the risk emerging from widespread fluctuation in exchange rate of major currencies and very irregular movement in interest rates in the global money market. Regulators of the Financial System

Central Bank

Bangladesh Bank acts as the Central Bank of Bangladesh which was established on December 16, 1971 through the enactment of Bangladesh Bank Order 1972- President's Order No. 127 of 1972 (Amended in 2003).
The general superintendence and direction of the affairs and business of BB have been entrusted to a 9 members' Board of Directors which is headed by the Governor who is the Chief Executive Officer of this institution as well. BB has 45 departments and 10 branch offices.
In Strategic Plan (2010-2014), the vision of BB has been stated as, "To develop continually as a forward looking central bank with competent and committed professionals of high ethical standards, conducting monetary management and financial sector supervision to maintain price stability and financial system robustness, supporting rapid broad based inclusive economic growth, employment generation and poverty eradication in Bangladesh".
The main functions of BB are (Section 7A of BB Order, 1972) -

1. to formulate and implement monetary policy;
2. to formulate and implement intervention policies in the foreign exchange market;
3. to give advice to the Government on the interaction of monetary policy with fiscal and exchange rate policy, on the impact of various policy measures on the economy and to propose legislative measures it considers necessary or appropriate to attain its objectives and perform its functions;
4. to hold and manage the official foreign reserves of Bangladesh;
5. to promote, regulate and ensure a secure and efficient payment system, including the issue of bank notes;
6. to regulate and supervise banking companies and financial institutions.

Core Policies of Central Bank

Monetary policy

The main objectives of monetary policy of Bangladesh Bank are:

1. Price stability both internal & external

2. Sustainable growth & development
3. High employment
4. Economic and efficient use of resources
5. Stability of financial & payment system

Bangladesh Bank declares the monetary policy by issuing Monetary Policy Statement (MPS) twice (January and July) in a year. The tools and instruments for implementation of monetary policy in Bangladesh are Bank Rate, Open Market Operations (OMO), Repurchase agreements (Repo) & Reverse Repo, Statutory Reserve Requirements (SLR & CRR).

Reserve Management Strategy

Bangladesh Bank maintains the foreign exchange reserve of the country in different currencies to minimize the risk emerging from widespread fluctuation in exchange rate of major currencies and very irregular movement in interest rates in the global money market. BB has established Nostro account arrangements with different Central Banks. Funds accumulated in these accounts are invested in Treasury bills, repos and other government papers in the respective currencies. It also makes investment in the form of short term deposits with different high rated and reputed commercial banks and purchase of high rated sovereign/supranational/corporate bonds. A separate department of BB performs the operational functions regarding investment which is guided by investment policy set by the BB's Investment Committee headed by a Deputy Governor. The underlying principle of the investment policy is to ensure the optimum return on investment with minimum market risk.

Interest Rate Policy

Under the Financial sector reform program, a flexible interest policy was formulated. According to that, banks are free to charge/fix their deposit (Bank /Financial Institutes) and Lending (Bank /Financial Institutes) rates other than Export Credit. At present, except Pre-shipment export credit and agricultural lending, there is no interest rate cap on lending for banks. Yet, banks can differentiate interest rate up to 3% considering comparative risk elements involved among borrowers in same lending category. With progressive deregulation of interest rates, banks have been advised to announce the mid-rate of the limit (if any) for different sectors and the banks may change interest 1.5% more or less than the announced mid-rate on the basis of the comparative credit risk. Banks upload their deposit and lending interest rate in their respective website.

Capital Adequacy for Banks and FIs

Basel-III has been introduced with a view to strengthening the capital base of banks with the goal of promoting a more resilient banking sector. The Basel III regulation will be adopted in a phased manner starting from the January 2015, with full implementation of capital ratios from the beginning of 2019. Now, scheduled banks in Bangladesh are required to maintain minimum capital of Taka 4 billion or Capital to Risk Weighted Assets Ratio (CRAR) 10%, whichever is higher. In addition to minimum CRAR, Capital Conservation Buffer (CCB) of 2.5% of the total RWA is being introduced which will be maintained in the form of CET1. Besides the minimum requirement all banks have a process for assessing overall capital adequacy in relation to their risk profile and a strategy for maintaining capital at an adequate level.

For FIs, full implementation of Basel-II has been started in January 01, 2012 (Prudential Guidelines on Capital Adequacy and Market Discipline (CAMD) for Financial Institutions). Now, FIs in Bangladesh are required to maintain Tk. 1 billion or 10% of Total Risk Weighted Assets as capital, whichever is higher.

Deposit Insurance

The deposit insurance scheme (DIS) was introduced in Bangladesh in August 1984 to act as a safety net for the depositors. All the scheduled banks Bangladesh are the member of this scheme Bank Deposit Insurance Act 2000. The purpose of DIS is to help to increase market discipline, reduce moral hazard in the financial sector and provide safety nets at the minimum cost to the public in the event of bank failure. A Deposit Insurance Trust Fund (DITF) has also been created for providing limited protection (not exceeding Taka 0.01 million) to a small depositor in case of winding up of any bank. The Board of Directors of BB is the Trustee Board for the DITF. BB has adopted a system of risk based deposit insurance premium rates applicable for all scheduled banks effective from January - June 2007. According to new instruction regarding premium rates, problem banks are required to pay 0.09 percent and private banks other than the problem banks and state owned commercial banks are required to pay 0.07 percent where the percent coverage of the deposits is taka one hundred thousand per depositor per bank. With this end in view, BB has already advised the banks for bringing DIS into the notice of the public through displaying the same in their display board.

Insurance Authority

Insurance Development and Regulatory Authority (IDRA) was instituted on January 26, 2011 as the regulator of insurance industry being empowered by Insurance Development and Regulatory Act, 2010 by replacing its predecessor, Chief Controller of Insurance. This institution is operated under Ministry of Finance and a 4 member executive body headed by Chairman is responsible for its general supervision and direction of business.
IDRA has been established to make the insurance industry as the premier financial service provider in the country by structuring on an efficient corporate environment, by securing embryonic aspiration of society and by penetrating deep into all segments for high economic growth. The mission of IDRA is to protect the interest of the policy holders and other stakeholders under insurance policy, supervise and regulate the insurance industry effectively, ensure orderly and systematic growth of the insurance industry and for matters connected therewith or incidental thereto.

Regulator of Capital Market Intermediaries

Securities and Exchange Commission (SEC) performs the functions to regulate the capital market intermediaries and issuance of capital and financial instruments by public limited companies. It was established on June 8, 1993 under the Securities and Exchange Commission Act, 1993. A 5 member commission headed by a Chairman has the overall responsibility to administer securities legislation and the Commission is attached to the Ministry of Finance.

The mission of SEC is to protect the interests of securities investors, to develop and maintain fair, transparent and efficient securities markets and to ensure proper issuance of securities and compliance with securities laws. The main functions of SEC are:

1. Regulating the business of the Stock Exchanges or any other securities market.

2. Registering and regulating the business of stock-brokers, sub-brokers, share transfer agents, merchant bankers and managers of issues, trustee of trust deeds, registrar of an issue, underwriters, portfolio managers, investment advisers and other intermediaries in the securities market.
3. Registering, monitoring and regulating of collective investment scheme including all forms of mutual funds.
4. Monitoring and regulating all authorized self regulatory organizations in the securities market.
5. Prohibiting fraudulent and unfair trade practices in any securities market.
6. Promoting investors' education and providing training for intermediaries of the securities market.
7. Prohibiting insider trading in securities.
8. Regulating the substantial acquisition of shares and take-over of companies.
9. Undertaking investigation and inspection, inquiries and audit of any issuer or dealer of securities, the Stock Exchanges and intermediaries and any self regulatory organization in the securities market.
10. Conducting research and publishing information.

Regulator of Micro Finance Institutions

To bring Non-government Microfinance Institutions (NGO-MFIs) under a regulatory framework, the Government of Bangladesh enacted "Microcredit Regulatory Authority Act, 2006'" (Act no. 32 of 2006) which came into effect from August 27, 2006. Under this Act, the Government established Microcredit Regulatory Authority (MRA) with a view to ensuring transparency and accountability of microcredit activities of the NGO-MFIs in the country. The Authority is empowered and responsible to implement the said act and to bring the microcredit sector of the country under a full-fledged regulatory framework.
MRA's mission is to ensure transparency and accountability of microfinance operations of NGO-MFIs as well as foster sustainable growth of this sector. In order to achieve its mission, MRA has set itself the task to attain the following goals:

1. To formulate as well as implement the policies to ensure good governance and transparent financial systems of MFIs.
2. To conduct in-depth research on critical microfinance issues and provide policy inputs to the government consistent with the national strategy for poverty eradication.
3. To provide training of NGO-MFIs and linking them with the broader financial market to facilitate sustainable resources and efficient management.
4. To assist the government to build up an inclusive financial market for economic development of the country.
5. To identify the priorities in the microfinance sector for policy guidance and dissemination of information to attain the MRA's social responsibility.

According to the Act, the MRA will be responsible for the three primary functions that will need to be carried out, namely:

1. Licensing of MFIs with explicit legal powers;
2. Supervision of MFIs to ensure that they continue to comply with the licensing requirements; and
3. Enforcement of sanctions in the event of any MFI failing to meet the licensing and ongoing supervisory requirements.

At a time when the entire country is grappling with rising dollar prices that put foreign exchange reserves under stress, some banks have made high profits from the volatile forex market, propelling the greenback to become dearer and making the inflation worse.

In the first half of the current year, banks generated income up to 400% from foreign exchange dealings, while their earnings from other sources, such as the share market and interests, declined.

Such huge profits have come at the cost of high inflation – as banks charge importers high, which eventually fueled soaring commodity prices in the local market.

High income from foreign exchange dealings helped banks show moderate profit growth in January-June of the current year, according to banks.

For instance, Brac Bank saw a 425% growth in foreign currency dealings in the first half of the current year.

The bank's income from foreign currency dealings surged to Tk93 crore in January-June from Tk17 crore in the same period of the previous year, according to the bank's financial statement.

However, its income from other sources declined, leading to a fall in earnings per share to Tk1.47 from Tk1.72 during the period.

Infographic: TBS

Likewise, Dutch-Bangla saw a 400% growth in income from foreign currency dealings in the period, causing a jump in its overall profit.

The bank's income from foreign currency dealings amounted to Tk146 crore in January-June, which was Tk29 crore in the same period last year. And, its earnings per share increased by 10% to Tk3.58, according to the bank.

AB Bank saw a 35% growth in its half-yearly profit, thanks to high income from foreign currency dealings. Its earnings from foreign currency dealings surged by 338% to Tk66 crore from Tk15 crore in the same time a year ago.

Islami Bank registered a 140% growth in income from foreign exchange dealings with a profit of Tk233 crore in January-June.

Rising dollar prices have brought in a good profit margin for banks, but most banks' overall profits did not rise as expected because of the interest rate cap and a fall in stock prices.

Federation of Bangladesh Chambers of Commerce and Industry (FBCCI) President Jasim Uddin recently claimed that banks were making a profit of Tk10 for every dollar they were selling.

The banks have been given a licence to do business, not to make such a high profit per dollar, he said.

"We cannot accept that banks will sell a dollar for Tk105-Tk110 after buying it from the central bank for Tk94," said the FBCCI president after paying a courtesy call on Bangladesh Bank Governor Abdur Rouf Talukder on Thursday.

He also claimed that many share traders have started trading in dollars.

Discarding his claim, Selim RF Hussain, managing director at Brac Bank, said it is completely wrong.

If banks could make such a huge profit per dollar, it would have come to the Bangladesh Bank's notice, he noted.

Explaining high income from foreign currency dealings, Selim RF Hussain said it is a normal trend – if foreign exchange market or local currency market remains volatile, profit margin of some organisations go up.

It is true that some banks made good profits from the volatile forex market but it was not true for all banks. The profit per dollar was not as high as the FBCCI president claimed, he also said.

If there is any unnatural profit growth, the Bangladesh Bank will look into it and take appropriate action, he pointed out.

The dollar price surged faster after the Russia-Ukraine conflict started in February this year. The inter-bank exchange rate, which was Tk85 at the beginning of the year, shot up to Tk94.7 this month as the Bangladesh Bank devalued taka faster amid a widening gap between kerb market and inter-bank rates.

However, banks were ignoring the inter-bank exchange rate by settling LCs at higher rates that went up to Tk105 this month.

The greenback soared to a record Tk112 at the kerb market on 25 July before coming down to Tk108 a day later. It was selling at TK110 on Thursday last. The taka was devalued by the central bank for the third time in a month on 24 July.

The Bangladesh Bank's continuous intervention through dollar sales put pressure on foreign exchange reserves, taking it to below $40 billion this month.

In May, the Bangladesh Bank issued a notice, asking exporters to encash their proceeds from the same banks through which they made shipment of goods.

The notice was issued amid the allegation that exporters were selling dollars at higher rates from their export proceeds, fueling volatility in the market.

The new instruction limited bargaining power of exporters in getting dollar prices from banks, but it had little impact on dollar prices in the market as banks were selling dollars to importers at higher prices, contributing to a surge in inflation.

Banks made their profits by purchasing dollars at lower prices from exporters and selling at higher prices to importers, say market insiders.

In May, the central bank and top bankers held a meeting agreeing to sell dollars at a similar rate for international trade to stop dollar price manipulation. But the decision was not implemented finally.

Bangladesh's private commercial banks (PCBs) saw their operating profit grow substantially in the just-concluded calendar year chiefly for lower cost of funds and private-sector- credit growth, sources say.

A rebound in foreign trade, covering export and import, from the previous year's corona depression also contributed to the banks' 'higher operating-profit growth' in the outgoing year, according to senior bankers.

Bangladesh's import expenses jumped by 53.74 per cent to US$30.32 billion during the July-November period of the current fiscal year (FY), 2021-22, from $19.72 billion in the same period of FY'21 while export earnings rose 24.29 per cent to $19.79 billion from $15.92 billion.

Actually, the country's foreign trade increased significantly in recent months thanks to a gradual pickup in economic activities, both domestic and global, amid reopening after more than one year due to the Covid-19 pandemic, they explained.

The FE collected unaudited operating-profit figures of 11 banks, out of a total of 41, including nine new PCBs, until going to press on Friday.

Of those banks, Islami Bank Bangladesh Ltd (IBBL) was the top profit-earner in the bygone year. Its earnings rose to Tk 24.30 billion in 2021 from Tk 23.50 billion a year before.

Pubali Bank Ltd stood second with Tk 11.40 billion in operating profit, up from Tk 9.35 billion in 2020.

Eastern Bank Ltd stood in the third position with an estimated earning of more than Tk 10.50 billion as operating profit in 2021 from Tk 8.70 billion in 2020.

EXIM Bank Ltd posted an operating profit worth Tk 7.80 billion in 2021 against Tk 7.41 billion a year ago, while the profit of Jamuna Bank Ltd rose to Tk 7.50 billion from Tk 6.37 billion.

Al-Arafah Islami Bank Ltd made an operating profit of Tk 7.50 billion in 2021 against Tk 6.80 billion of the previous year, while Shahjalal Islami Bank Ltd earned Tk 7.17 billion, up from Tk 4.81 billion in 2020.

NRBC Ltd booked an operating profit worth Tk 4.50 billion in 2021 against Tk 3.23 billion of the previous year, while the profit of Meghna Bank Ltd rose to Tk 1.05 billion from Tk 730 million.

The operating profit of South Bangla Agriculture and Commerce Bank rose to Tk 2.10 billion in the outgoing year from Tk 1.52 billion in 2020 while Midland Bank Ltd earned Tk 1.62 billion as operating profit from Tk 1.25 billion.

Some banks have yet to complete calculation of their annual accounts because the central bank Thursday relaxed further the loan-repayment policy for all the sectors to expedite the country's economic recovery from the fallout of Covid-19 pandemic.

"We're still working on the matter," a senior official at a PCB said while replying to a query.

He also said such policy relaxations have also helped improve the operational profit of the banks.

Under the policy relaxations, the banks are allowed to transfer interest earnings from such loans into their income accounts.

A senior executive of a leading PCB, however, says that the country's private-sector-credit growth maintained an upward trend in the recent months mainly due to higher trade financing for settling import-payment obligations.

The growth in the private-sector-credit flow rose to 10.11 per cent in November 2021 on a year-on-year basis from 9.44 per cent a month before. It was 8.21 per cent in November 2020.

The total outstanding loans with the private sector rose to Tk 12342.46 billion in November 2021 from Tk 12195.37 billion in the previous month. It was Tk 11209.02 in November 2020.

"Higher prices of essential commodities, including petroleum products, on the global market also pushed up the import- payments pressure on the economy in recent months," the private banker told the FE.

Meanwhile, the interest-rate spread increased in the outgoing year as the banks cut the deposit rates deeper than that of the lending ones, according to the bankers.

The weighted average spread between the lending and deposit rates widened to 3.99 per cent in November 2021 from 2.98 per cent a year before. It was 3.07 per cent in December 2020.

The weighted average interest rate on deposits fell to 3.99 per cent in November last from 4.64 per cent a year ago while the lending rate came down to 7.15 per cent from 7.62 per cent, according to Bangladesh Bank's (BB) latest statistics.

"Lower deposit rates have helped reduce the cost of funds that have pushed up our operational profits in 2021," said another executive of a PCB said while explaining the rising trend about their operating profits.

He also says the average cost of funds is now around 4.0 per cent which was nearly 5.0 in the previous year.

The operating profit, however, does not indicate the real financial health of a bank since the lenders have to make room for provisioning against the loans, particularly classified ones, and taxes that have to be paid to the government from the profits.

Operating profits of the banks and non-banking financial institutions are a major source of income tax of the National Board of Revenue (NBR).

As such, the aggregate operating profit of the PCBs has an impact on the revenue collection in thBig foreign banks in Bangladesh see profits take a hit

Large foreign banks operating in Bangladesh took a hit in 2021 as their profits plunged due to the impacts of the coronavirus pandemic and the lower interest rate regime.

Collective profits for the nine banks fell more than 33 per cent year-on-year to Tk 1,556 crore in 2021. It was Tk 2,336 crore in 2020, showed financial statements of the multinational lenders.

The interest income of five of the nine international banks went down owing to the ceiling on the lending and deposit rates and the moratorium announced by the central bank to give a cushion to businesses pummeled by the countrywide lockdowns and depressed demand.

The banks have been ordered to keep the deposit rate within 6 per cent and the lending rate at 9 per cent since April 1 of 2020 as the government looks to ensure a single-digit interest rate. The cap drastically brought down the interest income for almost all banks in Bangladesh.

The local operations of Standard Chartered, which is headquartered in London, logged profits of Tk 758 crore last year, down 44.5 per cent compared to 2020, when it raked in Tk 1,367 crore, according to its financial statements.

HSBC Bangladesh, another British bank, was also almost in the same situation. Its profits declined 30 per cent to Tk 378.36 crore in the recently concluded year.

Profits of Citibank NA, a US lender, plummeted 66.95 per cent to Tk 30 crore compared to the previous year's Tk 90.78 crore.

Sri Lanka's Commercial Bank of Ceylon, State Bank of India, Bank Alfalah of Pakistan, and the National Bank of Pakistan made higher profits in 2021.

Habib Bank, a Pakistani multinational bank, remained in the red.

Woori Bank witnessed 21 per cent lower profits of Tk 63.9 crore last year, against Tk 81 crore a year ago, according to the financial report of the Korean multinational lender. The net interest income dropped 6 per cent to Tk 55.9 crore.

"The decline in the profits of the foreign banks was not unexpected after such a devastating pandemic since the crisis has hurt almost all businesses," said Shah Md Ahsan Habib, a professor at the Bangladesh Institute of Bank Management.

Although the foreign banks were hit by the business slowdown, they have kept investing in technologies, he noted. "They will reap the benefit of the investment in the future."

In contrast, local banks showed higher profits and provided dividends in 2021, helped by the Bangladesh Bank's relaxed policy that allowed them to count income from unrealised instalments of loans.

"But this is not expected during a crisis," said Habib, adding that as many borrowers did not pay back their loans fully in the last two years, the net interest income of banks fell.

The BB allowed the borrowers to retain their loan status unchanged through the payment of a portion of the loans for two years.

The interest income of Standard Chartered Bangladesh was down 26 per cent to Tk 1,121 crore in 2021. The income from investment fell 31 per cent to Tk 338 crore mainly due to the drop in the interest earnings from government bonds and Treasury bills.

The income from the government bonds and Treasury bills declined to Tk 312 crore from Tk 439 crore a year earlier.

Standard Chartered Bangladesh cut the salary and allowances of its chief executive officer to Tk 4.38 crore from Tk 4.84 crore a year ago, the financial statements showed.

HSBC Bangladesh's net interest income dropped to Tk 766 crore, a fall of 8.24 per cent from Tk 835 crore in the previous year, according to the financial report.

Commissions, exchanges and brokerage charges fetched Tk 461 crore for the bank, up 12 per cent year-on-year, helped by higher earnings for the opening of letters of credits for imports.

The income from the opening of LCs stood at Tk 231 crore, a rise of 27 per cent.

The British lender managed to keep its operating costs almost unchanged: it was Tk 546 crore last year against Tk 544 crore in 2020.

HSBC Bangladesh's CEO saw a pay-cut of 23 per cent to Tk 4.33 crore.

In a statement, the bank says its underlying business was resilient and it is well-positioned for future growth.

"We saw good annual growth in overall assets and liability balances, and we maintained good profitability. We are also proud to have supported the people and businesses of Bangladesh during the pandemic."

Speaking about the fall in profit, the London-based lender said the pandemic impacted all banks and HSBC was no exception.

Standard Chartered Bangladesh says its profits were impacted by the lower income as well as higher loan impairment charges.

"The bank's income performance was adversely impacted by margin compression in both commercial and investment books due to the significant surplus liquidity in the market."

In a statement, the multinational lender says it booked higher impairment charges in 2021 to absorb any loan losses, which may arise post-payment moratorium.

The provisions held by the bank stand at 257 per cent of the required provisions as per Bangladesh Bank guidelines, and the provisions coverage ratio was 135 per cent of non-performing loans.

Despite the higher impairment charges, the bank's capital adequacy ratio remained strong at 23.4 per cent against the market average of 11.22 per cent in September.

"With its strong capital base and surplus liquidity, the bank is well-positioned to grow its business in 2022 and beyond," added Standard Chartered Bangladesh.

The National Bank of Pakistan returned to profits last year.

The profits stood at Tk 30.58 crore, compared to Tk 21.67 crore losses it incurred a year ago.

However, the Karachi-based state-run multinational commercial bank's net interest income was still in the red.

The net interest income was Tk 55 crore in the negative in 2021, an improvement from Tk 123 crore in the negative a year ago.

Six more banks asked to explain alleged unusual profit-making

Mostafizur Rahman | Published: 22:49, Sep 07,2022 | Updated: 18:04, Sep 08,2022

The Bangladesh Bank on Wednesday sought explanations from six more banks for alleged unusual profit-making by selling dollars for very high prices amid the ongoing foreign exchange market crisis.

The six banks are United Commercial Bank, Bank Asia, Dhaka Bank, Mercantile Bank, Islami Bank Bangladesh and HSBC Bank.

BB executive director and spokesperson Md Serajul Islam told New Age that the central bank issued the show-cause notice to the six banks on Wednesday.

He said that the banks were asked to explain their position for making unusual profits by selling dollars.

Earlier on August 17, the BB asked managing directors of six banks to explain allegation of making excessive profits from selling dollars at high rates.

The banks were Dutch-Bangla Bank, Southeast Bank, Prime Bank, City Bank, BRAC Bank and Standard Chartered Bank.

On August 8, the six banks had to remove heads of their treasury departments amid allegations of dollar price manipulation.

BB officials had said that the treasury chiefs held large amounts of dollars in order to raise the prices of the bank notes.

Banks' primary sources of foreign currency are export proceeds, remittances, foreign currency deposits and investments in various bonds.

According to central bank's regulations, there is a ceiling on the amount of foreign currency a bank can hold.

After July 15, no bank was allowed to hold foreign currency more than 15 per cent of its regulatory capital.

Previously, the rate was 20 per cent of a bank's regulatory capital that was reduced amid the current volatility on the foreign exchange market.

If banks get foreign currency above the ceiling, they have to sell the currency to other banks.

The exchange rate of the dollar shot up to Tk 119 on the open market, or kerb market, on August 10 amid a shortage of the currency on the financial market.

The interbank rate of the dollar was Tk 95 on Wednesday.

There are allegations that banks buy dollars from exporters at lower rates and sell those at much higher rates to importers to make huge profits.

The Bangladesh Bank has recently limited money exchange houses' dollar purchase-sale spread to Tk 1.5 after it set the difference at Tk 1 for banks.Due to the BB initiatives, the dollar price on the kerb market has reduced to Tk 110 recently.

BB's currency investment hits a profit of 29,247C

The central bank authorities have reportedly decided to give its officials a bonus equal to five months' basic salary

Bangladesh Bank has shown a huge profit in foreign currency revaluation. In FY22, the central bank made a profit of nearly Tk26,300 crore from foreign currency revaluation which pushed its total profit up to Tk29,247 crore.

It is more than five times higher than the Tk5,777 crore in FY21, according to the Bangladesh Bank annual report data for the last fiscal year.

However, Bangladesh Bank does not take the foreign currency revaluation profit as the bank's profit.

Data shows interest income from domestic currency has decreased as the government has taken less debt. Income has also decreased due to falling in bank rates and giving money to banks at low interest due to Covid-19.

As a result, the profit of Bangladesh Bank has decreased. In the last fiscal year, the net profit of Bangladesh Bank from local or domestic currency was Tk2,947 crore, which was Tk3,172 crore in FY21.

The central bank has recently finalized the annual report for FY22, which has already been approved by the board.

Based on this considerable profit, the central banker has reportedly decided to give its officials a bonus equal to five months' basic salary.

Regarding the matter, Bangladesh Bank Executive Director and Spokesperson Serajul Islam told to media that: “The Annual report was approved at the board meeting. It has been finalized by following international practice.”

Bangladesh Bank invests reserves in different countries and it also buys gold. So sometimes it increases the investment value and sometimes it may decrease.

“We know, if there is a surplus of dollars in the banks, Bangladesh Bank buys them, and if there is a crisis, it sells dollars from the reserve.”

Foreign currency revaluation profits

Due to the dollar crisis, it sold 762 million dollars from reserves in the last fiscal year.

On June 30, the central bank sold the dollar at the rate of Tk93.45 which is now Tk 95.

According to data, Bangladesh Bank has shown a profit of Tk26,300 crore in FY22 from the revaluation of foreign currency.

In the previous year, it had shown a profit of Tk 2,606 crore. In FY20 which was only Tk427 crore.

In FY19, the profit from foreign currency revaluation was Tk1,390 crore and in FY18 it was Tk 8,873 crore.

According to the annual reports, Bangladesh Bank's interest income from foreign currency increased to Tk2,837 crore in FY22, which was Tk2,544 crore in the previous fiscal year.

Profit from commission and bonus from foreign currency has increased to Tk52 crore, which was earlier Tk31 crore in FY21.

Operating Income Of Banks.

Operating Income refers to **the total amount of income generated by banks from its operations**, which measures the operational success of financial institutions. It is the sum of net interest income and non-interest income.

A number of commercial banks posted EBIT or operating profits in the adversity-fraught bygone year, in a significant growth amidst a series of loan-related scams in the country's banking system.

EBIT (Earnings Before Interest and Tax) or operating profits is one of the key indicators for measuring financial health of any institution.

Both public and private commercial banks saw their operating profit grow substantially in the just-concluded calendar year for lower cost of funds and private-sector- credit growth, sector insiders say.

The FE collected unaudited operating-profit figures of 12 banks, out of a total of 61, before the sun set for the year 2022.

Of the dozen, Rupali Bank Limited tops the list posting over 43-percent growth. Its earnings rose to Tk 2110 million in 2022 from Tk 1470 million a year before.

Union Bank stood second with a 25-percent growth as the private commercial bank earned operating profits amounting to Tk 4,500 million in the just-past year against Tk 3,600 million earned a year ago. Sonali Bank Limited becomes third-largest profit-earning bank recording Tk Tk 25,000 million in 2022 in a rise from Tk 20,900 million a year before. The growth is around 20 per cent.

Jamuna Bank Limited secured 18.57-percent growth in making operating profit of Tk 8,300 million in 2022 against Tk 7,000 million earned in the previous year.

Earning EBIT of Tk 8,450 million in 2022, Mercantile Bank Limited got positioned in the fifth position with a 17-percent growth. In 2021, the bank's operating profit was recorded Tk 7,220 million. Southeast Bank Limited managed to bag over 11-percent growth in the past calendar year with Tk 11,300 million earned as operating profit. In 2021, the figure was Tk 10,160 million.

Social Islami Bank Limited (SIBL) earned Tk 5,500 million as operating profits in 2022 and the figure jumped by Tk 500 million from the 2021 earnings.

Islami Bank Bangladesh Ltd (IBBL) registered unaudited profit worth Tk 26,460 million, up by around 9.0 per cent from the previous year's Tk 24,300 million.

Operating profits of Al-Arafah Islami Bank Limited increased by Tk 500 million to Tk 8,100 million in 2022 while NRBC's unaudited profit shot up by Tk 50 million to reach 4550 million in 2022.

However, South Bangla Agriculture and Commerce Bank Limited (SBAC) recorded negative growth as the bank's operating profit plummeted to Tk 2,000 million in 2022 compared with previous year's earnings of Tk 2100 million.

Some banks have yet to complete calculation of their annual accounts because the central bank recently relaxed the loan-repayment policy for all the sectors to expedite the country's economic recovery from the disruptions caused by the ongoing war in Europe.

"We're still working on the matter," a senior official at a PCB said in replying to a query.

He also said such policy relaxations also helped improve the operational profit of the banks.

Another top executive of another PCB said they cannot make much profit because of two factors - dollar appreciation amid the greenback shortfall and government belt-tightening measures. To meet foreign- currency obligation, he said, all the banks were forced to buy dollar at higher rates to clear import bills that ate up a portion of their profits while austerity measures to protect the reserves compelled them not to go for import.

However, he was very optimistic, saying that the unofficial withdrawal of lending-rate cap from the consumer's credits would help boost profitability of the banks in the days ahead.

Nonbank Financial Sector Vulnerabilities Surface as Financial Conditions Tighten

NBFIs have emerged as key players in the financial sector, and global financial stability could hinge on their resilience as policy is tightened to tackle high inflation

Antonio Garcia Pascual, Fabio Natalucci, Thomas Piontek

April 4, 2023

Recent strains at some banks in the United States and Europe are a powerful reminder of pockets of elevated financial vulnerabilities built over years of low rates, compressed volatility, and ample liquidity.

Such risks could intensify in coming months amid the continued tightening of monetary policy globally, making it especially important to understand and safeguard this broad swath of the financial sector that comprises an array of institutions beyond banks. Nonbank financial intermediaries, including pension funds, insurers, and hedge funds, also play a key role in the global financial system by providing financial services and credit and thus supporting economic growth.

The growth of the NBFI sector accelerated after the global financial crisis, accounting now for nearly 50 percent of global financial assets. As such, the smooth functioning of the nonbank sector is vital for financial stability.

However, NBFI vulnerabilities appear to have increased in the past decade. As we show in an analytical chapter of the latest Global Financial Stability Report, NBFI stress tends to emerge alongside *elevated leverage*, for example borrowing money to finance their investments or boost returns, or using financial instruments, like derivatives.

Stress is also brought on by *liquidity mismatches,* where an institution is unable to generate sufficient cash either through liquidation of assets, such as bonds or equities, or use of credit lines to satisfy investor redemption requests.

Finally, high levels of *interconnectedness* among NBFIs and with traditional banks can also become a crucial amplification channel of financial stress. Last year's UK pension fund and liability-driven investment strategies episode underscores the perilous interplay of leverage, liquidity risk, and interconnectedness. Concerns about the country's fiscal outlook led to a sharp rise in UK sovereign bond yields that, in turn, led to large losses in defined-benefit pension fund investments that borrowed against such collateral, causing margin and collateral calls. To meet these calls, pension funds were forced to sell government bonds, pushing their yields even higher.

It is useful to take a step back and look at the current environment in which NBFIs find themselves. With the fastest inflation in decades, and with price stability at the core of most central bank mandates, injecting central bank liquidity for financial stability purposes could complicate the fight against inflation. In a low-inflation environment, central banks can respond to financial stress by easing policy such as cutting interest rates or purchasing assets to restore market functioning.

Amid high inflation, however, challenging tradeoffs may emerge for central banks between fostering financial stability and achieving price stability during periods of stress that may threaten the health of the financial system.

Policymakers need appropriate tools to tackle turmoil in the NBFI sector that may adversely affect financial stability. Robust surveillance, regulation, and supervision are essential pre-requisites. Policymakers must also narrow or eliminate gaps in regulatory reporting of key data, including how much risk firms are taking with their borrowing or use of derivatives.

Policies are also needed to ensure NBFIs better manage risks, and this might be accomplished through timely and granular public data disclosures and governance requirements. These improvements in private sector risk management must be supported by appropriate prudential standards, including capital and liquidity requirements, alongside better resourced and stricter supervision.

This would help steer the business decisions of the NBFIs themselves away from excessive risk taking by removing both the incentive and opportunity to take on too much risk. It would also likely reduce the need for and frequency of central bank intervention to provide liquidity support during systemic stress events.

If central bank intervention is needed, they can consider three broad types of support:

- **Discretionary market-wide intervention** should be temporary and targeted to those NBFI segments posing risk to financial stability. The timing is also critical—a framework should be in place where data-driven metrics trigger a potential intervention, while policymakers ultimately retain the discretion to intervene.

- **Lender-of-last-resort intervention** should be available when a systemically important nonbank institution comes under stress. Such lending should be at the discretion of the central bank, at a higher interest rate, fully collateralized, and accompanied by greater supervisory oversight. A clear timeline should be established for restoring the NBFI's liquidity and return to market finance.

- **Access to standing lending facilities** could be granted to specific NBFI entities to reduce spillovers to the financial system, although the bar for such access should be very high to avoid moral hazard. Access should not be granted without the appropriate regulatory and supervisory regimes for the different types of NBFIs.

Clear communication is critical, so that liquidity support is not perceived to be working at cross-purposes with monetary policy. For example, purchasing assets to restore financial stability while continuing with quantitative tightening to bring inflation back to target may cloud intent and complicate communication. Announcements of central bank liquidity support should clearly explain the financial stability objectives, program parameters and timing.

At the same time, cooperation between domestic policy makers and international coordination between national authorities is essential. This helps better identify risks and manage crises. Specifically, internationally coordinated reforms can reduce the risks of cross-border spillovers, regulatory arbitrage, and market fragmentation.

Given the growing size and intermediation capacity of the NBFI sector globally, the development of the right toolbox for access to central bank liquidity, along with the appropriate guardrails limiting the need for its use, is a priority. The need to do so is all that much greater given that financial sector vulnerabilities could be poised to grow amid the continued tightening of monetary policy.

Challenges Faced by Banks and Non-Bank Financial Institutions in Bangladesh

Banks and Non-Bank Financial Institutions (NBFIs) are a portentous and integral part of financial management systems of a country – rich or poor, developed, developing and underdeveloped. Well-functiong Banks and NBFIs are a must for achieving the most desirable Sustainable Development Growth (SDG). They play a gargantual role in the economy of Bangladesh by accumulating the savings of the 165 million people in one hand and on the other hand invest the money in various economic activities – productive and unproductive finacing in industries, export-import services, public finacing, Small and Medium Enterprises (SMEs) financing and many more. Economic and financial sectors of the most of the countries of the world including Bangladesh, have been drastically sufferring from devastating COVID-19 Pandemic.In Bangladesh, financial sectors in general and Banks and NBFIs in particular, have been facing egregious hardship and challenges come from COVID-19 Pandemic, opprobrious world-wide financial and economic conditions, reduction of exports and imports, closure of businesses and industries, mis-management, intrution of corruption and on and on. This financial sector of Bangladesh is undergoing liquidity crunch owing to a number of demand and supply side factors. Alongside, governance issues within the banking and non-banking systems have contributed to high levels of non-performing loans (NPLs), resulting in lack of trust and confidence in this sector. The recent collapse of Peoples Leasing and Financial Services Limited due to ginormous fraud, misappropriation and misuse of its funds by the Company's management, has shattered the economic and financial images of NBFIs sector by depriving and denuding its deposit holders from their hard-earned money and lost peoples trust and confidence in NBFIs.

Challenges Arisen from Double-Standard Interest Policy

The Banks and NBFIs sectors are facing calamitous liquidity crisis of inadequate deposits due to the double standard policy that affected the investment in private and public sector as genuinely commented by financial experts and economists. The uniform lending and deposit rate or 9-6 policy hindered and stymied the deposit collection from the general depositors and eviscerate the financial stability and strength of Banks and NBFIs to a great extent. Implementation of government policy of uniform lending rate of 9% and deposit rate of 6% effective from 1st April 2020 had made it difficult and dicey to get deposits from deposit holders and created hypercritical liquidity crisis.

The Finance Ministry has triaged to the declining trend of interest rates in the financial markets, it lowered National Savings Certificates (NSCs) rates to 11.5 percent, which are still exceptionally higher than other deposit rates in the Banks and NBFIs sectors. Government borrows from the citizens of Bangladesh thorough NSCs. Currently, there are several NSC schemes such as: 5-year Bangladesh Sanchayapatra with an interest rate of 11.28 per cent, 3-monthly Profit Bearing Sanchayapatra with 11.04 per cent, Family Savings Certificate with 11.52 per cent interest for five years, and Pensioner Sanchayapatra with 11.76 per cent rate of interest. Due to uneven interest rate, i.e., higher-yielding NSCs, people will quickly and smartly rush to NSCs leaving Banks and NBFIs appalled. "Recently government has fixed the lending rate at 9% and deposit rate at 6% of Banking sector. This system of fixing lending and deposit rate of interest has created frustration among the management of Banks. Due to low deposit rate in Banks, general people are encouraged to invest in NSC" (Source: Prothom Alo dated 26/01/2021). The big difference in interest rates of NSCs and deposit interest rates of Banks and NBFIs severely affect investment environment in productive sectors of Bangladesh economy.

Table 4.6 Trends in Weighted Average Interest Rates of Scheduled Banks and their Spreads

Certificates (NSCs) rates to 11.5 percent, which are still exceptionally higher than other deposit rates in the Banks and NBFIs sectors. Government borrows from the citizens of Bangladesh thorough NSCs. Currently, there are several NSC schemes such as: 5-year Bangladesh Sanchayapatra with an interest rate of 11.28 per cent, 3-monthly Profit Bearing Sanchayapatra with 11.04 percent, Family Savings Certificate with 11.52 per cent interest for five years, and Pensioner Sanchayapatra with 11.76 percent rate of interest. Due to uneven interest rate, i.e.,higher-yielding NSCs, people will quickly and smartly rush to NSCs leaving Banks and NBFIs appalled. "Recently government has fixed the lending rate at 9% and deposit rate at 6% of Banking sector. This system of fixing lending and deposit rate of interest has created frustration among the management of Banks. Due to low deposit rate in Banks, general people are encouraged to invest in NSC" (Source: Prothom Alo dated 26/01/2021). The big difference in interest rates of NSCs and deposit interest rates of Banks and NBFIs severely affect investment environment in productive sectors of Bangladesh economy.

Challenges From COVID-19 Pandemic Devastating COVID-19 Pandemic inflicted 118.63 million people and took away 2.63 million lives as on 10th March 2021 in addition to severely affecting all sectors of economies of 208 countries world-wide. Financial sectors especially Banks and NBFIs sectors of Bangladesh are the worst sufferers. Government borrowing jumped to 79 percent in April 2020 from 44.60 percent in the previous month, according to BB data. In April, export and import fell drastically and businessmen were unable to make their payments for LC. Export earnings saw an unexpected 83 percent fall year-on-year in April when imports fell by 62 percent. "The image of the country's financial sector has been tarnished in the international arena as a good number of local banks have not made import payments on time. The number of allegations placed by foreign embassies in this regard has been rising as the respective overseas lenders failed to get their export earnings in due time, according to a Bangladesh Bank report." (Source: Daily Star 27/01/2021)

Non-Performing Loans are Threats to Banks and NBFIs Non-Performing Loans (NPLs) refers to those loans from which investing Banks and NBFIs fail to receive interest and to recover the principal as per schedule and reschedule. The NPLs are on the rise in Banks and NBFLs and has become an alarming and earth-shaking daily news in the media in Bangladesh. Bangladesh NPLs ratio stood at 8.9 % in September 2020, compared with the ratio of 9.2 % in the previous quarter. Financial experts consider 2% is the standard ratio for NPLs. BB has recently allowed Banks and NBFIs to extend loan payment schedule by rescheduling loans. As a result, the NPLs ratio is reduced but it may go up after expiry the rescheduled periods,as forecasted by the Banks and NBFIs.

"Hallmark Scam" of BDT 35,470m from Sonali Bank in 2012, embezzlement of BDT 45,000m from Basic Bank in 2013 and deceitfulness of Crescent and AnonTex of BDT 100,000m from Janata Bank in 2018, "Destiny Group Scam", "Bismillah Group scam" " Hallmark Group scam" and the recent collapse of Peoples Leasing and Financial Services Ltd. have instigated a question regarding the validity and legitimacy of credit assessment, credit supervision, board independence, management efficiency of the Banks and NBFIs, guiding, inspecting and supervising efficiency of BB. Besides, these scams are encouraging deliberate credit default behavior of borrowers. Consequently, banks face the pressure of liquidity risk, regulatory capital management risk and business risk. In addition, Banks and NBFIs are facing severe stress for their business, liquidity, investment, managerial efficiency and so on due to the substantial growth of NPLs. Economists and financial experts term NPLs as the "silent assassins'' of Banks and NBFIs. The NPLs topic is unquestionably the single most conundrum that the Banking and NBFIs sector of Bangladesh are brooking from. The NPL rate in Bangladesh is the second highest in Asia and 24th highest in the world. Back-to-back loans, squalid risk management,

Table 5.3(a) Ratio of Gross NPLs to Total Loans by Type of Banks

(in percent)

Bank types	2011	2012	2013	2014	2015	2016	2017	2018	2019	End June 2020
SCBs	11.3	23.9	19.8	22.2	21.5	25.0	26.5	30.0	23.9	22.7
SBs	24.6	26.8	26.8	32.8	23.2	26.0	23.4	19.5	15.1	15.9
PCBs	2.9	4.6	4.5	4.9	4.9	4.6	4.9	5.5	5.8	5.9
FCBs	3.0	3.5	5.5	7.3	7.8	9.6	7.0	6.5	5.7	5.5
Total	**6.1**	**10.0**	**8.9**	**9.7**	**8.8**	**9.2**	**9.3**	**10.3**	**9.3**	**9.2**

Source: BRPD, BB.

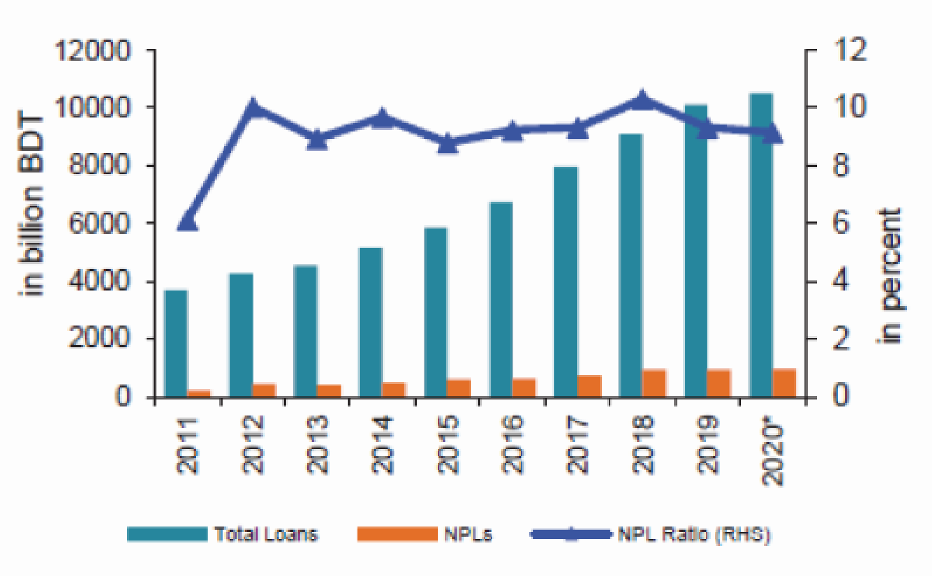
Table 5.3 (b) Ratio of Net NPL to Net Total Loans by Type of Banks

(in percent)

Bank types	2011	2012	2013	2014	2015	2016	2017	2018	2019	End June 2020
SCBs	-0.3	12.8	1.7	6.1	9.2	11.1	11.2	11.3	6.1	3.2
SBs	17.0	20.4	19.7	25.5	6.9	10.5	9.7	5.7	3.0	2.7
PCBs	0.2	0.9	0.6	0.8	0.6	0.1	0.2	0.4	-0.1	-0.5
FCBs	-1.8	-0.9	-0.4	-0.9	-0.2	1.9	0.7	0.7	0.2	-0.4
Total	**0.7**	**4.4**	**2.0**	**2.7**	**2.3**	**2.3**	**2.2**	**2.2**	**1.0**	**0.2**

Source: BRPD, BB.

Chart 5.4 Aggregate Position of NPLs to Total Loans



*Up to 30 June 2020
Source: BRPD, BB.

3.2 Total Money Lost through Major Scams, Irregularities, & Heists as reported in the media

Sonali, Janata, NCC, Mercantile & Dhaka Bank	BDT 4.89 crore
BASIC Bank	BDT 4,500 crore
Sonali Bank	BDT 3,547 crore
Janata Bank	BDT 10,000 crore
Janata Bank, Prime Bank, Jamuna Bank, Shahjalal Islami Bank & Premier Bank	BDT 1,174 crore
AB Bank	BDT 165 crore
NRB Commercial Bank	BDT 701 crore
Janata Bank	BDT 1,230 crore
The Farmers Bank	BDT 500 crore
Bangladesh Bank	BDT 679 crore
TOTAL	BDT 22,501 crore (USD 2.68 billion)

Note: As on 6th December 2018, 83.9 Taka per dollar (Bangladesh Bank).

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weak corporate governance and supervision, political pressure and malfeasance in sanctioning loans, weak legal and regulatory frameworks for recovering loans are considered to be the grander reasons for the rise of NPLs. If a recovery case is filed against a loan defaulter, it usually takes several years to resolve, exclusively for those involving large amounts. The most important indicator to demonstrate the asset quality is the ratio of gross Non-Performing Loans (NPLs) to total loans and net NPLs to net total loans. At the end of December 2019, the gross NPL ratio of the banking sector stood at 9.32 percent. Table 5.3(a) shows that FCBs had the lowest and SCBs had the highest gross NPL ratio. FCBs' gross NPL ratio was 5.74 percent, whereas those of SCBs, PCBs and SBs were 23.86, 5.78 and 15.13 percent respectively at the end of December 2019.

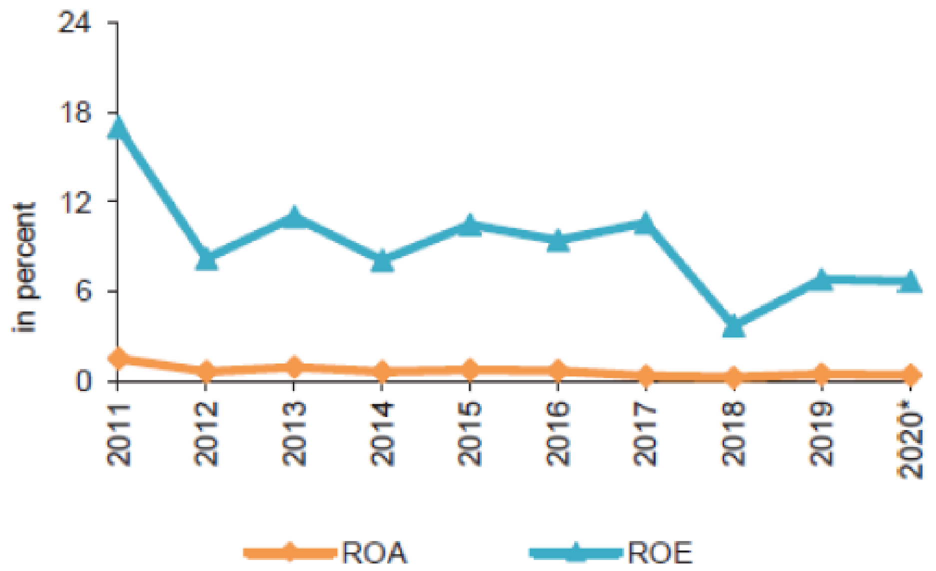
The banking and NBFIs sectors are now stuck in a quagmire of anguishes. All parameters of the banking sector indicate its obstinate fragility with no sign of revival on the horizon. The most discussed issue in the banking sector is the sky-rocketing non-performing loans (NPLs). In June 2019, the total volume of NPLs increased to BDT 112,430 crore which was 11.69 percent of total outstanding loans. Surprisingly, state-owned commercial banks had NPLs of over 30 percent of their total loans.

High Competition in Banking and NBFIs sector is a Big Challenge

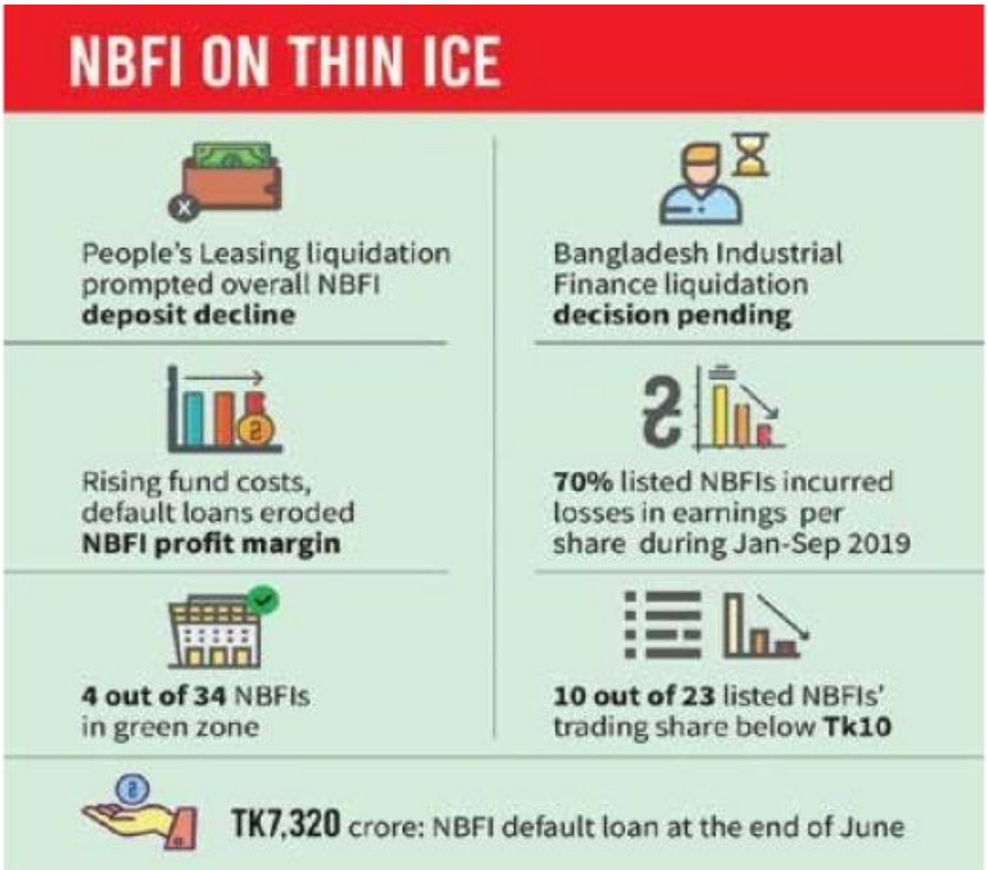
According to latest BB report, there are 61 scheduled banks – 6 state-owned commercial banks (SCBs), 3 specialized banks (SBs), 43 private commercial banks (PCBs) and 9 foreign commercial banks (FCBs). In addition, there are 5 non-scheduled banks and 34 NBFIs operating in Bangladesh. All are controlled, supervised and guided by BB. Generally, the rationale to open new banks and NBFIs depends on the size of the economy of a country, its GDP, purchasing power of the people, productivity, export, import, employment and many more economic conditions and it should not be personal or political reasons. Due to unplanned increase of Banks and NBFIs in Bangladesh, Banks and NBFIs face hard-hitting competition to attract and keep customers. To survive in the highly competitive financial sector, Banks and NBFIs have to incur more costs in different forms, their revenues are down that severally affect their profitability. Financial experts and economists are critical about the opening new banks considering the existing economic conditions of the country. The new bank is set to join the others at a time when the banking and financial sector is perforated with a number of loan scams and bad loans due to a lack of good governance and proper surveillance. “The existing banks were already struggling to survive amid the current situation over business activities. In addition, new banks seem reluctant to expand their business to rural areas as they mainly focus on urban areas” Ibrahim Khalid former Deputy Governor of BB said. (Source: Daily Star, 13/02/2021). The revenues and net-earnings of the Banks and NBFIs of Bangladesh are on decline due to various causes including over-number of Banks and NBFIs. Dividends on shares of Banks and NBFIs have down-surged that ultimately affected the stock market of Bangladesh

The cost associated with stiff competition and compliance management is just one of many banking industry challenges forcing financial institutions to change the way they do business. The swelling cost of capital combined with continued low interest rates, decreasing return on equity, and decreased proprietary trading are all putting excessive pressure on traditional sources of banking profitability. In spite of this, shareholder expectations remain unbothered.[M Jalal Hussain FCA

Chart 5.6 Trends in Aggregate Profitability in the Banking Industry



*Up to 30 June 2020
Source: DOS, BB.



Amaranthine Innovation and Technology is a Challenge

Technologies are changing, upgrading and advancing at supersonic speed in all businesses and so in Banks and NBFIs. Maintainable success in business requires vision, prowess, munificent clientele relationship, and continuous innovation and latest technology. Benchmarking effective practices throughout the industry can provide valuable insight, helping Banks and NBFIs stay viable. However, benchmarking alone only empowers institutions to keep up with the pack — it rarely leads to innovation. As the truism goes, businesses must benchmark to survive, and innovate to thrive; revolution is a vital differentiator that ruptures the wheat from the repartee. Innovation stems from phantasms, and visions are discovered through customer acquaintances and monophonic organizational analysis. Some FCBs and PCBs have advanced by applying the advanced technologies and are successful in attracting high value customers and doing good businesses than the Banks that are not well equipped with latest innovation and digital-technologies. However, Banks and NBFIs using antediluvian business management applications or siloed systems will be amateurish to keep up with this progressively digital-first world. Without a solid, forward-thinking technological foundation, Banks and NBFIs will miss out on critical and advanced business evolution. Digital renovation is not just an upright idea — it's become domineering for survival in the competitive and emulous financial sector.

Anemic and Impuissant Internal and External Controls in Banks and NBFIs

Banks and NBFIs have their own internal audit and compliance departments. In addition, they are audited and inspected by BB audit and inspection team, external auditors, credit rating agencies and auditors from Auditor General's office if they are State-owned Commercial Banks (SCBs).

Despite so many audit and inspections, the frauds and loan-scams remain undetected and unearthed, especially in case of scam involving huge amount for a long of period. This raises questions about the integrity, capability, creditability, accountability and effectiveness of the above stated internal and external audit and inspection teams and remains a big challenge for Bank and NBFIs. It was widely published in the local dailies as earth-shacking news that the audit and inspection team members of various agencies didn't disclose and hid the loan-scams and irregularities by taking bribe from concerned Banks and NBFIs. Due to weak, feeble and ineffective management, the corrupt officials remain unpunished and, in few cases, departmental disciplinary actions are taken by transferring the convict from one department to another department or from one branch to another branch. Lack of honest, sincere, ethical and integrated senior managers in Banks and NBFIs is a serious uncontrollable challenge. Defilement of corporate ethics and insider frauds have been termed as unfathomable risks for Banks and NBFIs. The Financial Stability Board (FSB) had submitted letter to the Finance Ministers and Central Bank Governors of G20 countries in 2019 commenting that "numerous instances of misconduct in the financial industry in recent years have damaged confidence in financial institutions and undermined trust in markets. The implications of misconduct can be far-reaching, limiting the potential of finance to serve real economies and to foster global economic growth"

Ways Forward Strong and effective internal and external audit and inspection systems are a must to control fraud and irregularities in Banks and NBFIs. Board of Directors of Banks and NBFIs and BB management may play an important role from sanctioning a loan to recovery of loan and punishing the corrupt and criminal managers and staff rigorously. Good governance in the banking and non-banking financial sectors is very much needed. Authorities may consider that SCBs, SBs and PCBs Boards of Directors be composed of competent, perspicacious and au courant professionals, instead of those appointed on political reasons alone. Management should allow full operational freedom in conducting banks' daily operations. Both the Board and management must be accountable to BB. BB should be allowed authority to ensure that individuals sitting on Boards possess operational knowledge of banking and finance. Promoting and introducing technology-driven and digital services and products in Banks and NBFIs may help address stiff competition and improve performances at national and global level.The legal systems dealing with Banks and NBFIs default loans like Artaho Rin Adalat Ain 20003 and Bankruptcy Act 1997 are very complicated and lengthy. It's observed that it took many years to settle a NPL case under the said laws. To stream line the Banks and NBFIs operation, the obstacles and barriers in recovering default loans need to be removed by amending the laws and creating more courts to handle NPLs. All NPLs are not deliberate. Some borrowers face business problems – less export due to lack of good buyers, heavy competition, lack of materials due to import restrictions and so on. Congenial invest-climate is needed for Banks and NBFIs Local investors need to be encouraged to invest more in industries and businesses by introducing favorable rules, regulations, laws, reducing the interest gap between investment in Banks, NBFIs and NSCs. Despite adopting various measures for smooth and dynamic operation of Banks and NBFIs, many challenges remained unresolved. It's thus important to look at other countries' planning, measures and experiences in dealing with excessive NPLs, frauds and irregularities and adopt in Bangladeshi Banks and NBFIs. To reduce NPLs to tolerable levels, creative regulatory solutions and well-designed risk extenuation techniques have been utilized in several countries in Asia, Africa, Latin America and Europe that may be applied in Bangladesh. Banks and NBFIs management should recruit qualified, knowledgeable, intelligent, honest, sincere and integrated managers. "In looking for people to hire, look for three qualities: integrity, intelligence, and energy. And if they don't have the first, the other two will kill you" - Warren Buffett, the business magnet of USA said.

Conclusion

The financial sectors including Banks and NBFIs in Bangladesh are passing thorough a crucial and critical stage. These sectors demand a robust, resilient, well-guided and well-supervised systems to tackle the great challenges faced by Banks and NBFIs. The existing rules, regulations and laws that conflict and act as deterrent instead of perfect solution to smooth operations – sanctioning of loans, recovery of loans from defaulted clients, actions against corrupt officials, etc., need to be changed or amended. It's the time to convert the traditional banking systems to a customer-centric, digital, mobile and online banking system using latest FinTechs. The lessons from economic and financial history tell us that no country won't be able to achieve SDGs, economic recovery and economic solvency – keeping its Banks and NBFIs in crisis. Proactive, timely and corrective steps need to be taken by the state-policy-makers, the Central Bank and the stake-holders of Banks and NBFIS to save this sector from the economic-financial-shock-waves and make it solid, strong, effective and efficient

Procedure for Liquidation or Winding up of Company in Bangladesh: Steps

Step 1 | File and Winding up or Liquidation Petition to the Court

A company may be wound by the court in certain circumstances: if the company through the special resolution decided that it must be wound up by the court; or if default is made in filling the statutory report or in holding the statutory meeting; or if the number of members reduced below the required number as per the Company Law; or the company is incapable of paying its debts; or if the court is of opinion that it is just and equitable to wind up the company.

When a company is deemed to unable to pay its debts is considered by section 242 of the Companies Act 1994. These will be if a creditor to whom the company is indebted for a sum and the company neglects to pay the sum for three weeks or if execution or other process issued on a decree or order of any court in favor of a creditor of company is returned unsatisfied in whole or in part or if it is proved to satisfaction of court that the company is unable to pay its debts and court shall take into account the contingent and prospective liabilities of company.

Section 316-321 of the Companies Act 1994 deals with winding up subject to supervision of court. When a company has by special or extraordinary resolved to wind up voluntarily the court may make an order that the voluntary winding up shall continue but subject to supervision of court and such terms as the court thinks just. Where an order is made for winding up subject to supervision, the liquidator may, subject to any restriction imposed by the court, exercise all the powers as if the company was being wound up altogether voluntarily.

It is to be noted that, according to section 247 of the 1994 Act, a winding up of a company by the court shall be deemed to commence at the time of the presentation of the petition for the winding up.

Step 2 | Draft and Prepare Winding Up Documents

In case of voluntary winding up, the second step is to prepare documents. These are Declaration of Solvency, (which shall include information such as the company has no debts among other things) and Profit and Loss Account and Audited Balance. These documents shall have to be approved by the majority directors of the company.

Step 3 | Documents Needs to be submitted to RJSC

The approved Declaration of Solvency then must be filed with the RJSC (Registrar of Joint Stock Companies and Firms) within 5 weeks.

Step 4 | Pass a Special Resolution in the Company

The next step is to pass a special resolution through the extraordinary general meeting to approve the decision of winding of the company and the appointment of the liquidator. This (the content of the meeting) shall also be filed with the RJSC. The above stated special resolution must be advertised, within 10 days of its passing, in the official Gazette, and in a newspaper circulating in the district where the registered office of the company is located.

Step 5 | Appointment of the Liquidator

After that, the liquidator shall accept the appointment and this must also be notified to the RJSC and the same shall be informed to the Deputy Commissioner of Taxes (having the jurisdiction) within 30 days of the said appointment.

Step 6 | Preparation of Final Report by the Liquidator

The liquidator shall prepare a Final Account showing how the winding ups has been conducted and the assets distributed. After that, an extra ordinary general meeting shall be called by the liquidator. The notice of the meeting must be given by way of advertisement which must not be less than one month before the meeting. Such an advertisement shall be given in the official Gazette, and in a newspaper circulating in the district where the registered office of the company is located. A special resolution shall be passed in the extraordinary general meeting with regards to the disposal of the books and papers of the company.

Step 7 | Filling all the Documents respectively to RJSC

Finally, there is a duty to hold a final meeting and the submission of the documents to the Registrar. Now the company winded up.

Case Study: The People's Leasing Case:

Hollowing out of People's Leasing: An insider job

The company owed Tk1,242 crore to individual depositors as of December 2018

Individual depositors on Wednesday rushed to the office of People's Leasing and Financial Services (PLFS) to withdraw money following a government move to liquidate the non-bank financial institution.

They, however, did not find anyone to meet, as no high official was present.

The company owed Tk1,242 crore to individual depositors as of December 2018.

On June 27, the finance ministry in a letter asked the Bangladesh Bank (BB) to take necessary steps to liquidate the institution.

It also directed the central bank to file a complaint with the Anti-Corruption Commission (ACC) against all officials involved in the money embezzlement of PLFS.

The instruction came after BB on May 21 proposed the ministry to lay off PLFS, which failed to pay back money to depositors.

This is the first financial institution that has been put in liquidation in the country's history.

The total loss of PLFS stood at Tk 2,324 crore at the end of December 2018. Its capital shortfall stood at Tk 2,013 crore. PLFS owed Tk 798 crore to different banks and financial institutions.

The size of its total loan portfolio was Tk1,145.18 crore, of which 67.46 percent was classified as of December last year.

Who is responsible for the downfall of PLFS?

An investigation by the central bank in 2014 revealed massive corruption by directors, involving Tk670 crore.

They embezzled the money from the institution in different ways between 2004 and 2013, when M Moazzam Hossain was its chairman.

Later in 2015, the central bank removed five board members.

Of them, Humaira Alamin, Arafin Shamsul Alamin and Nargis Alamin are also directors of Shamsul Alamin group.

The two others are Motiur Rahman and Khabir Uddin Miah.

Moazzam was identified by the central bank as one of the main culprits for dragging the institution into collapse.

Moazzam, in collusion with other directors swindled Tk123 crore from PLFS in the name of purchasing a disputed land at the city's Green Road.

The land was purchased from two dubious companies - Jenith and Jefair.

The money was used for adjusting default loan accounts of directors, according to the BB findings.

The central bank had asked PLFS to file a case with money loan court as well as a criminal case against Moazzam.

The company filed a case only with the money loan court against its former chairman.

PLFS neither got registry of the land nor got back the money.

Moazzam, who resigned from PLFS in November 2015, is now a director of a new generation bank - South Bangla Agriculture and Commerce (SBAC) Bank.

Motiur Rahman, who was among the five PLFS directors removed for their involvement in irregularities, has a defaulted loan of around Tk100 crore with the firm.

His wife is now a director of SBAC Bank.

Shamsul Alamin group took over Tk100 crore from PLFS when its three directors were in the board of the financial institution for 10 years until 2015.

Moreover, the group was involved in bringing out Tk123 crore in the name of purchasing land in collusion with Moazzam, according to central bank's findings.

Alamgir Shamsul Alamin, who is also president of the Real Estate and Housing Association of Bangladesh (REHAB), is the managing director of the business group.

Besides, he holds the post of managing director of Paramount Properties, where Moazzam is a director. PLFS had a loan of Tk65 crore to the group as of May last year.

Of the three directors of Shamsul Alamin group, who were in the PLFS board, are Almagir's family members. Humaira is his wife, Arafin is his younger brother and Nargis is Arafin's wife.

Contacted, Alamgir said they were repaying the money regularly and ready to pay the full amount.

The group was in the board of PLFS for 10 years, he said.

Asked who are responsible for the current situation of PLFS, he said 'off course who ran the company'.

Former PLFS director Khabir defaulted with a loan of above Tk100 crore with the company.

He took the credit against 11 unknown names between 2009 and 2010, when he was on its board.

Khabir has a jewelry business named Al Hassan Jewelry and Diamond.

During a visit to his jewelry shop at Gulshan in the city, he refused to talk to this correspondent.

Some influential clients who did not repay their loans have intensified the deterioration of PLFS.

For instance, Md Syful Islam, who was holding directorship of Islami Bank Bangladesh Ltd (IBBL) - the largest private bank in the country - even a month ago, is among the PLFS defaulters.

He took Tk4.5 crore from the institution in 2009 and in the last eight years, he turned defaulter for three times, taking the total outstanding loans to over Tk10 crore.

Syful - also a managing partner of an audit firm named Syful Shamsul Alam & Co - was holding the directorship of IBBL as the representative of Blue International.

The company he was representing in IBBL board has 2 percent holdings with the bank worth around Tk100 crore.

He quit the IBBL directorship a month ago citing personal ground.

Syful took the loan from PLFS in 2009 for purchasing a 98-katha land in Savar on the outskirts of the city and for constructing a building on his own land at Bashundhara Residential Area in the city where he owns a 15-katha land worth some Tk8 crore.

Just two weeks before taking the IBBL directorship on May 30, 2016, he rescheduled his loan for a second time by compromising required down payment with special consideration of the central bank.

The first installment payment started in June 2016 but he did not pay regularly and eventually turned defaulter again in February 2017.

PLFS then served him a notice through the central bank to vacate his directorship with the Islami Bank as bank company act does not allow a defaulter to hold a directorial position.

Contacted Sami Huda, managing director of PLFS, said Syful did not pay his loan despite repeated commitments with the company.

“As he failed to pay back the money, we marked him as defaulter and wrote to the central bank to vacate his directorship from the Islami Bank,” he said.

Intraco Group

The Chittagong-based business conglomerate started business with PLFS in 2005 by taking working capital of Tk26 crore for five years.

However, it did not repay the loan in 13 years even after availing special facilities including interest waiver beyond the banking norms.

In 2016, the company was allowed for a third time to reschedule its loans with special benefits. PLFS waived all the interest amount of Tk13 crore to get back the money fast to meet up its liquidity crisis at that time.

The company was given five years to pay off only the principal amount of Tk 25 lakh. Even during the period, no interest would be charged against the principal amount, which completely beyond the banking practice.

Despite getting such unique offer, the company did not continue the payment and turned defaulter in March last year. As the company could not continue the installment payment, the special facility was cancelled by PLFS.

As a result, all the interest from the year 2016 was calculated and the outstanding loan amount stood at around Tk 50 crore as of March last year, according to PLFS.

Hakim Ali, who is known for establishing first four-star hotel named Hotel Agrabad in Chittagong, is chairman of Intraco group.

His son, Mohammed Riyadh Ali, is managing director of the business group, while his wife Monowara Hakim Ali is a director.

Monowara is also president of Chittagong Women Chamber Of Commerce and Industry. Monowara and Riyadh both have personal guarantee against the loan accounts with PLFS.

[**Jebun Nesa Alo** 10 July, 2019, 08:15 pm,The Business Standard]

Bangladesh Financial Intelligence

Bangladesh Financial Intelligence Unit (BFIU) is the central agency of Bangladesh responsible for analyzing Suspicious Transaction Reports (STRs), Cash Transaction Reports (CTRs) & information related to money laundering (ML) /financing of terrorism (TF) received from reporting agencies & other sources and disseminating information/intelligence thereon to relevant law enforcement agencies. BFIU has been entrusted with the responsibility of exchanging information related to money laundering and terrorist financing with its foreign counterparts. The main objective of the BFIU is to establish an effective system for prevention of money laundering, combating financing of terrorism and proliferation of weapons of mass destruction.

BFIU was established in June 2002, in Bangladesh Bank (Central bank of Bangladesh) named as 'Anti Money Laundering Department'. To enforce and ensure the operational independence of FIU, Anti Money Laundering Department has been transformed as the Bangladesh Financial Intelligence Unit (BFIU) in 25 January, 2012 under the provision of Money Laundering Prevention Act, 2012 and has been bestowed with operational independence. BFIU has also achieved the membership of Egmont Group in July, 2013.

Legal Framework

BFIU works under the provisions of Money Laundering Prevention Act, 2012 and Anti-Terrorism Act, 2009 (including amendments in 2013).

Corporate Fraud? Definition, Types, and Example

What Is Corporate Fraud?

Corporate fraud refers to illegal activities undertaken by an individual or company that are done in a dishonest or unethical manner. Often, this kind of business fraud is designed to give an advantage to the perpetrating individual or company. Corporate fraud schemes go beyond the scope of an employee's stated position and are marked by their complexity and economic impact on the business, other employees, and outside parties.

Key Takeaways

- When companies engage in activities that are dishonest or illegal, it is referred to as corporate fraud.
- There are many forms of corporate fraud including falsified accounting and misrepresenting services or products.
- The Enron scandal from 2001 is a well-known example of corporate fraud.

How Corporate Fraud Works

Corporate fraud can be challenging to prevent and tricky to catch. By creating effective policies, a system of checks and balances, and physical security, a company may limit the extent to which fraud can take place. Corporate fraud is considered a white-collar crime.

Types of Corporate Fraud

Though it may be conducted in a variety of ways, corporate fraud frequently is performed by taking advantage of confidential information or access to sensitive assets and then leveraging those assets for gain. The fraud is often hidden behind legitimate business practices or exchanges to disguise the illicit activity. Multiple stakeholders involved in corporate fraud also allows for elaborate fraud schemes to be protected by a group of complicit actors.

For example, a company's financial accounting records may be altered to present an image of high revenue and profits compared with the actual financial results. These actions might be taken to hide shortcomings such as a net loss, slow revenue, declining sales, or hefty expenses. Falsified accounting might be done to make the company more attractive to potential buyers or investors, or ultimately protect a public company's stock or valuation from dropping.

Other forms of corporate fraud may aim to disguise or misrepresent a service or product the company is developing or has in service, hiding its flaws or defects. Rather than investing in repairing, refurbishing, or redesigning the product, those responsible for the product attempt to deflect or disguise these issues. This might be done if the department or company does not have the finances to correct the problem or if revealing the issue might drive away customers and investors.

If a company or individual claims it is putting some of its funds towards investments or other types of monetary reserves that are intended to gain in value, but in actuality, those funds have been expended or diverted elsewhere, this counts as a type of corporate fraud.

Example of Corporate Fraud

The deceptive accounting and business practices that led to the downfall of Enron is an example of corporate fraud. Due to the widespread use of loopholes and other disguising tactics, the company hid debt from failed deals, the sum reaching into the billions of dollars. To maintain the charade, those responsible pressured their auditors to hide their deception, which included the destruction of financial documents.

Accounting Fraud? Definition and Examples

Accounting fraud is the intentional manipulation of financial statements to create a false appearance of corporate financial health. Furthermore, it involves an employee, accountant, or the organization itself misleading investors and shareholders. A company can falsify its financial statements by overstating its revenue, not recording expenses, and misstating assets and liabilities.

Key Takeaways

- Accounting fraud is the illegal alteration of a company's financial statements in order to manipulate a company's apparent health or to hide profits or losses.
- Overstating revenue, failing to record expenses, and misstating assets and liabilities are all ways to commit accounting fraud.
- The Enron scandal is one of the most famous examples of accounting fraud in history.

Understanding Accounting Fraud

For accounting fraud to take place, a firm must deliberately falsify financial records. Consider a firm that makes an estimate that must be revised later. No accounting fraud has taken place because the errors were not deliberate. Now suppose the CEO of a publicly-traded company knowingly makes false statements about the firm's prospects. The Securities and Exchange Commission (SEC) may well charge that CEO with fraud. However, it is not accounting fraud because no financial records were falsified.

Always be careful when alleging accounting fraud. Fraud requires intent, which can be difficult to prove.

Overstating Revenue

A company can commit accounting fraud if it overstates its revenue. Suppose company ABC is actually operating at a loss and not generating enough revenue. To cover up this situation, the firm might claim to be producing more income on financial statements than it does in reality. On its statements, the company's profits would be inflated. If the company overstates its revenues, it would drive up the firm's share price and create a false image of financial health.

Unrecorded Expenses

Another type of accounting fraud takes place when a company does not record its expenses. The company's net income is overstated, and its costs are understated on the income statement. This type of accounting fraud creates a false impression of how much net income a company is receiving. In reality, it may be losing money.

Financial Statement Manipulation

Financial statement manipulation is a type of accounting fraud that remains an ongoing problem in corporate America. Although the Securities and Exchange Commission (SEC) has taken many steps to mitigate this type of corporate malfeasance, the structure of management incentives, the enormous latitude afforded by the Generally Accepted Accounting Principles (GAAP), and the ever-present conflict of interest between the independent auditor and the corporate client continues to provide the perfect environment for such activity.1

Due to these factors, investors who purchase individual stocks or bonds must be aware of the issues, warning signs, and the tools that are at their disposal in order to mitigate the adverse implications of these problems.

Key Takeaways

- The manipulation of financial statements to commit fraud against investors or skirt regulation is a real and ongoing problem, costing billions of dollars each year.2
- Managers may also "cook the books" in order to qualify for certain executive compensation that relies on certain financial performance metrics being met.
- Because generally accepted accounting standards can be flexible and open for interpretation by a company's management, fudging numbers can be difficult to detect.

How Financial Statements Are Manipulated

Reasons Behind Financial Statement Manipulation

There are three primary reasons why management manipulates financial statements. First, in many cases, the compensation of corporate executives is directly tied to the financial performance of the company. As a result, they have a direct incentive to paint a rosy picture of the company's financial condition in order to meet established performance expectations and bolster their personal compensation.

Second, it is a relatively easy thing to do. The Financial Accounting Standards Board (FASB), which sets the GAAP standards, provides a significant amount of latitude and interpretation in accounting provisions and methods. For better or worse, these GAAP standards afford a significant amount of flexibility, making it feasible for corporate management to paint a particular picture of the financial condition of the company.

Third, it is unlikely that financial manipulation will be detected by investors due to the relationship between the independent auditor and the corporate client. In the U.S., the Big Four accounting firms and a host of smaller regional accounting firms dominate the corporate auditing environment. While these entities are touted as independent auditors, the firms have a direct conflict of interest because they are compensated, often quite significantly, by the very companies that they audit. As a result, the auditors could be tempted to bend the accounting rules to portray the financial condition of the company in a manner that will keep the client happy—and keep its business.

How Financial Statements Are Manipulated

There are two general approaches to manipulating financial statements. The first is to exaggerate current period earnings on the income statement by artificially inflating revenue and gains, or by deflating current period expenses. This approach makes the financial condition of the company look better than it actually is in order to meet established expectations.

The second approach requires the exact opposite tactic, which is to minimize current period earnings on the income statement by deflating revenue or by inflating current period expenses. It may seem counterintuitive to make the financial condition of a company look worse than it actually is, but there are many reasons to do so: to dissuade potential acquirers; getting all of the bad news "out of the way" so that the company will look stronger going forward; dumping the grim numbers into a period when the poor performance can be attributed to the current macroeconomic environment; or to postpone good financial information to a future period when it is more likely to be recognized.

Specific Ways to Manipulate Financial Statements

When it comes to manipulation, there are a host of accounting techniques that are at a company's disposal. *Financial Shenanigans* (2018) by Howard Schilit outlines seven primary ways in which corporate management manipulates the financial statements of a company.

1. **Recording Revenue Prematurely or of Questionable Quality**
   1. Recording revenue prior to completing all services
   2. Recording revenue prior to product shipment
   3. Recording revenue for products that are not required to be purchased
2. **Recording Fictitious Revenue**
   1. Recording revenue for sales that did not take place
   2. Recording investment income as revenue
   3. Recording proceeds received through a loan as revenue
3. **Increasing Income with One-Time Gains**
   1. Increasing profits by selling assets and recording the proceeds as revenue
   2. Increasing profits by classifying investment income or gains as revenue
4. **Shifting Current Expenses to an Earlier or Later Period**
   1. Amortizing costs too slowly
   2. Changing accounting standards to foster manipulation
   3. Capitalizing normal operating costs in order to reduce expenses by moving them from the income statement to the balance sheet
   4. Failing to write down or write off impaired assets
5. **Failing to Record or Improperly Reducing Liabilities**
   1. Failing to record expenses and liabilities when future services remain
   2. Changing accounting assumptions to foster manipulation
6. **Shifting Current Revenue to a Later Period**
   1. Creating a rainy day reserve as a revenue source to bolster future performance
   2. Holding back revenue
7. **Shifting Future Expenses to the Current Period as a Special Charge**
   1. Accelerating expenses into the current period
   2. Changing accounting standards to foster manipulation, particularly through provisions for depreciation, amortization, and depletion3

While most of these techniques pertain to the manipulation of the income statement, there are also many techniques available to manipulate the balance sheet, as well as the statement of cash flows. Moreover, even the semantics of the management discussion and analysis section of the financials can be manipulated by softening the action language used by corporate executives from "will" to "might," "probably" to "possibly," and "therefore" to "maybe." Taken collectively, investors should understand these issues and nuances and remain on guard when assessing a company's financial condition.

Financial Manipulation via Corporate Merger or Acquisition

Another form of financial manipulation may happen during the merger or acquisition process. One classic approach occurs when management tries to whip up support for a merger or acquisition based primarily on the improvement in the estimated earnings per share of the combined companies. Let's look at the table below in order to understand how this type of manipulation takes place.

Detecting Financial Statement Fraud

By

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Reviewed by Andy Smith

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On Dec. 2, 2001, energy behemoth Enron shocked the world with its widely-publicized bankruptcy after the firm was busted for committing egregious accounting fraud.1 Its dubious tactics were aimed at artificially improving the appearance of the firm's financial outlook by creating off-balance-sheet special purpose vehicles (SPVs) that hid liabilities and inflated earnings. But in late 2000, The Wall Street Journal caught wind of the firm's shady dealings, which ultimately led to the then-largest U.S. bankruptcy in history.2 And after the dust settled, a new regulatory infrastructure was created to mitigate future fraudulent dealings.

Key Takeaways

- Financial statement fraud occurs when corporations misrepresent or deceive investors into believing that they are more profitable than they actually are.
- Enron's 2001 bankruptcy in 2001 led to the creation of the Sarbanes-Oxley Act of 2002, which expands reporting requirements for all U.S. public companies.
- Tell-tale signs of accounting fraud include growing revenues without a corresponding growth in cash flows, consistent sales growth while competitors are struggling, and a significant surge in a company's performance within the final reporting period of the fiscal year.

- There are a few methods to inconsistencies, including vertical and horizontal financial statement analysis or by using the total assets as a comparison benchmark.

2:12

Detecting Financial Statement Fraud

What Is Financial Statement Fraud?

The Association of Certified Fraud Examiners (ACFE) defines accounting fraud as "deception or misrepresentation that an individual or entity makes knowing that the misrepresentation could result in some unauthorized benefit to the individual or to the entity or some other party." Put simply, financial statement fraud occurs when a company alters the figures on its financial statements to make it appear more profitable than it actually is, which is what happened in the case of Enron.

Financial statement fraud is a deliberate action wherein an individual "cooks the books" to either mislead investors.

According to the ACFE, financial statement fraud is the least common type of fraud in the corporate world, accounting for only 10% of detected cases. But when it does occur, it is the most costly type of crime, resulting in a median loss of $954,000. Compare this to the most common and least costly type of fraud—asset misappropriation, which accounts for 85% of cases and a median loss of only $100,000.3

Nearly one-third of all fraud cases were the result of insufficient internal controls.4 About half of all the fraud reported in the world were executed in the United States and Canada, with a total of 895 reported cases or 46%.5

The FBI counts corporate fraud, including financial statement fraud, among the major threats that contribute to white-collar crime. The agency states that most cases involve accounting schemes where share prices, financial data, and other valuation methods are manipulated to make a public company appear more profitable.6

Types of Financial Statement Fraud

And then there's the outright fabrication of statements. This, for instance, famously occurred when disgraced investment advisor Bernie Madoff collectively bilked some 4,800 clients out of nearly $65 billion by conducting an elaborate Ponzi scheme that involved wholly falsifying account statements.7

Financial statement fraud can take multiple forms, including:

- Overstating revenues by recording future expected sales
- Inflating an asset's net worth by knowingly failing to apply an appropriate depreciation schedule
- Hiding obligations and/or liabilities from a company's balance sheet

- Incorrectly disclosing related-party transactions and structured finance deals

Another type of financial statement fraud involves cookie-jar accounting practices, where firms understate revenues in one accounting period and maintain them as a reserve for future periods with worse performances, in a broader effort to temper the appearance of volatility.

The Sarbanes-Oxley Act of 2002

The Sarbanes-Oxley Act of 2002 is a federal law that expands reporting requirements for all U.S. public company boards, management, and public accounting firms. The Act, often abbreviated as Sarbanes–Oxley or SOX, was established by Congress to ensure that companies report their financials honestly and to protect investors.

The rules and policies outlined in SOX are enforced by the Securities and Exchange Commission (SEC) and broadly focus on the following principal areas:

1. Corporate responsibility
2. Increased criminal punishment
3. Accounting regulation
4. New protections

The law is not voluntary., which means that all companies must comply.8 Those that don't adhere to the are subject to fines, penalties, and even prosecution.

Financial Statement Fraud Red Flags

Financial statement red flags can signal potentially fraudulent practices. The most common warning signs include:

- Accounting anomalies, such as growing revenues without a corresponding growth in cash flows.
- Consistent sales growth while competitors are struggling.
- A significant surge in a company's performance within the final reporting period of a fiscal year.
- Depreciation methods and estimates of assets' useful life that don't correspond to those of the overall industry.
- Weak internal corporate governance, which increases the likelihood of financial statement fraud occurring unchecked.
- Outsized frequency of complex third-party transactions, many of which do not add tangible value, and can be used to conceal balance sheet debt.
- The sudden replacement of an auditor resulting in missing paperwork.
- A disproportionate amount of management compensation derived from bonuses based on short-term targets, which incentivizes fraud.

Financial Statement Fraud Detection Methods

While spotting red flags is difficult, vertical and horizontal financial statement analysis introduces a straightforward approach to fraud detection. Vertical analysis involves taking every item in the income statement as a percentage of revenue and comparing the year-over-year trends that could be a potential flag cause of concern.

A similar approach can also be applied to the balance sheet, using total assets as the comparison benchmark, to monitor significant deviations from normal activity. Horizontal analysis implements a similar approach, whereby rather than having an account serve as the point of reference, financial information is represented as a percentage of the base years' figures.

Comparative ratio analysis likewise helps analysts and auditors spot accounting irregularities. By analyzing ratios, information regarding day's sales in receivables, leverage multiples, and other vital metrics can be determined and analyzed for inconsistencies.

A mathematical approach known as the Beneish Model evaluates eight ratios to determine the likelihood of earnings manipulation, including asset quality, depreciation, gross margin, and leverage. After combining the variables into the model, an M-score is calculated. A value greater than -2.22 warrants further investigation, while an M-score less than -2.22 suggests that the company is not a manipulator.

The Bottom Line

Federal authorities have put laws in place that make sure companies report their financials truthfully while protecting the best interests of investors. But while there are protections in place, it also helps that investors know what they need to look out for when reviewing a company's financial statements. Knowing the red flags can help individuals detect unscrupulous accounting practices and stay one step ahead of bad actors attempting to hide losses, launder money, or otherwise defraud unsuspecting investors.

Securities Fraud? Definition, Main Elements, and Examples

What Is Securities Fraud?

Securities fraud, also referred to as stock or investment fraud, is a type of serious white-collar crime that can be committed in a variety of forms but primarily involves misrepresenting information investors use to make decisions.

The perpetrator of the fraud can be an individual, such as a stockbroker. Or, it can be an organization, such as a brokerage firm, corporation, or investment bank. Independent individuals might also commit this type of fraud through schemes such as insider trading.

Key Takeaways

- Securities fraud is an illegal or unethical activity carried out involving securities or asset markets in order to profit at the expense of others.
- This type of fraud is a serious crime usually involving the investment world.
- Examples of securities fraud include Ponzi schemes, pyramid schemes, and late-day trading.
- Securities fraud can also include false information, pump-and-dump schemes, or trading on insider information.

Understanding Securities Fraud

The Federal Bureau of Investigation (FBI) describes securities fraud as criminal activity that can include high-yield investment fraud, Ponzi schemes, pyramid schemes, advanced fee schemes, foreign currency fraud, broker embezzlement, hedge-fund-related fraud, and late-day trading.1 In many cases, the fraudster seeks to dupe investors through misrepresentation and to manipulate financial markets in some way.

This crime includes providing false information, withholding key information, offering bad advice, and offering or acting on inside information.

Types of Securities Fraud

Securities fraud takes on many forms. In fact, there is no shortage of methods used to trick investors with false information. High-yield investment fraud, for example, may come with guarantees of high rates of return while claiming there is little to no risk. The investments themselves may be in commodities, securities, real estate, and other categories. Advance fee schemes can follow a more subtle strategy, where the fraudster convinces their targets to advance them small amounts of money that are promised to result in greater returns.

Sometimes the money is requested to cover processing fees and taxes for the funds that allegedly await to be disbursed. Ponzi and pyramid schemes typically draw upon the funds furnished by new investors to pay the returns that were promised to prior investors caught up in the arrangement. Such schemes require the fraudsters to continuously recruit more victims to keep the sham going for as long as possible.

One of the newer types of securities fraud is Internet fraud. This type of scheme is also referred to as a pump-and-dump scheme, in which people use chat rooms and forums to spread false or fraudulent information concerning stocks. The intention is to force a price increase in those stocks—the pump, and then when the price reaches a certain level, they sell them off—the dump.

The FBI warns that security fraud is often noted by unsolicited offers and high-pressure sales tactics on the part of the fraudster, along with demands for personal information such as credit card information and Social Security numbers.1 The Securities and Exchange Commission (SEC), the FBI, and other federal and state agencies investigate allegations of securities fraud. The crime can carry both criminal and civil penalties, resulting in imprisonment and fines.

Examples of Securities Fraud

Some common types of securities fraud include manipulating stock prices, lying on SEC filings, and committing accounting fraud. Some famous examples of securities fraud are the Enron,2 Tyco,3 Adelphia,4 and WorldCom scandals.5

Here, bad actors try to manipulate the price of a stock for their own gain by spreading false information, often via Internet or newsletter, and then getting out of their position after that false information has been acted upon by unsuspecting investors. For instance, during the summer months of the stock below, a pump and dump scheme was initiated by using a "wrong number" scam. A message was left on victims answering machines that talked of a hot stock tip and was constructed so that the victim would think that the message was an accident.

As seen in the above chart, the price rose from around $0.30 to nearly $1.00, a more than 200% increase in a one-week period. This drastic increase was seen along with an equally large increase in volume. The stock had seen an average daily trading volume before the price increase of less than 250,000, but during the scam, the stock traded up to nearly 1 million shares on a number of trading days. The unsuspecting investors would have bought into the stock at around $1.00. As seen above, it fell to around $0.20, an 80% decline in value for those unfortunate investors.

What Is Insider Trading, and When Is It Legal?

By Akhilesh Ganti

Updated March 07, 2022

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Investopedia / Mira Norian

What Is Insider Trading?

Insider trading involves trading in a public company's stock or other securities by employees with non-public, material information about the company. Insider trading can be either illegal or legal depending on when the insider makes the trade and the laws of the country the person is in.

In the U.S., insider trading is illegal when the material information is still non-public, and those who commit it face harsh consequences.

Key Takeaways

- Insider trading is the buying or selling of a publicly traded company's stock by someone who has non-public, material information about that stock.
- Material nonpublic information is any information that could substantially impact an investor's decision to buy or sell the security that has not been made available to the public.
- This form of insider trading is illegal and comes with stern penalties including both potential fines and jail time.
- Insider trading can be legal as long as it conforms to the rules set forth by the SEC.

1:43

Insider Trading

Understanding Insider Trading

The U.S. Securities and Exchange Commission (SEC) defines illegal insider trading as:

The buying or selling a security, in breach of a fiduciary duty or other relationship of trust and confidence, on the basis of material, nonpublic information about the security.1

Material information is any information that could substantially impact an investor's decision to buy or sell the security. Non-public information is information that is not legally available to the public.

The question of legality stems from the SEC's attempt to maintain a fair marketplace. An individual who has access to insider information would have an unfair edge over other investors, who do not have the same access and could potentially make larger, unfair profits than their fellow investors.

Illegal insider trading includes tipping others when you have any sort of material nonpublic information. Legal insider trading happens when directors of the company purchase or sell shares, but they disclose their transactions legally. The Securities and Exchange Commission has rules to protect investments from the effects of insider trading. It does not matter how the material nonpublic information was received or if the person is employed by the company.

For example, suppose someone learns about nonpublic material information from a family member and shares it with a friend. If the friend uses this insider information to profit in the stock market, then all three of the people involved could be prosecuted.1

The best way to stay out of legal trouble is to avoid sharing or using material nonpublic information, even if you overheard it accidentally.

Pyramid Scheme: How Does It Work

A pyramid scheme is a fraudulent and unsustainable investment pitch that relies on promising unrealistic returns from imaginary investments. The early investors actually get paid those big returns, which leads them to recommend the scheme to others. Investors' returns are paid out of the new money flowing in. Eventually, no new investors can be found and the pyramid collapses.

In a variation of the pyramid scheme, investors at each level charge initiation fees that are paid by the next layer of investors. A portion of those fees is paid on to those in the top layers of the pyramid. Eventually, no one is left to recruit. The pyramid collapses.

Often called pyramid scams, these operations are illegal in the U.S.1

Key Takeaways

- A pyramid scheme funnels earnings from all recruited participants on lower levels of an organization to participants on higher levels.
- It is a felony in the U.S. to recruit participants into pyramid schemes.
- Pyramid schemes rely on income from recruitment fees and not, as participants may believe, from the sale of actual goods or services with real value.
- Multi-Level Marketing operations (MLMs) are legitimate business programs in which distributors earn money from the sale of tangible goods and from commissions on their recruited distributors' purchases and sales.

- Pyramid schemes often masquerade as MLMs but their focus is on fees from recruits, not revenue from product sales.

How Pyramid Schemes Work

Pyramid schemes are so named because their compensation structures resemble a pyramid. The scheme starts with a single point on top where the original members exist and becomes progressively wider toward the bottom as people are recruited by every level of recruits.

Image by Julie Bang © Investopedia 2019

Say that the scheme's founder Mike sits alone at the top of the pyramid. He recruits 10 people with some promise of a big return on their money. They're represented by the level directly below him on the pyramid.

Each of those new, 10 members, or participants, pays Mike a certain fee to take part in the opportunity he's offered them. Then, each of those members is encouraged to recruit 10 more members, for a total of 100 members.

Now each of those 100 new recruits must pay fees to the tier-two recruiters, who must send a percentage of their earnings up to Mike. This recruitment and payment cycle repeats over and over again for as long as possible. As it does, money continues to flow upward to those in the levels above.

The emphasis in pyramid schemes is on recruiting new members. Seldom is the sale of any product or service actually involved, though it may have been implied to attract recruits. There is no identifiable source of income other than that coming from those recruited.2

According to the hard-sell pitches made at recruitment events, those bold enough to take the pyramid plunge will receive substantial cash from the recruits below them. However, in practice, the prospective member pools tend to dry up over time. By the time a pyramid scheme invariably shuts down, the top-level operatives may walk away with loads of cash while the majority of lower-level members are left empty-handed.

Note

According to the U.S. Securities and Exchange Commission (SEC), investors should be aware of these features of pyramid schemes:

- No genuine product or service
- Promises of high returns in a short time period
- Easy money or passive income
- No demonstrated revenue from retail sales
- Buy-in required
- Complex commission structure
- Emphasis on recruiting3

Types of Pyramid Schemes

Multi-Level Marketing Pyramid Scheme

Multi-level marketing (MLM) is a legal business program. This business model involves the sale of actual goods or services by distributors or participants in the MLM. Distributors get paid for those products and services of the MLM that they sell. They can also receive income from sales made by distributors that they've recruited and from people those recruits then bring in.4

However, some pyramid schemes disguise themselves as MLMs. The Federal Trade Commission warns people to take note of, and avoid, MLM promoters who:

- Make extraordinary claims of enormous earning potential
- Try to persuade people that recruiting others is where the real money lies
- Pressure people to get involved without learning more about the company
- Make it clear that an opportunity will be lost unless people get in immediately

Another warning sign is seeing existing distributors who continue to buy products that they can never sell so that they can qualify for some kind of reward.4

Chain Emails

Chain emails persuade naive recipients to donate money to everyone listed within an email. After making their donations, the donors are invited to delete the first name on the list and replace it with their own.

They're instructed to forward the email along to their own groups of contacts, in the hope that one or more of them will send cash their way. In theory, recipients will keep collecting donations until their name is deleted from the list.

Ponzi Schemes

Ponzi schemes are investment cons that work by robbing Peter to pay Paul. They may not necessarily adopt a pyramid scheme's hierarchical structure but they do promise high returns to existing investors.

Ponzi schemes typically involve a single, initial investment only from investors. Then, those investors wait for the promised return on their money. That is provided by new money from other investors persuaded to take part by the leader of the scheme. Most Ponzi participants end up losing everything when money for this sort of scheme dries up.

Investment advisor Bernard Madoff, arguably the most notorious Ponzi scheme artist, was sentenced to 150 years in prison for operating a multibillion-dollar Ponzi scheme.5 Madoff convinced many high-profile individuals to invest with him, falsified portfolios and relevant paperwork, and paid off early investors with money received from later investors. Most investors lost everything. Madoff died in prison on April 14, 2021.

Example of a Pyramid Scheme

In recent years, the SEC filed charges to stop a pyramid scheme masquerading as an MLM program. The company, which was called CKB, solicited investors all over the world, and in particular, focused on Asian-American communities in New York and California.3

The SEC alleged that CKB posed as a very profitable MLM company that made money selling online educational courses for children. Unfortunately, this classic pyramid scheme involved little or no retail sales. Its only source of revenue was the money it procured from new investors.3

How Pyramid Schemes Collapse

Pyramid schemes are viable as long as new, paying participants continue to buy in. The pyramid base must continue to grow. When the pool of available and willing participants disappears, the entire structure collapses.

It's impossible for pyramid schemes to function for long terms. People will invariably lose their money. Even high-level early participants may lose money near the end, due to waiting periods that delay payments from lower level recruits.

Is a Pyramid Scheme Illegal in the United States?

Essentially, yes. In the U.S., it is a felony crime to recruit any person to take part in a pyramid scheme. This crime may result in four years in prison and a fine of $5,000.1

How Do Pyramid Schemes Succeed?

The success of pyramid schemes is usually limited to founders and early-stage members. These people fraudulently attract new, fee-paying members eager to make a promised quick and large monetary return. These members then recruit more fee-paying members. This cycle continues. The income flows up to the founders and earlier members. The scheme typically collapses once no more fee-paying members can be found to support the existing members with their payments.

Are Pyramid Schemes the Same as Multi-Level Marketing Programs?

No, they are not the same. MLMs are legal, legitimate businesses whose distributors earn money from the sale of actual products and from commissions on products sold by distributors that they recruit. However, sometimes, pyramid schemes pose as MLMs to attract people who are likely to want to work with the MLM model.

The Bottom Line

Pyramid schemes are illegal in many countries. The pyramid model of profiting from a network of contacts often forces individuals to recruit their family members, friends, and acquaintances. This ultimately can strain relationships. Investors would be wise to avoid such schemes.

Ponzi Scheme vs. Pyramid Scheme: What's the Difference?

By
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Updated November 30, 2021
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Ponzi Scheme vs. Pyramid Scheme: An Overview

Ponzi and pyramid schemes have many similar characteristics based on the same concept: unsuspecting individuals get fooled by unscrupulous investors who promise them extraordinary returns in exchange for their money. Unlike a regular investment, these schemes can offer consistent profits only as long as the number of investors continues to increase. Once the number tapers off, so does the money.

Ponzi and pyramid schemes are self-sustaining as long as cash outflows can be matched by monetary inflows. The basic differences arise in the type of products that schemers offer their clients and the structure of the two ploys, but both can be devastating if broken down.

Key Takeaways

- Ponzi and pyramid schemes involve unscrupulous investors taking advantage of unsuspecting individuals by promising them extraordinary returns in exchange for their money.
- With Ponzi schemes, investors give money to a portfolio manager and are paid out with the incoming funds contributed by later investors.
- With a pyramid scheme, the initial schemer recruits other investors to recruit others (and so on) where new recruits pay the person who recruited them for the right to participate or perhaps sell a certain product.
- These schemes promise big results and often fail to provide financial documents to investors.
- Contact local authorities, the SEC, and/or the FTC if you suspect you've been a victim of any type of financial fraud, including Ponzi and pyramid schemes.

Ponzi Schemes

Ponzi schemes are based on fraudulent investment management services. They promise investors higher returns than traditional investments by paying returns to investors from money taken from new investors.

Here's how it works. Investors contribute money to the portfolio manager (the person running the scheme) who promises them a high return. When those investors want their money back, they are paid out with the incoming funds contributed by later investors.

The person who organizes this type of fraud is in charge of controlling the entire operation. But rather than put the money into a type of investment that earns interest, they merely transfer funds from one client to another and forgo any real investment activities.

Warning Signs of a Ponzi Scheme

So how do you know if you're involved in a Ponzi scheme? There are several telltale signs, including:

- Promises of high returns. Be wary if your portfolio manager makes claims that your profits will net you substantially higher returns than those of traditional investments.

- Little to no risk. Every investment offers some degree of risk. So there should be some alarm bells when someone says you'll be completely shielded and your money is protected.
- Lack of registration and licenses. Legitimate investments are regulated and managers are licensed. Make sure you ask to see any documents and credentials of anyone who is offering big results for your money.
- Complicated investment strategies. If you can't understand how your money generates returns, it's probably too good to be true.
- Missing paperwork and payments. You should be concerned if you aren't receiving any statements and/or if you don't get the payments that you're promised.

Examples of Ponzi Schemes

- **Bernie Madoff:** The most famous Ponzi scheme in recent history—and the single largest fraud of investors in the United States—was orchestrated for more than a decade by Bernard Madoff, who defrauded investors in Bernard L. Madoff Investment Securities LLC. Madoff built a large network of investors from whom he raised cash, pooling his almost 5,000 clients' money into an account he withdrew from. But he never actually invested the money, and once the 2007-2008 financial crisis took hold, he could no longer sustain the fraud. The total loss to investors was estimated to be around $65 billion.12 The controversy sparked a period in late 2008 that is known as Ponzi Mania, in which regulators and investment professionals were on the hunt for other Ponzi schemes.
- **JSG Capital Investments:** The U.S. Attorney's Office of the Northern District of California said two men were indicted in 2016 by a grand jury for wire fraud. Jaswant Singh Gill and Javier Carlos Rios of JSG Capital Investments were accused of promising investors that they would buy pre-IPO shares of private companies. Instead, the two men used the money for their own use and paid them interest to prevent individuals from getting suspicious. More than $5.5 million was diverted while the two men were accused of raising $9.3 million from their investors.3

Money managers should be able to offer verifiable financial data; true investments can be easily checked.

Pyramid Schemes

A pyramid scheme works a little differently than a Ponzi scheme. This scheme is structured so that the initial schemer must recruit other investors who will continue to recruit other investors, and those investors will then continue to recruit additional investors, and so on.

People at the top of the pyramid tend to profit the most. And because they earn more money, they're able to entice more people to join. As more people join, more money finds its way into the pyramid, which gets funneled in from new investors to the people higher up. But those at the bottom lose out, especially if they can't get others to join.

There may sometimes be an incentive that is presented as an investment opportunity, such as the right to sell a particular product or multilevel marketing (MLM). Each investor pays the person who recruited them for the chance to sell this item. The recipient must then share the proceeds with those at the higher levels of the pyramid structure.

Warning Signs of a Pyramid Scheme

You may be able to guess when you're in a pyramid scheme if the following is true:

- Recruitment. This is the main way of drawing people into the scheme. And you can't join (and thus, earn money) unless you pay a fee. In most cases, you'll also be promised more money if you recruit others.
- Fast cash. Most pyramid schemes promise to pay you big returns in a short amount of time. In many cases, these returns usually come from money paid by new recruits.
- Passive income. There are many schemes that promise to pay you money without any actual work. Again, this money is almost always coming from new recruits to the pyramid.
- Lack of documentation. Like the Ponzi scheme, there is almost never any documentation that proves how the revenue is generated. Be sure to ask for financial statements, which should be audited by a financial professional.
- Hard to understand the commission structure. If you can't understand where your profits are coming from or how anyone in the scheme is paid, then it's probably too good to be true.

Examples of Pyramid Schemes

- **Business in Motion:** This scheme required investors in Canada to pay $3,200 to join the scheme. This allowed them to purchase vacation packages that they could then resell to others for a higher fee, thus earning a bigger return. In order to keep the money coming for those at the top, the scheme required more people to join. But the vacation deals weren't even the cheapest on the market, which concerned many of the people involved. Canadian authorities charged the organizer, who was ordered to pay $6.5 million to roughly 2,000 people in a 2014 class action lawsuit.4
- **Herbalife:** One of the largest accused pyramid schemes was with the nutritional company Herbalife (HLF). The company is an MLM that develops and markets dietary supplements with operations in more than 90 countries. Federal regulators in the United States said that the company deceived consumers about the potential for returns. The claim also stated that Herbalife compensated its distributors for bringing others into the scheme, asking these new players to purchase products before the program began. Even though it was labeled as an illegal pyramid scheme and paid out more than $200 million in damages, Herbalife's products still sell, and the stock price looks healthy.5

Other types of investment fraud include affinity fraud, microcap fraud, and pump-and-dump scams.

Key Differences

Ponzi and pyramid schemes are both similar investment frauds perpetrated by one or more individuals seeking personal gain. They both involve deceiving others by promising substantial income or returns on an investor's initial investment. But there are inherent differences between the two.

One key difference is that pyramid schemes are harder to prove than Ponzi schemes. They are also better protected because the legal teams behind corporations are much more powerful than those protecting an individual.

Another thing that sets these two types of schemes apart is that the Ponzi scheme only requires investors to put up their money in exchange for returns. Pyramid schemes, on the other hand, require investors to pay a fee or purchase products in order to participate and earn returns.

What to Do If You Are the Victim of a Scheme

Don't allow yourself to be duped if someone asks you to invest your hard-earned money with promises of big returns. But if you are enthralled by the idea and there is a chance that it may be legitimate, get a second opinion. Use a lawyer or certified public accountant (CPA) to scour the documents for inconsistencies.

But it is equally as important to investigate those who manage investors' money. There are a number of ways that you can report the perpetrators of Ponzi and pyramid schemes—or any other type of financial fraud:

- Contact your local law enforcement agency and file a report.
- You can also call the Securities and Exchange Commission (SEC) to ask if there are open investigations into a money manager or prior instances of fraud.
- Check with the Federal Trade Commission (FTC) by phoning the agency or filing a complaint online.

What Are the Main Differences Between a Ponzi and Pyramid Scheme?

Ponzi and pyramid schemes are two different types of financial fraud. But there are key points that make them distinct from one another. Ponzi schemes can be easier to detect while pyramid schemes can be hidden to make them look legitimate.

Ponzi schemes simply require a cash investment to earn returns. Pyramid schemes, on the other hand, need you to pay a fee and/or purchase products and services in order to participate and earn income.

How Do You Tell if You're in a Ponzi Scheme?

There are several warning signs of a Ponzi scheme. First, the investment manager will promise you substantially higher returns that any traditional investment with little to no risk. The investment may not be registered and the individual may not even be licensed by state and federal authorities, which is a requirement. Investment strategies are often too complicated to understand and you may not receive any statements. Finally, if you begin missing any of your regular payments, you may be the victim of a Ponzi scheme.

How Does a Pyramid Scheme Work?

Pyramid schemes are a form of financial fraud. They can be disguised as financial opportunities that make them appear legitimate. Pyramid schemes offer big returns for little investment capital and often promise a way to earn income passively. They require individuals to pay an entrance fee and/or purchase products/services in order to participate. These people are then required to bring in more people to the scheme. People at the top are paid the most, receiving a portion of the money that the new recruits contribute. Those at the bottom of the pyramid make little to nothing, especially when no new individuals are recruited.

How Do You Report a Ponzi or Pyramid Scheme?

If you believe that you've been a victim of a Ponzi or pyramid scheme (or any other form of financial fraud), contact your local authorities. You can also file complaints with the Securities and Exchange Commission or the Federal Trade Commission by phone or through their websites.

The Bottom Line

There are two additional important factors to consider: The only guilty party in the Ponzi and pyramid scheme is the originator of the corrupt business practice, not the participants (as long as they are unaware of the illegal business practices). Secondly, a pyramid scheme differs from a multi-level marketing campaign, which offers legitimate products.

Money Laundering: What It Is and How to Prevent It

Learn how the prevention of money laundering has become an international effort

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Updated March 28, 2023

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What Is Money Laundering?

Money laundering is the illegal process of making large amounts of money generated by criminal activity, such as drug trafficking or terrorist funding, appear to have come from a legitimate source. The money from the criminal activity is considered dirty, and the process "launders" it to make it look clean.

Money laundering is a serious financial crime that is employed by white-collar and street-level criminals alike.1 Most financial companies today have anti-money-laundering (AML) policies in place to detect and prevent this activity.2

Key Takeaways

- Money laundering is the illegal process of making "dirty" money appear legitimate instead of ill-gotten.
- Criminals use a wide variety of money-laundering techniques to make illegally obtained funds appear clean.

- Online banking and cryptocurrencies have made it easier for criminals to transfer and withdraw money without detection.
- The prevention of money laundering has become an international effort and now includes terrorist funding among its targets.
- The financial industry also has its own set of strict anti-money laundering (AML) measures in place.

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Click Play to Learn How Money Laundering Works

How Money Laundering Works

Money laundering is essential for criminal organizations that wish to use illegally obtained money effectively. Dealing with large amounts of illegal cash is inefficient and dangerous. Criminals need a way to deposit money in legitimate financial institutions, yet they can only do so if it appears to come from legitimate sources.

The process of laundering money typically involves three steps: placement, layering, and integration.

- **Placement** surreptitiously injects the "dirty money" into the legitimate financial system.
- **Layering** conceals the source of the money through a series of transactions and bookkeeping tricks.
- In the final step, **integration**, the now-laundered money is withdrawn from the legitimate account to be used for whatever purposes the criminals have in mind for it.

Note that in real-life situations, this template may differ. Money laundering may not involve all three stages, or some stages could be combined or repeated several times.3

There are many ways to launder money, from the simple to the very complex. One of the most common techniques is to use a legitimate, cash-based business owned by a criminal organization. For example, if the organization owns a restaurant, it might inflate the daily cash receipts to funnel illegal cash through the restaurant and into the restaurant's bank account. After that, the funds can be withdrawn as needed. These types of businesses are often referred to as "fronts."

Banks are required to report large cash transactions and other suspicious activities that might be signs of money laundering.4

Variants of Money Laundering

One common form of money laundering is called smurfing (also known as "structuring"). This is where the criminal breaks up large chunks of cash into multiple small deposits, often spreading them over many different accounts, to avoid detection. Money laundering can also be accomplished through the use of currency exchanges, wire transfers, and "mules"—cash smugglers, who sneak large amounts of cash across borders and deposit them in foreign accounts, where money-laundering enforcement is less strict.

Other money-laundering methods include:

- Investing in commodities such as gems and gold that can be moved easily to other jurisdictions;
- Discreetly investing in and selling valuable assets such as real estate, cars, and boats;
- Gambling and laundering money at casinos;
- Counterfeiting; and
- Using shell companies (inactive companies or corporations that essentially exist on paper only).

What Is Electronic Money Laundering?

The Internet has put a new spin on the old crime. The rise of online banking institutions, anonymous online payment services, and peer-to-peer (P2P) transfers with mobile phones have made detecting the illegal transfer of money even more difficult. Moreover, the use of proxy servers and anonymizing software makes the third component of money laundering, integration, almost impossible to detect—money can be transferred or withdrawn with little or no trace of an Internet protocol (IP) address.

Money also can be laundered through online auctions and sales, gambling websites, and virtual gaming sites, where ill-gotten money is converted into gaming currency, then back into real, usable, and untraceable "clean" money.

The newest frontier of money laundering involves cryptocurrencies, such as Bitcoin. While not totally anonymous, they are increasingly being used in blackmail schemes, the drug trade, and other criminal activities due to their relative anonymity compared with more conventional forms of currency.5

AML laws have been slow to catch up to newer types of cybercrimes, since most of the laws are still based on detecting dirty money as it passes through traditional banking institutions and channels.

How to Prevent Money Laundering

Governments around the world have stepped up their efforts to combat money laundering in recent decades, with regulations that require financial institutions to put systems in place to detect and report suspicious activity. The amount of money involved is substantial. According to the United Nations Office on Drugs and Crime, global money-laundering transactions account for roughly $800 billion to $2 trillion annually, or some 2% to 5% of global gross domestic product (GDP), although it is difficult to estimate the total amount due to the clandestine nature of money laundering.3

In 1989, the Group of Seven (G-7) formed an international committee called the Financial Action Task Force (FATF) in an attempt to fight money laundering on an international scale. In the early 2000s, its purview was expanded to combating the financing of terrorism.6

The United States passed the Bank Secrecy Act in 1970, requiring financial institutions to report certain transactions, such as cash transactions above $10,000 or any others that they deem suspicious, on a suspicious activity report (SAR) to the Department of the Treasury.14 The information that the banks provide to the Treasury Department is used by the Financial Crimes Enforcement Network (FinCEN), which can share it with domestic criminal investigators, international bodies, or foreign financial intelligence units.7

While these laws were helpful in tracking criminal activity, money laundering itself wasn't made illegal in the United States until 1986, with the passage of the Money Laundering Control Act.8 Shortly after the Sept. 11, 2001, terrorist attacks, the USA Patriot Act expanded money-laundering efforts by allowing investigative tools designed for the prevention of organized crime and drug trafficking to be used in terrorist investigations.1

The Association of Certified Anti-Money Laundering Specialists (ACAMS) offers a professional designation known as a Certified Anti-Money Laundering Specialist (CAMS). Individuals who earn CAMS certification may work as brokerage compliance managers, Bank Secrecy Act officers, financial intelligence unit managers, surveillance analysts, and financial crimes investigative analysts.9

Why Is It Important to Combat Money Laundering?

Anti-money laundering (AML) seeks to deprive criminals of the profits from their illegal enterprises, thus eliminating the main motivation for them to engage in such nefarious activities. Illegal and dangerous activities, such as drug trafficking, people smuggling, terrorism funding, smuggling, extortion, and fraud, endanger millions of people globally and impose tremendous social and economic costs upon society. As the proceeds of such activities are legitimized by money laundering, combating money laundering may result in a reduction in criminal activity and hence a significant benefit to society.

What Is an Example of Money Laundering?

Say that cash has been earned illegally from selling drugs, and the drug dealer wishes to buy a new car with the proceeds. Because it is difficult and suspicious to try to purchase a vehicle entirely in cash, the dealer needs to launder the money to have it appear legitimate. The drug dealer also owns a small laundromat, a highly cash-intensive business. The cash from the drug deal is mingled with the laundromat's cash and then taken to a bank for deposit. Then, drawing a check from the laundromat's account, the dealer is able to buy the car without suspicion.

Another common form of money laundering in casinos is to buy chips from the casino with cash, and to receive checks in return for the chips from the casino, often without gambling at all or placing minimal bets.

How Can You Tell If Someone Is Laundering Money?

There are several red flags to look out for that may point to money laundering. Some of these include suspicious or secretive behavior by an individual around money matters, making large transactions with cash, owning a company that seems to serve no real purpose, conducting overly-complex transactions, or making several transaction just under the reporting threshold.

What Are Some Ways in Which Real Estate Is Used for Money Laundering?

Some common methods used by criminals for money laundering through real estate transactions include undervaluation or overvaluation of properties, buying and selling properties in rapid succession, using third parties or companies that distance the transaction from the criminal source of funds, and private sales.10

How Are Cryptocurrencies Being Used in Money Laundering?

The U.S. Financial Crimes Enforcement Network (FinCEN) noted in a June 2021 report that convertible virtual currencies (CVCs)—another term for cryptocurrencies—have grown to become the currency of choice in a wide range of online illicit activities.11

Apart from being the preferred form of payment for buying ransomware tools and services, online exploitative material, drugs, and other illegal goods online, CVCs are increasingly used to layer transactions and obfuscate the origin of money derived from criminal activity. Criminals use a number of money-laundering techniques involving cryptocurrencies, including "mixers" and "tumblers" that break the connection between an address (or crypto "wallet") sending cryptocurrency and the address receiving it.

Company Law

Company Law initiates with Act 43 of 1850, which was based on the English Companies Act of 1844, making it possible, for the first time, to incorporate and register a company without obtaining a royal charter. Under the Indian Act, the supreme courts in the presidency towns of Calcutta, Bombay and Madras were authorized to order the registration of unincorporated companies of partners associated under a deed containing a provision that the shares were transferable. The privilege of limited liability was not conferred upon by this Act, although a company was permitted to sue and be sued in its registered name.

In 1857, an act for the incorporation and regulation of joint stock companies and other associations either with or without limited liability of the members thereof was passed. But under this Act the privilege of limited liability was not extended to a company formed for the purpose of banking or insurance. This disability was removed by the Act of 1860, based on the English Companies Act of 1857. Then, following the English Companies Act of 1862, a comprehensive act was passed in India in 1866 for consolidating and amending the laws relating to the incorporation, regulation and winding up of trading companies and other associations. Between 1866 and 1913, various amendments in the Indian law were made following similar changes in England. The law relating to companies was re-enacted in a comprehensive form in the Companies Act of 1913. This Act was principally based on the English Companies (Consolidation) Act of 1908. Between 1908 and 1936, small amendments were made in the Act of 1913. The Indian Companies (Amendment) Act, 1936 introduced important provisions in the Act of 1913 in the light of the English Companies Act, 1929. This Amendment Act of 1936 also recognized for the first time the system of managing agencies in the subcontinent.

After the partition of India (1947), India passed a new comprehensive Act in 1956, based primarily on the English Companies Act, 1948 and the suggestions made in the Bhava Company Law Committee Report. During the Pakistan period a Company Law Commission was set up and it suggested amendments in 1962 in the light of the English and Indian amendments, and subsequently some amendments were made. The Securities and Exchange Ordinance, 1969 was the most important piece of legislation incorporating corporate activities during this period. It supplemented the Capital Issues (Continuance of Control) Act of 1947, giving extensive powers to the controller of capital issues.

After the emergence of Bangladesh a Company Law Reforms Committee was set up in 1979, comprising leading government servants, chartered accountants and lawyers. The committee made many recommendations for changes in company law but not until 1994 was a new comprehensive act passed by Jatiya Sangsad. The Securities and Exchange Commission Act of 1993 created the securities and exchange commission which oversees the issue of capital. Its primary purpose is to protect the investing public in corporate investments. It has been given extensive powers to make rules and regulations. Its responsibilities include those of the Controller of Capital Issues under the Acts of 1947 and 1969.

The essential elements of company law are the concepts of the company as a separate legal entity, irrespective of the closeness of the shareholders, investor protection, management of a company and the modes of winding up, and accounts and securities trading.

Artificial personality An incorporated company has an artificial personality distinct from its members. Corporate personality became an attribute of the normal joint stock company at a comparatively late stage, and it was not until the celebrated case of Salmon vs Salmon (1897) that the English House of Lords held that a company which was composed of seven members, all of them belonging to a family of husband, wife and children, was in the eyes of the law a different personality from its members so that a debenture created and issued in favour of the master of the house by the company would be a valid transaction. The courts, however, made exceptions to this rule of a separate personality of a company, especially in the fields of tax and fraud. But this principle still holds good and the Appellate Division of the Supreme Court in the case of Rujab Ali vs Mokarram Hossain (1977) held, while reconfirming that a company is a separate personality, that a shareholder has no direct interest in the property of a company.

The permanence of the general constitution of the company is secured by the memorandum of articles which cannot, save as provided by the act, be modified or altered. Neither can the articles authorise the company to do anything which is expressedly or implicitly forbidden by the act, e.g to pay dividends out of the capital, nor take away from the company or its members any rights conferred by the Act, i.e the right of a member to petition to wind up the company. Subject to these limitations the articles may contain such regulations for the management of the company as the original incorporators think fit. The articles constitute a network of rules regulating the affairs of the company. Each article is a rule for the regulation of the relations between the company and its shareholders and relations between the shareholders and the management. The articles may explain the memorandum in case of ambiguity.

The memorandum of association is the basic constitution of the company. The shares may be of the smallest nominal amount, and one share is enough to constitute membership. There is nothing in the act requiring that the subscribers shall be independent or unconnected, or have a substantial interest, or have a mind and will of their own, or that there shall be anything like a balance of power in the constitution of the company. If there are seven or, in the case of a private company, two members the law is complied with. The word 'person' includes a body corporate and a company may be a member in another company. Foreigners may be the shareholders subject to conditions laid down by the Bangladesh Bank and the Board of Investment. There is at present almost no restriction on foreigners becoming shareholders although the Securities and Exchange Commission may lay down conditions about the sale of their shares in case they buy quoted shares of primary issue.

The memorandum and articles of association form the constitution of the company and Section 26 prescribes that every member of the company is entitled to a copy of these documents on payment of a fee. To ensure that a member is not misled, the law further requires that any alteration of the memorandum and articles of association should be incorporated in those documents. The High Court Division had a verdict to this end that there is no provision in the companies act to correct clerical errors in the memorandum or articles of association, and these may be amended with the court's approval where needed.

Investor protection and accounts The concept of investor protection encompasses the notion that a company must have its accounts audited and place them at least once before the annual general meeting of shareholders (Section 183 of the Companies Act 1994). The Act further provides that the company shall furnish the informations that the balance sheet and the audited accounts of the company contain.

The law requires that a public company must publish a prospectus at the time of inviting subscriptions for shares or debentures in the company, and this document contains particulars of those in management, the project for which the money is required, and the general financial background of the company (Section 135 of the Act of 1994). If the company is listed in the stock exchange, the prospectus must be approved by the Securities and Exchange Commission. The act provides for investigation by the registrar of joint stock companies on its own or on complaint by shareholders holding one-tenth of the issued shares; but in practice this is a rare phenomenon in this country. However, Section 233 of the Act of 1994 specifically provides for protection of minority shareholders where the affairs of the company are being run in a manner prejudicial to the interests of a shareholder or the petitioners who must hold one-tenth of the issued share capital. The concept of minority protection is new, and judges are yet to lay down decisions which would really entrench the minority shareholders' position in the company. A shareholder may also petition the Court if he can show that it is just and equitable to wind up a company.

Management of a company A company is managed by its board of directors. The powers of the board are generally contained in the articles of association of the company, and where the powers are given to the board the general meeting has no authority to interfere in the management. The general body of shareholders has ultimate control in a sense that they may remove the board and replace them by a body of persons after their liking, but until then the board is the supreme managing body. The functions of the general meeting are generally confined to amending the memorandum and articles of association of the company, passing the annual balance sheets and the audited accounts of the company, electing directors in place of those who retire at the general meeting etc. The articles sometimes vest the managing director with plenary powers of management where the founding entrepreneur desires to keep control of the management, but the Act now provides that a managing director cannot be appointed for more than five years at a time, and his appointment must be ratified by the general meeting. In law, however, he remains a servant of the company and the board may dispense with his services, if necessary, on payment of compensation if there is a service contract.

Managing agents The country is witnessing the gradual elimination of an important feature of the management of the companies i.e. the managing agency system which was peculiar to the subcontinent and had been a direct legacy of the British economic colonization. The origin of the system lies in early British contacts with India. The servants of the east india company used to do business on their own, sometimes by appointing their own agents. The board of directors of the East India Company turned a blind eye to this, and very soon it became an accepted practice to have a business started by a managing agent. The function of these mercantile houses primarily consisted in importing British goods and exporting Indian goods and raw materials as agents of British agents or firms. In addition to their commercial or trading functions, the Calcutta mercantile houses also carried on financial activities and were responsible for introducing modern banking in India as an extension of trade in the European community there. These houses later frequently acted as investment bankers, and provided funds for the establishment and operation of indigo plantations, tea gardens and jute mills. Such was the importance of some of those mercantile houses that their managers were sometimes called 'merchant princes'.

The managing agency houses took advantage of the expanding English commerce and there was a mushrooming of business in India. The managing agency houses supplied directors to look after the British company's interests in India, and soon it became an invariable practice for newly formed companies to entrust their business in India to these managing agencies, who looked after the company's interests, while the investors and the board of directors in England quietly enjoyed the fruits of their enterprise without having to bother about management. In return, the managing agency houses were remunerated handsomely on the basis of fixed pay and commission. Thus the managing agency system is purely a product of British colonisation of India. Able Indian merchants followed in the footsteps of English mercantile houses; Parsis, Gujaratis and Marwaris promoted companies of which they became the managing agents.

The swadeshi movement of 1905 gave added impetus to indigenous business and many new companies were founded, and these were controlled by existing managing agencies. The managing agents rendered valuable services by providing money and technical know-how in an emerging market, and it was a common feature for an entrepreneur to call upon a managing agency for assistance. Strangely enough, not until 1936 did the legislature think it fit to insert provisions in the then Companies Act of 1913, which restricted the amount a managing agent may charge by way of commission. With the emergence of Bangladesh the entrepreneurs were able to start their own business, and this system is getting a natural death in this country. India still has a few managing agents.

Winding up A company may be wound up either voluntarily or compulsorily by the court. Usually the Company Bench of the High Court Division is crowded with petitioners who seek to wind up a company either on the ground that it is unable to pay back debts (Taka five thousand remaining unpaid for three weeks in spite of a notice to pay) or that it is just and equitable that the company should be wound up became of a deadlock in the management, fraud and oppression etc of shareholders. Generally if a company is wound up a liquidator is appointed to take over the assets of the company. The liquidator winds up the business of the company, pays the creditors, and distributes the surplus, if any, to the members. In practice the assets are sold at a pittance, and the creditor who petitioned the court for winding up the company ends up with nothing or very little.

Jurisdiction The High Court Division exercises special statutory jurisdiction to try matters under the Companies Act. Under Section 3 of the Companies Act, an application relating to the company should be made to the original side of the High Court Division. The case of Murshed

C.J and Abu Sayeed Chowdhury of Dacca Jute Mills Ltd vs Satish Chandra Banik and others (1967) are decided by way of special statutory jurisdiction conferred upon the Court by the Act itself. However, in the case of Md. Shamsuzzaman Khan vs MS Islam (1976) it was held that Section 3 of the Companies Act only gives certain jurisdiction to the High Court for resolution of the disputes under the Companies Act. If the nature of the dispute which is being litigated upon is entirely a civil dispute, it can only be decided by a competent civil court.

Securities laws The laws relate to shares and debentures traded in the stock exchanges. There are two stock exchanges in the country, in Dhaka and Chittagong. The Securities and Exchange Commission created under the Securities and Exchange Commission Act of 1993 is entrusted with the task of ensuring proper issuance of shares and debentures to protect the interests of investors in securities and to promote the development of, and to regulate, the capital and securities market. The history of securities laws in Bangladesh, as in other countries, follows the development of this branch of law in the United States of America.

After the great Wall Street crash of 1929 the Democrats promised sweeping changes in the laws relating to share markets and dealings, and two laws were passed in the USA in 1933 and 1934 creating the U.S Securities and exchange Commission which has earned since then a good reputation as a protector of the American economy. In Pakistan the Securities and Exchange Ordinance provided for banning of fraudulent activities in share trading, but the law was not applied seriously until 1996. [M Zahir]

A Brief Description of Company Directors from a Historical and the Legal Perspective of Bangladesh

Although company is regarded as a legal person yet it cannot manage itself like a natural person. Companies are managed by the directors. During the course of their duty, managers are bound to follow specific rules regulations and perform specific duties. A company's progress greatly depends on how efficiently the directors are handling its various affairs. And for this reason, directors are referred to as the brain of a company.[1] So, they have immense duty and responsibilities regarding governing a company and their failure to do so causes devastating consequences for a company. In this paper, an overview has been made on the historical development of the concept of directors, the nature of their duties and analysis has been made based on the various criticisms of the concept in the context of Bangladesh.

ORIGIN AND DEVELOPMENT

The existence of directors can be traced back to Dutch East India Companies. Gradually, countries around the world followed the Dutch model of an independent panel of directors to oversee companies.[2] Although, till the nineteenth century, general meeting was regarded as the supreme forum of company decisions, the notion drastically changed after the decision of the case ***Automatic Self-Cleansing Filter Syndicate Co Ltd v Cuninghame [1906] 2 Ch 34*** where it was held that if the article of association permits, then board of directors could be the highest decision-making organ of a company. Although such a new notion failed to receive general approval at first but things started to change when the House of Lords accepted such a view in the case ***Quin & Axtens v Salmon*** **[1909] AC 442.** Gradually legal systems around the world started following this decision and thus started the ascent of the board of directors in the decision-making process. However, the modern concept of supremacy of the board of directors was expressed in ***John***

Shaw & Sons (Salford) Ltd v Shaw [1935]2 KB 113 where the supremacy of article of association was established over the supremacy of shareholders and the trend of governing company through board members got approved. However, in the U.S.A, the concept was first introduced through the New York stock exchange in 1811 and gradually various banks and institutions started following it. Bangladesh inherited the concept from the British legal system. However, after the 1990's we have observed a trend to incorporate various American norms in the management process of the board of directors and so is still followed today.

DIRECTORS

Directors are the members of a panel that is appointed to manage and govern the company and to represent the shareholders. They are generally professional men hired to direct company affairs. However, they are not the servant of the company rather they are the officers. However, in the ***Lee v Lee's Air Farming Ltd.*** Case it was held that a director is entitled to work as an employee. Also, directors are regarded as agents of the company in the 1866 case of ***Ferguson v Wilson***. The general principle of agency is therefore applicable regarding the relationship of the directors with the company. Also, directors work as a trustee of the institution and he is responsible for a community system comprise of various interest groups like labour, consumers, the general public and the state. The directors constitute the brain of a company and in ***Fancton v Denville*** it was held that when the brain (directors) functions, the corporate is said to function.

In Bangladesh, **The Companies Act, 1994** provides that only natural persons can be appointed as directors. It also provides the obligation of having at least three directors for a public company and two for a private company. However, the act does not provide the duties of the director but from analysing various provisions and case laws along with principles of company law we could identify so.

DUTIES OF DIRECTORS

The various duties of directors can be classified into two categories: i) Statutory duties; ii) Duties of general nature.

Statutory Duties:

The statutory duties of directors begin from the date of incorporation and ends when the company is liquidated. **The Companies Act, 1994** provides in **section 96** that every director has to attend the board meeting. Also, **section 97** states the duty of directors to uphold qualification share. In the case of Bankruptcy, a director must leave his office under **section 99**. Furthermore, it is a director's duty not to enter selling contracts of company goods and materials without the approval of the board of directors. Managing directors have a duty not to act as managing directors of more than one company. Also, they have to maintain a term not exceeding five years. Also, **section 114** suggests that directors have a duty not to take any compensation for his loss of office due to the transfer of all or any shares. Section 111 to 113 provides instances when the director cannot take money indirectly. Again, if a director has any interest in case of entering any contract on behalf of the company, he must disclose so under section 130. Also, section 131 provides his duty not to vote in favour of any contract that might be good for his interest. The director must ensure the delivery of prospectus to the registrar for registration. Directors have also the duty to prepare and send a copy of the statutory report to every shareholder 21 days before the statutory report. **Section 39** also make it the duty of a director to deliver share certificate of all the shares within 90 days of allotment. Calling an extra-ordinary general meeting is another duty of a director under

section 87. Ensuring payment of dividends and making a declaration of solvency also constitutes the statutory duty of the directors.[3]

Duties of general nature

The general duties of directors include those which has been created by various case laws and the principle of company law. It includes the fiduciary relation of directors with the company. In the ***Avaling Barford v Perion Ltd*** case duty not to breach trust has been regarded as one of the duties of directors. Again, not to do any personal gain causing pecuniary losses of the company is another general duty of a director established in ***Albion Steel and wire Co. v Martin*** case. Furthermore, the directors while in office have a duty not to engage in trading in corporate control and earn profit. Also, he has a duty not to misuse corporate information. In the 1925 case of ***City Equitable Fire Insurance Co*** the duty of directors to:

1. Act honestly,
2. Exercising reasonable diligence,
3. Liability of mere errors of judgement,
4. Attending board meetings.

Joint Stock Discount Co. v Brown case also provided the duty of directors not to be negligent. ***Cobb v Becke*** case provides *the "delegate non protest delegate"* principle which means directors have a duty not to delegate their duties to other officials. Furthermore, in case of fraud by any director, such director shall be personally liable for his default. In ***Aberdeen Railway Ltd v Blaikie*** disclosing any interest in any transaction has been held as a duty of a director. The benefit gained in the case of non-disclosure can be claimed by the company. So, directors have a huge amount of duty in a company.

ANALYSIS

Despite having so many duties regarding maintaining a company, the role of directors is not free from scrutiny. Firstly, critics often indicate the overshadowing of general shareholders by the directors. The shareholders are supposed to be the owner of the company. So, theoretically, they should have enough power to express their mind regarding governing the company. However, the directors are more involved in doing so thus making the shareholder a mere titular owner.[4] Again, directors are some of the highest-paid persons in the job market. It creates an imbalanced capitalistic situation which greatly contributes toward disparity. There are reported incidents around the world where the wage of the worker does not get a raise very often but the directors are bagging more and more every year.[5] Also, often there are incidents of dishonesty and corruption by the directors that not just only affects the company but also affects the country and economy in great. We have seen so in various cases of corruption by the various banks in Bangladesh.

CONCLUSION

Although, the directors are not above criticisms their role in respect of managing and governing the company cannot be undermined in today's world. Directors are the most efficient persons to run a company as they have technical knowledge and skills regarding so in contrast to the shareholders. Furthermore, various legal and institutional mechanisms are there to prevent any kind of irregularities on part of the directors. That's why the directors are here for centuries to manage the companies and they are doing so with utmost efficiency. Therefore, it can be said that the directors play the most vital role in respect of managing and governing companies in today's world and there is no alternative to them.[**Mashrur Rahman Mahin],**

Institutions

Banking and Non-Banking Financial Institutions

There are two types of financial institutions: banking and non-banking. This article shows the differences between banking and non-banking financial institutions.

Table of Content

- What are Banking Financial Institutions?
- Types of Banking Financial Institutions
- What are Non-Banking Financial Institutions?

There are two main types of financial institutions: banking and non-banking. Banking institutions include commercial banks, savings and loan associations, and credit unions. Non-banking financial institutions include insurance companies, pension funds, and hedge funds. So what sets these two groups apart? This article will discuss the key differences between banking and non-banking financial institutions!

What are Banking Financial Institutions?

Banking financial institutions are in the business of taking deposits from the public and making loans. In addition, they provide other services such as investment banking, foreign exchange, and safe deposit boxes. These institutions are heavily regulated by governments to protect consumers and ensure that the banking system is stable.

Types of Banking Financial Institutions

There are two types of banking financial institutions: depository and non-depository.

- Depository institutions include banks, savings and loans associations, credit unions, and mutual savings banks
- Non-depository institutions include finance companies, insurance companies, and pension funds

What are Non-Banking Financial Institutions?

Non-banking financial institutions (NBFCs) are companies that provide financial services such as lending, insurance, and investment banking but that are not regulated as banks. This means that they have a different set of rules and regulations to follow.

Types of Non-Banking Financial Institutions

There are a few different types of non-banking financial institutions, which include:

1. Insurance companies: These companies sell insurance policies to individuals and businesses. The policies can provide coverage for things like car accidents, medical expenses, or property damage.
2. Investment banks: These banks help companies raise money by issuing and selling securities. They also provide advice on mergers and acquisitions, and they trade stocks and bonds.
3. Pension funds: These funds provide retirement income for workers. The money is invested in stocks, bonds, and other assets.
4. Mutual funds: These funds pool money from investors and invest it in a portfolio of stocks, bonds, and other assets.
5. Hedge funds: These funds are private investment partnerships that use a variety of investment strategies to make money.
6. Private equity firms: These firms invest in private companies and help them grow. They may also take the companies public.
7. Venture capital firms: These firms invest in early-stage companies with high growth potential.

Each of these non-banking financial institutions serves a different purpose, but they all work towards the ultimate goal of providing funding for businesses and individuals.

How do Non-Banking Financial Institutions differ from Banks?

There are a few key ways that non-banking financial institutions differ from banks.

1. Non-banking financial institutions are not regulated by the government like banks are. This means that they are not subject to the same laws and regulations.
2. Non-banking financial institutions do not take deposits from customers. Instead, they raise money by selling securities or borrowing money.
3. Non-banking financial institutions are not required to maintain a reserve ratio like banks are. This ratio is the percentage of deposits that a bank must keep in reserve in case of withdrawals.
4. Non-banking financial institutions are not subject to the same capital requirements as banks. This means that they are not required to have a certain amount of money in the reserve to protect against losses.
5. Finally, non-banking financial institutions are not subject to the same lending restrictions as banks. This means that they can lend money to anyone they choose, without having to follow the government's guidelines.

These differences between banks and non-banking financial institutions can make it easier for businesses to access funding. However, it is important to remember that non-banking financial institutions are not regulated in the same way as banks, so it is important to do your research before choosing one.

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Act NO. 14 of 1991

An Act made to make provisions for banking companies

Whereas it is expedient to make provisions for banking companies therefore the following Act is hereby passed:

Chapter I

Preliminary

/ **1. Short title.-** (1) This Act may be called the Banking Companies Act, 1991. (2) It shall be deemed to have come into force on 14th February 1991.

2. Application of other Acts.- The provisions of this Act shall be in addition to, and not, save as hereinafter expressly provided, in derogation of, the Companies Act, 1913 (VII of 1913) , and any other Act for the time being in force.

3. Limited application of this Act to co-operative banks and other financial institutions. Nothing in this Act shall apply to a co-operative bank or any other financial institution registered under the Co- operative Societies Ordinance, 1985 (Iof 1985) or any other Act for the time being in force relating to co- operative banks:

Provided that the Bangladesh Bank may carry out inspections of and issue directions to co-operative banks as prescribed for banking companies under section 44 and 45 of this Act.

4. Power to suspend operation of this Act.- (1) The Government if, on a representation made by the Bangladesh Bank in this behalf it is satisfied that it is expedient so to do, may by notification in the official Gazette suspend for at most 60 days the operation of all or any of the provisions of this Act in relation to any specified banking company. (2) The Government may, by notification in the official Gazette, extend from time to time, the period of any suspension under sub-section (1) for such period or periods, not exceeding 60 days at one time, as it thinks fit, so however that the total period does not exceed one year. (3) Notifications issued under this section shall be submitted to the national parliament as follows:

a) if it is in session, within 10 days of the issue of the notification, and b) if it is not in session, within 10 days of the beginning of the session following the issue of the notification.

5. Definitions.- In this Act, unless there is anything repugnent in the subject or context,-

a) "approved securities" means securities in which a trustee may invest money under clause (a), clause (b), clause (bb), clause (c) or clause (d) of Section 20 of the Trust Act, 1881 (II of 1882) and for the purpose of section 13 (3) includes such securities as the Government may, by notification in the official Gazette, declare to be approved securities for the purpose of this section. b) "company" means any company which may be wound up under the Companies Act; c) "Companies Act" means Companies Act; 1913 (VII of 1913); d) "demand liabilities" means liabilities which must be met on demand; e) "secured loan or advance" means a loan or advance made on the security of assets the market value of which is not at any time less than the amount of such loan or advance, and "unsecured loan or advance" means a loan or advance not so secured, or that part of it which is not so secured; f) "scheduled bank" has the same meaning as in the Bangladesh Bank Order (P. NO. 127 of 1972) Article 2 (j); g) "debtor" means-

1. any person, company or organisation accepting deposits of money on the basis of shared win and loss, or
2. any person, company or organisation taking advantage of financial opportunities on the basis of shared win and loss, purchase or lease on rent, or in any other way;

h) "new bank" means any bank denominated in the Bangladesh Banks (Nationalisation) Order, 1972 (P. No. 26 of 1972); i) "creditor" means-

1. any person, company or organisation accepting deposits of money on the basis of shared win and loss, or
2. any company or financial organisation granting financial opportunities on the basis of shared win and loss, purchase or lease on rent, or in any other way;

j) "private company" has the same meaning as in the Companies Act; k) "Bangladesh Bank" means Bangladesh Bank established under the Bangladesh Bank Order, 1972 (P. No. 127 of 1972); l) "rule" means a rule made under this Act;

Chapter II

Business of Banking Companies

/

7. Business of Banking Companies.- (1) In addition to the business of banking, a banking company may engage in all or any of the following forms of business, namely:-

a) the borrowing, raising or taking up of money; b) the lending or advancing of money either upon or without security; c) the drawing, making, accepting, discounting, buying, selling, collecting and dealing in bills of exchange, hoondees, promissory notes, coupons, drafts,bills of lading, railway receipts, warrants, debentures, certificates, participation term certificates, term finance certificates, musharika certificates, modareka certificates, such other instruments as may be approved by the Bangladesh Bank, and such other instruments and securities whether transferable or negotiable or not; d) the granting and issuing of letters of credit, traveller's checks, and circular notes; e) the buying, selling and dealing in gold and silver coins and coins of other metals; f) the buying and selling of foreign exchange including foreign bank notes; g) the acquiring, holding, issuing on commission, underwriting and dealing in stocks, funds, shares, debenture stock, obligations, participation term certificates, term finance certificates, musharika certificates, modareka certificates and such other instruments and investments of any kind as may be approved by the Bangladesh Bank; h) the purchasing and selling of bonds, scrips or other forms of securities, participation term certificates, term finance certificates, musharika certificates, modareka certificates and, on behalf of the constituents of the Bangladesh Bank or others, such other instruments as may be approved by the Bangladesh Bank; i) the negotiating of loans and advances; j) the receiving of all kinds of bonds or other valuables on deposit or for safe custody or otherwise; k) providing vaults for the safety of the deposits; l) the collecting and transmitting of money against securities; m) acting as agents for the Government, local authorities or any other person; n) the carrying on of agency business of any description including the clearing and forwarding of goods and acting as a law agent on behalf of customers, but excluding the business of a managing agent or treasurer of a company; o) contracting for public and private loans and negotiating and issuing the same;

p) the effecting, insuring and underwriting of shares, stocks, debentures, debenture stock of any company, corporation or association and the lending of money for the purpose of any such issue; qu) the carrying on and transacting of every kind of guarantee and indemnity business; r) the buying and acquiring of any kind of property including merchandise, patents, designs, trademarks and copyrights,in addition to, at the normal business period of a bank, such or similar transactions as-

1. repurchase by the seller, or
2. selling in the way called purchase on rent, or
3. repayment of outstanding rates, or
4. leases, or
5. sharing out of revenues, or
6. financing in any other way;

s) bringing into possession any property which may satisfy or partly satisfy any of the claims of the banking company and the managing and borrowing of such property; t) acquiring, holding and managing of any property or any right,title or interest in any such property which may form the security or part of the security for any loans or advances or which may be connected with any such security; u) undertaking and executing trusts; v) undertaking the administration of movable and immovable property as executor, trustee or otherwise; w) for the benefit of employees or ex-employees of the banking company or the dependants and connections of such persons-

1. establishing and supporting, or aiding in the establishment and support of associations, institutions, funds, trusts or any other establishment;
2. granting pensions and allowances;
3. making payments toward insurance;

4. subscribing to any exhibition or any object generally useful;
5. guaranteeing money for all these purposes.

x) the acquisition, construction, maintenance and alteration of any building or works necessary or convenient for the purpose of the banking company; y) selling, improving, managing, exchanging, leasing, mortgaging or otherwise transferring or turning into acount or otherwise disposing of all or any part of the property or rights of the banking company; z) acquiring and undertaking the whole or any part of the business of any person or company, when such business is of a nature enumerated or described in this subsection; aa) doing all such other things as are incidental or conducive to the promotion or advancement of the business of the company; ab) any other form of business which the Government may, by notification in the official

11. Prohibition of employment of managing agents and restrictions on certain forms of employment.- (1) No banking company-

a) shall employ or be managed by a managing agent; or b) shall employ or continue the employment of any person-

i) who is, or at any time has been, adjudicated insolvent, or has suspended payment, or has compounded with his creditors, or who has been convicted by a criminal court of an offence involving moral turpitude; ii) whose remuneration or part of whose remuneration takes the form of commission or of a share in the profit of the company: Provided that nothing contained in subclause (ii) shall apply to the following commissions and bonuses given by a banking company, namely- a) any bonus given in pursuance of a settlement or award arrived at or made under any law relating to industrial disputes or in accordance with any scheme framed by a concerned banking company or in accordance with the usual practice prevailing in the banking business; or b) any commission given to any broker (including guarantee broker), cashier, contractor, clearing and forwarding agent,auctioneer or any other person employed by the banking company under a contract otherwise than as a regular member of the staff of the company; or iii) whose remuneration is excessive in the view of the Bangladesh Bank.

Explanation 1.- For the purpose of this sub-clause "remuneration" shall include wages, fees and advantages in addition to the wages given by a banking company to whatever person, but not money or allowances given in order to meet the expenses arising normally from the fulfilment of one's duties. **Explanation 2.-** For the purpose of this sub-clause the Bangladesh Bank may, in order to decide whether a remuneration is excessive or not, take into consideration the following items, namely:-

a) the financial solvency of the banking company, the extension of its activities, the size of its business and the general tendency of its earning capacity; b) the number of its branches and offices; c) the competency, age and experience of the person receiving the remuneration; d) the amount of the remuneration given to any other person employed in the banking company or to persons employed in similar positions in other banking companies in about the same condition; e) the interest of its depositors;

c) shall be managed by any person-

i) who is a director of any other company not being a subsidiary company of the said banking company or a company registered under section 26 of the

Companies Act, except with the previous approval of the Bangladesh Bank; or ii) who is engaged in any other business or vocation; or iii) who had a contract with the company for a period exceeding five years at any one time: Provided that any contract with the company for its management may be renewed or extended for a further period not extending five years at a time if the directors of the company so decide: Provided further that nothing in this clause shall apply to a director, other than the managing director, of a banking company by reasons only of his being a director.

(2) Where a person holding the office of a chairman, director, manager or chief executive officer, by whatever name called, of a banking company is found by any court or tribunal or other authority to have contravened the provision of any law and the Bangladesh Bank is satisfied that the contravention is of such a nature that the association of such person with the banking company will be detrimental to the interests of the banking company or its depositors or otherwise undesirable, the Bangladesh Bank may make an order that that person shall cease to hold the office with effect from such date as may be specified therein; and thereupon his office shall, with effect from the said date, become vacant. (3) Any order made under sub-section (2) may provide that the said person shall not, without the permission of the Bangladesh Bank, in any way, directly or indirectly, be concerned with, or take part in the management of the banking company or any other banking company for such period, not exceeding five years, as may be specified in the order. (4) No order under subsection (2) shall be made unless the concerned person has been given opportunity of making a representation to the Bangladesh Bank against the proposed order: Provided that it shall not be necessary to give any such opportunity if, in the opinion of the Bangladesh Bank, any delay would be detrimental to the interests of the banking company or its depositors. (5) Any decision or order of the Bangladesh Bank made under this section shall be final.

12. Restrictions on removal of records and documents. -No banking company shall remove from its head-office or any of its branches, whether they are at the time being functioning or not, any of its records or documents relating to its business to a place outside Bangladesh, without the prior permission in writing of the Bangladesh Bank. **Explanation.** - In this section-

a) the term "records" means any electronically or otherwise preserved ledger, day-book, cash book, account book and all other books used in the business of a banking company; and b) the term "document" means any electronically or otherwise preserved voucher, cheque, bill, pay order, security for an advance and any other document supporting entries in the books of, or claims by or against, a banking company.

13. Minimum paid up capital and reserves.- (1) Unless it has paid-up capital and reserves of such

(6) If any dispute arises in computing the amount of the paid-up capital and reserves of any banking company, the decision of the Bangladesh Bank thereupon shall be final. (7) If the Bangladesh Bank is convinced that any bank fails to preserve the minimum revised capital and reserves in accordance with this section, the banking company concerned shall be forced to pay such fine as may be prescribed.

14. Regulation of paid-up capital, subscribed capital and authorized capital and voting rights of share-holders. -(1) No banking company incorporated in Bangladesh, except new banks and special banks, shall commence its business in Bangladseh unless it satisfies the following conditions, namely:-

a) that its subscribed capital is no less than one half of the authorized capital; b) that its paid-up capital is no less than one half of the subscribed capital; c) that if the capital is increased it complies with the conditions prescribed in clause a) and b) within such period, not exceeding two years, as the Bangladesh Bank may determine; d) that its capital consists of ordinary shares only; e) that, subject to the provisions contained in clause f), the voting rights of any of its shareholders are proportionate to the contribution made by him to the paid-up capital of the company; f) that the voting rights of any one shareholder, except those of the Government, do not exceed five per cent of the total voting rights of all the shareholders.

(2) Notwithstanding anything contained in any law for the time being in force or in any contract or instrument, no suit or other proceeding shall be filed against any person registered as the holder of a share in a banking company other than a new or special bank on the ground that the title to the said share has been vested in a person other than the registered holder: Provided that nothing contained in this subsection shall apply in case that a suit or other proceeding is filed by one of the following persons, namely:-

a) any person having obtained the transfer of a share from a registered shareholder in accordance with the laws relating to the transfer of shares; b) any other person acting on behalf of a minor or lunatic person on the ground that he holds as the registered holder the share on behalf of the minor or lunatic.

(3) Every chairman, managing director, director or chief executive officer, by whatever name called, and all of his family members, of any banking company except new and special banks shall transmit to the Bangladesh Bank through that banking company accounts containing full particulars of the extent and value of his holding of shares, assets and obligations, whether directly or indirectly, in the said banking company or any other company and of any change in the extent of such holding or any variation in the rights and duties attaching thereto and such other information relating to those shares, assets and obligations as the Bangladesh Bank may, by order, require and in such form and at such time as may be specified by the Bangladesh Bank in the order.

15. Election of new directors.- (1) The Bangladesh Bank may, by order, require any banking company except new and special banks to call a general meeting of the company within two months from the date of the order or within such further time as the order may allow in this behalf, to elect in accordance with the provisions of this ordinance new directors. (2) Every director elected under subsection (1) shall hold office until the date up to which his predecessor would have held office, if the election had not been held. (3) Any election duly held under this section shall not be called in question in any court. (4) The Bangladesh Bank may, by general order, make provisions to the effect that no banking company except new and special banks shall appoint its managing directors or chief executive officers, whatever be the name of the office, without the previous approval of the Bangladesh Bank and no managing director or chief executive officer appointed in this way shall be removed from his office, acquitted or dismissed without the previous approval of the Bangladesh Bank.

16. Restriction on the period of office of directors.- (1) No person except the chief executive officer of a banking company, by whatever name called, shall hold the office of a director for more than six years in continuance. **Explanation.-** In this subsection a period of six years in continuance shall be equivalent to a interval of no less than three years. (2) No person having hold an office for a period of six years without cessation according to subsection (1) shall be again eligible as director unless three years have passed since the end of the said period.

17. Vacancy of the office of a director.- (1) If any director of an banking company fails to-

a) pay advances or loans accepted by him or instalments or interests on that advances or loans, or b) pay the money he is bound to for any security, or c) accomplish any duty to be accomplished by him and the responsibility for which he has taken on in writing,

and the said banking company gives him order through a notice by the Bangladesh Bank to pay the said advances, loans, instalments, interests or money or to accomplish the said duties and he fails to accomplish those duties and payments within two months after receipt of the order, in that case the office of director shall be vacant beginning from the expiry of the said term. (2) Whoever has received a notice under sub-section (1) may, within thirty days after receipt of the notice, send his statements on the subject in question, if any, in written form to the Bangladesh Bank, and a copy thereof to the banking company who issued the notice. (3) The decision of the Bangladesh Bank on any statement under subsection (2) shall be final.

18. Some rules concerning benefits for directors.- (1) Notwithstanding anything contained in any other Act or memorandum of association, no banking director shall take from the bank any financial or other privilege except the regular fees for participation in the meetings of the Executive Board of the bank or money determined by the Board for the performance of any duty considered important for the

actually been capitalised or otherwise accounted for as a loss, b) in any case where adequate provision for the depreciation in the value of its investments in shares, debentures or bonds (other than approved securities) has been made to the satisfaction of the auditor of the banking company, c) in any case where adequate provision for bad debts has been made to the satisfaction of the auditor of the banking company.

23. Restrictions on the employment of common directors.- (1) No banking company incorporated in Bangladesh, except new and special banks, shall have, without the permission of the Bangladesh Bank, as a director any person who is-

a) a director of any other banking company, or a director of an institution lending money without being engaged in the business of banking; b) a director of companies which are entitled to exercise voting rights in excess of twenty per cent of the total voting rights of all the shareholders of the banking company: Provided that the provisions of this subsection do not apply to directors appointed by the Government.

(2) If immediately before the commencement of this Ordinance any person holding office as a director of a banking company is also a director of companies which are entitled to exercise voting rights in excess of twenty per cent of the total voting rights of all the shareholders of the banking company, he shall, from such commencement within such period as the Bangladesh Bank may specify in this behalf-

a) either resign his office as a director of the banking company, or b) choose such companies as are not, on the strength of their shares of the said banking company, entitled to exercise voting rights in excess of twenty per cent of the total voting rights of all the shareholders of the banking company as companies in which he wishes to continue to hold the office of a director and resign his office as a director in the other companies.

24. Reserve Fund.- (1) Every banking company incorporated in Bangladesh shall create a reserve fund and if the amount in such fund together with the amount in the share premium account is not less than its paid-up capital or the amount of the premium settled from time to time in this behalf for any banking company by the Bangladesh Bank, shall, out of the profit as disclosed in the profit and loss account prepared under section 38 and before any money is transferred to the Government or declared as profit, transfer to the reserve fund a sum equivalent to not less than twenty per cent of that profit. (2) Where a banking company appropriates any money from the reserve fund or the share premium account for any purpose, it shall, within twenty-one days from the date of such appropriation, report the fact to the Bangladesh Bank: Provided that the Bangladesh Bank may extend the period for such report or condone any delay in the making of such report.

25. Cash Reserve.- (1) Every banking company, not being a scheduled bank, shall maintain in Bangladesh by way of cash reserve in cash with itself, or with the Bangladesh Bank or its agent, or both banks in equal parts, a sum equivalent to not less than five per cent. of its time and demand liabilities: Provided that the Bangladesh Bank may, in any particular case, change, by notification in the official Gazette and subject to the conditions settled therein in this behalf, the requirements relating to the cash reserve or repeal, on previous approval by the Government, such requirements. **Explanation.-** (1) For the purpose of this section "liability" shall not include the paid-up capital or the cash reserves or the credit balance in the profit and loss account of the banking company or the amount of any loan taken from the Bangladesh Bank. (2) Every banking company, not being a scheduled bank, shall, if the Bangladesh Bank requires any information regarding funds reserved in accordance with the provisions of subsection (1), submit a report containing that information and signed by two officers of the said company to the Bangladesh Bank. (3) Every banking company failing to submit a report in accordance with the provisions of subsection (2) shall be punishable by the Bangladesh Bank with a fine of no more than 2500 Takas for every day it fails so to do. (4) If a report submitted under subsection (1) shows that the banking company which submitted the report maintained an amount of cash less than the amount determined under subsection (1) at the close of any working day preceeding the submission of the report, the Bangladesh Bank may order the banking company to pay it for those days a penal interest on the said deficit exceeding by three per cent the bank rate, and if a subsequent report shows again that the said banking company maintained an amount of cash less than the amount determined under subsection (1) at the close of any working day preceeding the day determined for the submission, the Bangladesh Bank may order the banking company to pay it for those days a penal interest on the said deficit exceeding by five per cent the bank rate. (5) If a banking company has been ordered on the basis of a report submitted by itself to pay a penal interest exceeding by five per cent the bank rate under subsection (4) and if a subsequent report shows that it maintains an amount of cash less than the amount determined under subsection (1), the Bangladesh Bank may order the said banking company not to accept new deposits from such date as the Bangladesh Bank may determine, and if the said banking company accepts any deposit in disregard of that order, the Bangladesh Bank may inflict a fine of no more than 5000 Takas on it for every day it does so, to be paid to the Bangladesh Bank. (6) Any fine inflicted under this section shall be realised within such period as the Bangladesh Bank may determine and if it has not been realized within the said period, it shall be recoverable as public demand.

26. Subsidiary Companies.- (1) A banking company shall not form any subsidiary company except a subsidiary company formed for one of the following purposes, namely:-

a) the undertaking and executing of trusts; b) the undertaking of the administration of any property as executor, trustee or otherwise; c) the provision of safe vaults in order to provide for the security of the deposits; d) the undertaking of the business of banking in accordance with the directions of the shariat;

ii) any member of the family of any of its directors; iii) any commercial institution or private company in which the banking company itself, or any of its directors or any member of the family of any of its directors is involved as director, owner or shareholder; iiii) any public limited company which is in some way or other controled by the company itself, or any of its directors or any member of the family of any of its directors, or the shares of which are held by any of the said persons to such an extent as to give it control of no less than twenty per cent of the voting rights.

(2) No banking company shall give to any of the following persons or institutions any loan or advance without the approval of the majority of the directors, excluding the director concerned,-

a) any of its directors; or b) any person, commercial institution or company in which any of the directors of the said banking company is interested as partner, director or guarantor.

Explanation.- For the purpose of this subsection "director" shall include the director's wife, husband, father, mother, son and daughter. (3) No banking company shall, without the previous permission in writing of the Bangladesh Bank, give to any person or institution, directly or indirectly, any benefit the aggregate value of which exceeds-

a) 15 per cent of the total capital of the said banking company; or b) 25 per cent of the total capital of the said banking company where the security of the said benefits has been provided by such financial securities as might be easily put on the market for sale.

Explanation.- (1) "Benefit" shall mean any loan, advance or any other loan benefit, or financial guaranties or any such obligation as any banking company has taken on in behalf of any person or institution; and (2) "Total capital" shall mean paid-up capital and reserve fund including those various kinds of security which are in accordance with the provisions of the Bangladesh Bank under section (13), certificates of indebtedness, deposits, obligations etc..

(4) Every banking company shall, before the close of the month to which the report relates, submit to the Bangladesh Bank a report in the prescribed form and manner, and in the said report the following particulars shall be mentioned-

a) all loans and advances granted by it to companies, private as well as public, in which the banking company or any of its directors is interested as director; and b) all loans and advances granted by it to public companies in which the banking company or any of its directors is interested as managing agent or guarantor.

(5) If on examination of any report submitted under subsection (4) it appears to the Bangladesh Bank that any loans or advances referred to in that subsection have been granted to the detriment of the interests of the depositors of the banking company, the Bangladesh Bank may, by order in writing, prohibit the banking company from granting any such further loans or advances or impose restrictions on the granting of such loans or advances, and may direct the banking company to secure the repayment of loans or advances granted in this way within such time as may be specified in the order.

28. Restrictions on the respite of loans.- (1) No banking company shall, without the previous approval of the Bangladesh Bank, grant respite of loans taken from it by any of the following persons or institutions,-

a) any of its directors, and his family members; b) a commercial institution or company in which any director of the banking company is interested as landowner, co-director, managing agent; and c) any such person in which any director of the banking company is interested as partner or landowner.

(2) Any respite of loans in disregard of the provisions of subsection (1) shall be illegal, and whoever is responsable for such a respite shall be punishable with imprisonment for no more than three years or a fine of no more than thirty thousand Takas or both.

29. Power of the Bangladesh Bank to control the giving of advances.- (1) Whenever the Bangladesh Bank is satisfied that it is necessary or expedient so to do, it may determine the policy in relation to advances to be followed by banking companies generally or by any banking company in particular and when the policy has been so determined, all banking companies or the banking company concerned shall be bound to follow the policy so determined. (2) Without prejudice to the generality of the power vested in the Bangladesh Bank under subsection (1), the Bangladesh Bank may give directions, strictly to be complied with, to banking companies either generally or to any banking company or group of banking companies in particular with regard to the following items,-

a) the upper limit of the loan to be given; b) the ratio to be maintained between the total amount of an advance and loans of little amount or of other kind; c) the purposes for which advances may or may not be given; d) the upper limit of advances to be given to any banking company or any group of banking companies or person or assembly of persons; e) the limit of interests on secured advances and advances; and f) the rate of interest to be charged on advances.

(3) Whenever a banking company fails to comply with any direction referring to a subject mentioned in clause (a) and (b) of subsection (1), the Bangladesh Bank may order that banking company to deposit at

to the company as the Government or law of Bangladesh grants to companies incorporated in Bangladesh, and that the company complies with all the provisions of this Act applicable to companies incorporated outside Bangladesh.

(5) The Bangladesh Bank may cancel a licence granted to a banking company under this section on account of the following reasons, namely:-

a) if the company ceases to carry on banking business in Bangladesh; b) if the company at any time fails to comply with any of the conditions imposed upon it under subsection (1); or c) if at any time that company fails to fulfil any of the conditions referred to in subsection (4):

Provided that before cancelling a licence under clause b) and c) , the Bangladesh Bank, unless it is of opinion that the delay will be prejudicial to the interests of the company's depositors or the public, shall grant to the company on such terms as it may specify, an opportunity of taking the necessary steps for complying with or fulfilment of the provisions of those clauses. (6) Any banking company aggrieved by a decision cancelling a licence under this section may, within thirty days from the date on which the decision of the Bangladesh Bank is communcated to it, appeal to the Government. (7) The decision of the Government where an appeal has been preferred to it under subsection (6) or of the Bangladesh Bank where no appeal has been preferred shall be final.

32. Restrictions on opening of new, and transfer of existing places of business.- (1) Without the previous permission in writing of the Bangladesh Bank-

a) no banking company shall open a new place of business in any part of Bangladesh or change the location of an existing place of business; and b) no banking company incorporated in Bangladesh shall open a new place of business outside Bangladesh or change the location of an existing place of business outside Bangladesh.

(2) The provisions of subsection (1) shall not apply to the opening for a period not exceeding one month of new places of business for the purpose of offering bank services temporarily on the occasion of exhibitions, melas, comferences or other like occasions: Provided that information of such opening is given to the Bangladesh Bank within one week of the date of opening. (3) The Bangladesh Bank may, before giving the permission referred to in subsection (1) to any banking company, require to be satisfied by an inspection under section 44 or otherwise regarding any subject of that banking company.

33. Maintenance of liquid assets.- (1) Every banking company shall maintain in Bangladesh in cash,

gold or unencumbered approved securities valued at a price not exceeding the current market price, an amount which shall not at the close of business on any day be less than the percentage of its time and demand liabilities the Bangladesh Bank determines from time to time. **Explanation.-** For the purposes of this section, "unencumbered approved securities" shall include the approved securities which the banking company has lodged with another institution for an advance or any other kind of credit; but this definition shall include only such amount of the value of the securities as has not been drawn. (2) In computing the amount referred to in subsection (1), amounts deposited by any banking company incorporated outside Bangladesh with the Bangladesh Bank under subsection (3) of section 13, amounts deposited by any banking company within Bangladesh in current account with the Bangladesh Bank or any of its agents or both and amounts maintained with the Bangladesh Bank as balancing deposits shall be deemed to be cash. (3) The Bangladesh Bank shall determine the method of ascertaining assets and liabilities and the ratio of assets to be maintained continually. (4) Every banking company shall, before the close of the month to which the report relates, submit to the Bangladesh Bank a monthly report in the prescribed form and manner, which shall contain the following informations, namely:-

a) its assets maintained in accordance with this section; and b) its time and demand liabilities in Bangladesh at the close of each Thursday during the month, and if any Thursday is a public holiday under the Negotiable Instruments Act, 1881 (XXVI of 1881), at the close of the proceeding working day.

(5) Where it appears to the Bangladesh Bank that a banking company at any time fails to maintain liqiuid assets to the extent determined, that banking company shall be bound to pay for the deficit in the mentioned assets a fine in form of the highest interest rate taken by the Bangladesh Bank for the granting of loans.

34. Assets in Bangladesh.- (1) On the close of any working day the assets in Bangladesh of every banking company shall not be less in value than such amount of its present time and demand liabilities as the Bangladesh Bank may prescribe by law: Provided that the percentage so determined shall under no circumstances exceed eighty per cent of those liabilities. (2) Every banking company shall, before the close of the month succeding that to which the report relates, submit to the Bangladesh Bank a report in the prescribed form and manner, which shall contain the following particulars, namely:-

a) its assets maintained in accordance with this section; b) its time and demand liabilities in Bangladesh at the close of every Thursday during a month or if any Thursday is a public holiday under the Negotiable Instruments Act, 1881 (XXVI of 1881), at the close of the proceeding working day.

57. Punishments for certain activities in relation to banking companies.- (1) No person shall-

a) obstruct any person from lawfully entering or leaving any office or place of business of

a banking company or from carrying on any business there; or

b) hold, within the office or place of business of any banking company, any demonstration

which is violent or do anything which obstructs, or is calculated to obstruct, the usual

activities and transactions of the banking company; or

c) act in any manner calculated to undermine the confidence of the depositors in the

banking company.

(2) Whoever violates any provision of subsection (1) without any reasonable excuse shall be punishable

With imprisonment of no more than two years or a fine of no more than twenty thousand Takas or both.

(3) For the purpose of this section, "banking company" shall include Bangladesh Bank.

Chapter five

Acquisition of the undertakings of banking companies

58. Acquisition of the undertakings of banking companies.- (1) If, upon receipt of a report from the

BangladeshBank, the Government is satisfied that a banking company-

a) has, on more than one occasion, failed to comply with the directions given to it in

writing under section 29 or section 45, in so far as such directions relate to banking policy,

or

b) is being managed in a manner detrimental to the interests of its depositors, and that in the interest of the depositors of such banking company, or in the interest of banking policy, or for the better provision of credit generally or of credit in any particular area, it is necessary to acquire the undertaking of such banking company, the Government may, after consultation with the Bangladesh Bank, by notified order, acquire the undertaking of such company, hereinafter referred to as the acquired bank, with effect from such date as may be specified in the order, hereinafter referred to as the appointed date:

Provided that no undertaking of any banking company shall be so acquired unless such banking company has been given resonable opportunity of showing cause against the proposed action.

Explanation.- In this chapter, "undertaking" in relation to a banking company incorporated outside Bangladesh, means the undertaking of the company in Bangladesh.

(2) Subject to the other provisions contained in this part, on the appointed date, the undertaking of the acquired bank and all the assets and liabilities of the acquired bank shall stand transferred to, and vest in, the Government.

(3) The assets and liabilities of the undertaking of an acquired bank shall include all rights, powers, authorities, privileges and all property, whether movable or immovable, including cash balances, reserve funds, investments, deposits and all other interests and rights in, or arising out of, such property as may be in the possession of, or held by, the acquired bank immediately before the appointed date and all its account books, records and documents and shall also include all its debts, liabilities and Obligations, of whatever kind.

(4) Notwithstanding anything contained in subsection (2), if the Government is satisfied that the undertaking of the acquired bank and its assets and liabilities should, instead of vesting in the

Government, or continuing to so vest, vest in a company established under any scheme made under this

Part or in any corporation, hereinafter in this Part referred to as the transferee bank, it may, by an order

notified in the official Gazette, direct that the said undertaking including the assets and liabilities thereof,

shall vest in the transferee bank either on the publication of the notified order or on such other date as

may be specified in the order.

(5) Where the undertaking of the acquired bank and the assets and liabilities thereof vest in the

transferee bank under subsection (4), the transferee bank shall, on and from the date of such vesting, be

deemed to have become the transferee of the acquired bank and all the rights and all liabilities in relation

to the acquired bank shall, on and from the date of such vesting, be deemed to have been the rights and

liabilities of the transferee bank.

(6) Unless otherwise expressly provided by or under this Part, all contracts, bonds, powers of attorney,

grants of legal representation and other instruments of whatever kind subsisting or having effect

immediately before the appointed date and to which the acquired bank is a party or which are in favour

of the acquired bank shall be of as full force and effect against or in favour of the Government or the

transferee bank as if in the place of the acquird bank the Government or, as the case may be, the

transferee bank had been a party thereto or as they had been issued in favour of the Government or the

transferee bank, as the case may be.

(7) If, on the appointed date, any suit, appeal or other legal proceeding is pending by or against the

acquired bank, the same shall be continued and shall be deemed to have been filed by or against the

Government or the transferee bank, as the case may be.

59. Power of the Government to make scheme.- (1) The Government may, after consultation with the

Bangladesh Bank, make a scheme for carrying out the purposes of this chapter in relation to any

acquired bank.

(2) In particular, and without prejudice to the generality of the foregoing power, the said scheme may

provide for all or any of the following matters, namely:

a) the company, or the corporation, to which the undertaking including the assets and

liabilities of the acquired bank may be transferred, and the constitution, capital, name and

office thereof;

b) the constitution of the first Board of management, by whatever name called, of the

transferee bank, and all such matters in connection therewith as the Government may

consider to be necessary or expedient;

c) the continuance of the services of the employees of the acquired bank in the

Government or in the transferee bank, as the case may be, on the same terms and

conditions on which they had been employed at the acquired bank;

d) the continuance of the right of any person who, on the appointed date, is entitled to or is

in receipt of, a pension or other superannuation or compassionate allowance or benefit

from the acquired bank or any provident, pension or other fund or any authority

administering such fund, to be paid by the Government or the transferee bank, as the case

may be, the same pension, allowance or benefit so long as he observes the conditions on

which the the pension, allowance or benefit was granted;

e) the manner of payment of the compensation payable in accordance with the provisions

of this chapter to the share-holders of the acquired bank, and where the acquired bank is a

Banking company incorporated outside Bangladesh, to the acquired bank in full

Satisfaction of their or as the case may be, its, claims;

f) the provision for completing the effectual transfer to the Government or the transferee bank, as the case may be, of any asset or liability which forms part of the undertaking of

the acquired bank in any country outside Bangladesh;

g) such incidental, consequential and supplemental matters as may be necessary to secure

that the transfer of the business, property and liabilities of the acquired bank to the

Government or transferee bank, as the case may be, is effectual and complete.

(3) The Government may, after consultation with the Bangladesh Bank, by notification in the official

Gazette, add to, amend or vary any scheme made under this section.

(4) Every scheme made under this section shall be published in the official Gazette.

(5) Copies of every scheme made under this section shall be laid before the Parliament as soon as it may

be after it is made.

(6) The provisions of this part in relation to schemes shall have effect notwithstanding anything to the

contrary contained in any other provisions of this Act or in any other law oor any agreement, ward or

other instrument for the time being in force.

(7) Every scheme made under this section shall be binding on the Government or transferee bank, and

also on all members, creditors, depositors and employees of the acquired bank and of the transferee bank

and on any other person having any right, liability or power in relation to, or in connection with, the

acquired bank or the transferee bank.

60. Compensation to be given to the share-holders of the acquired bank.- (1) Every person who,

immediately before the appointed date, is registrated as a holder of shares in the acquired bank or, where

the acquired bank is a banking company incorporated outside Bangladesh, the acquired bank, shall be

given by the Government, or the transferee bank, as the case may be, such compensation in respect of the transfer of the undertaking of the acquired bank as is determined in accordance with the prescribed

principles.

(2) Nothing contained in subsection (1) shall affect the rights inter se between the holder of any share in

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the acquired bank and any person who may have any interest in such shares; and such other person shall

be entitled to enforce his interest against the compensation determined under sub-section (1), but not

against the Government, or the transferee bank.

(3) The amount of compensation to be given under sub-section (1) shall be determined in the first

instance by the Government or, as the case may be, the transferee bank, in consultation with the

Bangladesh Bank and in accordance with the rules made under the said sub-section, and shall be offered

by it to all those to whom compensation is payable under the said sub-section in full satisfaction thereof.

(4) If the amount of compensation offered in terms of sub-section (3) is not acceptable to any person to

whom the compensation is payable, such person may, before such date as may be notified by the

Government in the official Gazette, request the Government in writing, to have the matter referred to the

Tribunal constituted under section 61.

(5) If the Government receives requests under sub-section (4) from shareholders holding shares not less

than one-fourth in value of the paid-up capital ofthe acquired bank, or, where the acquired bank is a

banking company incorporated outside Bangladesh, from the acquired bank, the Government shall have

the matter referred to the Tribunal for decision.

(6) If the Government does not receive any requests under sub-section (4), the amount of compensation

offered under sub-section (3), or where any such request has been received and referred to ther Tribunal

in accordance with the provision of sub-section (5), the amount determined by it, shall be the

compensation payable under sub-section (1) and shall be final and binding on all parties concerned.

61. Constitution of the Tribunal.- (1) The Government may, for the purpose of this chapter, constitute

a Tribunal consisting of one Chairman and two other members.

(2) The Chairman of the Tribunal shall be a person who is, or has been a judge of the Supreme Court,

and of the two other members, one shall be a person who, in the opinion of the Government, has had

experience in banking and commercial matters and the other shall be a person who is a chartered

accountant within the meaning of the Chartered Accountants Order, 1973 (P.O.No.2 of 1973).

(3) If, for any reason, a vacancy occurs in the office of the Chairman or any other member of the

Tribunal, the Government may fill the vacancy by appointing another person thereto in accordance with

the provisions of sub-section (2); and any proceeding may be continued before the Tribunal, so

reconstituted, from the stage at which the vacancy occurred.

(4) The Tribunal may, for the purpose of determining any compensation payable under this chapter,

choose one or more persons having special knowledge or experience of any relevant matter to assist it in

any matter whatsoever.

62. The Tribunal to have powers of a civil Court.- (1) The Tribunal shall have the powers of a civil

Court, while trying a suit, under the Code of Civil Procedure, 1908 (Act V of 1908), in respect of the

following matters, namely:-

a) summoning and enforcing the attendance of any person and examining him on oath;

b) requiring the discovery and production of documents;

c) receiving evidence on affidavits;

d) issuing commissions for the examination of witnesses and documents etc..

(2) Notwithstanding anything contained in subsection (1) or in any other Act for the time being in force,

the Tribunal shall not compel the Government or Bangladesh Bank,-

a) to produce any books of accounts or other documents which the Government, or the

Bangladesh Bank, claims to be of a confidential nature, or

b) to make any such books or documents parts of the record of the proceedings before the

Tribunal, or

c) to give inspection of any such books or documents to any party before it or to any other

person.

63. Procedure of the Tribunal.- (1) The Tribunal shall have power to regulate its own procedure.

(2) The Tribunal may hold the whole or any part of its inquiry in camera.

(3) Any clerical or arithmetical error in any order of the Tribunal or any error arising therein from any

accidental slip or omission may be corrected by the Tribunal either of its own motion or on the

supplication of any of its parties.

Chapter six

Suspension of business and winding up of banking companies.

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64. Suspension.- (1) The High Court Division may, on the application of a banking company which is

temporarily unable to meet its obligations, make an order staying for a fixed period on such conditions

as it may think fit the commencement or continuance of all proceedings against the company, and a copy

of that order shall be forwarded to the Bangladesh Bank, and the Highcourt Division may from time to

time extend the period. But the extended period shall not exceed six month.

(2) No application under subsection (1) shall be receivable unless it is acompanied by a report of the

Bangladesh Bank to the effect that the banking company which made the application will be able to pay

its debts:

Provided that in the case of an application not accompanied by such report the High Court Division may,

if it thinks reasonable, grant remedy under this section to that company, and if such remedy is granted,

shall call for a report from the Bangladesh Bank on the affairs of the banking company, on receipt of

which it may either rescind its order or pass such further order as it may think fit and proper.

(3) When an application under subsection (1) is submitted, the High Court Division may appoint a

special officer who shall forthwith take into his custody or under his control all the assets, books,

documents, effects and actionable claims to which the banking company is or appears to be entitled and

shall also exercise such other powers as the High Court may confer on him, having regard to the

interests of the depositors of the banking company.

(4) Where the Bangladesh Bank is satisfied that the affairs of a banking company in respect of which an

order under subsection (1) has been made, are being conducted in a manner detrimental to the interests

of its depositors, it may make an application to the High Court Division for the winding up of that

banking company, and where such application has been made, the High Court Division shall not extend

the period of an order to stay proceedings under that subsection.

65. Winding up by High Court.- (1) Notwithstanding anything contained in section 153, 162 and 271

of the Companies Act, and without prejudice to the powers given under subsection (1) of section 64, the

High Court Division shall under this section order the winding up of a banking company, if-

a) the banking company is unable to pay its debts;

b) the Bangladesh Bank makes an application for its winding up under this section or

section 64.

(2) The Bangladesh Bank shall make an application under this section for the winding up a banking

company if it is directed so to do by an order under clause b) of subsection (5) of section 44.

(3) The Bangladesh Bank may make an application under this section for the winding up of a banking

company,-

a) if the banking company-

i) has failed to comply with the requirements specified under section 13; or

ii) has by reasons of the provisions of section 31 become disentitled to carry

on banking business in Bangladesh;

iii) has been inhibited from receiving fresh deposits by an order under

clause a) of subsection (5) of section 44, or under clause b) of subsection (5)

of Article 36 of the Bangladesh Bank Order, 1972 (P.O. No. 127 of 1972);

or

iv) has failed to comply with any requirement of this Ordinance other than

the requirements laid down in section 13, and after being informed about its

failures by a notice in writing, continues so to do;

v) has contravened any provision of this Ordinance and continues such

contravention beyond such period as may be specified in that behalf by the

Bangladesh Bank from time to time, after notice in writing of such

contravention has been conveyed to it; or

b) if in the opinion of the Bangladesh Bank-

i) a compromise or arrangement sanctioned by a Court in respect of the

banking company cannot be worked satisfactorily with or without modifications; or

ii) the returns, statements or information furnished to it under or in

pursuance of the provisions of this Ordinance disclose that the banking

company is unable to pay its debts; or

iii) the continuance of the banking company is prejudicial to the interests of

its depositors.

(4) Without prejudice to the provisions contained in section 163 of the Companies Act, a banking

company shall be deemed to be unable to pay its debts if-

a) it has refused to meet any lawful demand made at any of its offices or branches within

two working days; or

b) such demand is made elsewhere and the Bangladesh Bank certifies that the banking

company is unable to pay its debts; or

c) the Bangladesh Bank certifies in writing that the banking company is unable to pay its

debts.

(5) The Bangladeh Bank shall send a copy of any application made under subsection (1) to the registrar

of the Supreme Court.

66. Court liquidator.- (1) When, having regard to the number of proceedings for the winding up of

banking companies and the extent of the work involved in such proceedings, the Government is of the

opinion that it is necessary and expedient, for the purpose of conducting all proceedings for the winding

up of banking companies and performing such other duties in reference thereto as the High Court

Division may impose, to attach a court liquidator to the High Court Division, it may, after consultation

with the Bangladesh Bank, appoint a court liquidator for such period as it may determine.

(2) Where there a court liquidator has been appointed under sub-section (1) and an order has been passed

by the High Court Division for the winding up of any banking company, then, notwithstanding anything contained in section 171 or 175 of the Companies Act, the court liquidator shall become the official

liquidator of the banking company.

(3) Where there is a court liquidator attached to the High Court Division and any proceeding, for the

winding up of a banking company in which any person other than the Bangladesh Bank or the court

liquidator has been appointed as official liquidator, is pending immediately before the commencement of

this Ordinance or the date on which the liquidator is so attached, whichever is later, then,

notwithstanding anything contained in section 176 of the Companies Act, the person appointed as

official liquidator shall, on such commencement or, as the case may be, on the date of the attachment, be

deemed to have vacated his office and the vacancy shall be deemed to be filled up by the appointment of

the court liquidator as the official liquidator:

Provided that where the High Court Division, after giving the court liquidator and the Bangladesh Bank

an opportunity of being heard, is of opinion that the appointment of the court liquidator would be

detrimental to the depositors of the banking company, it may direct the former official liquidator to

continue to act as such.

67. Appointment of the Bangladesh Bank etc. as liquidator.- Notwithstanding anything contained in

section 50, or in section 175 of the Companies Act, where in any proceeding for the winding up of a

banking company the Bangladesh Bank applies to the High Court Division to appoint the Bangladesh

Bank or any individual as official liquidator, the application shall ordinarily be granted and the

liquidator, if any, functioning in such proceeding shall vacate office upon such appointment.

68. Companies Act to apply to liquidators.- (1) All the provisions of the Companies Act relating to a

liquidator, and so far as they are not inconsistent with this Ordinance, shall be applicable in the case of

liquidators appointed under section 67 or 68.

(2) Any reference to the "official liquidator" in this chapter or in chapter 7 shall be construed as

including a reference to any liquidator of a banking company.

69. Restriction on stay of proceedings.- Notwithstanding anything to the contrary contained in section

173 of the Companies Act, the High Court Division shall not make any order staying the proceedings in

relation to the winding up of a banking company, unless it is satisfied that an arrangament has been

made whereby the company can pay its depositors in full as their claims accrue.

70. Submission of a preliminary report by the official liquidator.- Notwithstanding anything to the

contrary contained in section 177 B of the Companies Act, where a winding-up order has been made in

respect of a banking company whether before or after the commencement of this Ordinance, the official

liquidator shall submit a preliminary report to the High Court Division within two month from the date

of the winding-up order or where the winding-up order has been made before such commencement,

within two months from such commencement and that report shall contain the following items, namely:

a) the information required by the Companies Act so far as it is available to him;

b) the amount of assets in cash which are in his custody or under his control on the date of

the report;

c) the amount which is likely to be collected in cash before the expiry of that period of

two month:

Provided that the High Court Division may, if it thinks fit, in any particular case extend the period of

two months by a further period of one month.

71. Notice to preferential claimants etc. .- (1) Within fifteen days from the date of the winding-up

order of a banking company or where the winding-up order has been made before the commencement of

this Act, within one month from such commencement, the official liquidator shall, for the purpose of

making an estimate of the debts and liabilities of the banking company (other than its liabilities and

obligations to its depositors), by notice served in such manner as the Bangladesh Bank may direct, call

upon every claimant entitled to preferential payment under section 230 of the Companies Act and every

secured and every unsecured creditor of the company to send to him within one month from the date of

the service of the notice a statement of the amount claimed by him.

The Bank Company Act, 1991

(2) Every notice under subsection (1) sent to a claimant having a claim under section 230 of the

Companies Act shall state that if a statement of the claim is not sent to the official liquidator before the

expiry of the period of one month from the date of the service, the claim shall not be treated as a claim

entitled to be paid under that section in priority to all other debts, and it shall be treated as an ordinary

debt of the banking company.

(3) Every notice under subsection (1) sent to a secured creditor shall require him to value his security

before the expiry of the period of one month from the date of the service of the notice and shall state that

if he does not send a statement of the claim together with the valuation of the security before the expiry

of the said period, the official liquidator shall himself value the security and such valuation shall be

binding on the creditor.

(4) If a claimant or creditor fails to comply with the direction in the notice sent to him under subsection

(1), then-

a) in the case of a claimant, his claims will not be entitled to be paid in priority to all other

debts, but shall be treated as an ordinary debt of the banking company;

b) in the case of a creditor, the official liquidator shall himself value the security and such

valuation shall be binding on the creditor.

72. Power to dispense with meetings of creditors etc. .- Notwithstanding anything to the contrary

contained in section 178 A and 183 of the Companies Act, the High Court Division may, in the

proceedings for winding-up a banking company dispense with any meeting of claimants or other

creditors of the company or the appointment of a committee if, in order to avoid unjustified delay and

expense, it thinks fit so to do.

73. Booked depositors' credits to be deemed proved.- In any proceeding for the winding-up of a

banking company, every depositor shall be deemed to have filed his claim for the amount shown in the

books of the banking company as standing to his credit; and, notwithstanding anything to the contrary

contained in section 191 of the Companies Act, the High Court Division shall presume such claim to

have been proved, unless the official liquidator shows that there is reason for doubting its correctness.

74. Preferential payment to depositors.- (1) In every proceding for the winding-up of a banking

company where a winding-up order has been made, whether before or after the commencement of this

Ordinance, within three months from the date of the winding-up order or where the winding-up order

has been made before such commencement, within three months therefrom, the preferential payments

referred to in section 230 of the Companies Act, in respect of which claims have been raised in view of, and within one month from the date of the service of the notice under section 71, shall be made by the

official liquidator or adequate provision for such payment shall be made by him .

(2) In the case of preferential payments in accordance with the provision of subsection (1), the procedure

shall be as follows, namely:-

a) in the first place, to every depositor in the savings bank account of the banking

company a sum of 2500 Takas or the balance at his credit, whichever is less;

b) in the second place, in order to pay what is due to the creditors of the banking

company, to every other depositor of the company fifty per cent. of the balance at his

credit or 2500 Takas whichever is less:

Provided that the sum total of the amounts paid under clause a) and b) to any one person who is a

depositor in the savings bank account of the banking company and a depositor in any other account,

shall not exceed the sum of 2500 Takas, but this provision shall not apply in the case of a person who is

jointly with any other person depositor in an account.

(3) Where within the period of three months referred to in subsection (1) full payment in cash cannot be

made of the accounts required to be paid under clause a) or b) , the official liquidator shall pay within

that period to every depositor under clause a) or, as the case may be, clause b) on a pro rata basis so

much of the amount due to the depositor with assets in cash as he is able to do, and the official liquidator

shall pay the rest of the amount to every depositor as and when sufficient assets are collected by the

official liquidator in cash.

(4) After payments have been made to the depositors in accordance with subsection (1), (2) and (3), the

official liquidator shall pay on a pro rata basis the general creditors with the assets of the banking company, and he shall then, as and when the assets of the banking company are collected by him in

cash, make payment on a pro rata basis with the collected assets, of the further sums which are due to

the depositors referred to in clause a) and clause b) of subsection (2).

(5) In order to enable the official liquidator to have under his control in cash as much of the assets of the

banking company as possible, the securities given to to secured creditors may be redeemed by the

official liquidator-

a) where the amount due to the creditor is more than the value of the securities as assessed

by him or, as the case may be, as assessed by the official liquidator, on payment of such

value; and

b) where the amount due to the creditor is equal to or less than the value of the securities

as so assessed, on payment of the amount due:

Provided that where the official liquidator is not satisfied with the valuation made by the creditor, he

may apply to the High Court Division for making a valuation.

(6) When any claimant, creditor or depositor to whom a payment is to be made in accordance with the

provisions of subsection (1), (2), (3), (4) or (5), cannot be found or is not readily traceable, adequate

provision shall be made by the official liquidator for such payment.

(7) For the purpose of this section, the payments specified in each of the following clauses shall be

treated as payments of a different class, namely:-

a) payments to preferential claimants under section 230 of the Companies Act;

b) payments under clause a) of subsection (2) to the depositors in the savings bank

account;

c) payments under clause b) of subsection (2) to the other depositors;

d) payments to the general creditors;

e) payments to the depositors in addition to those specified in clause a) and clause b) of subsection (2).

(8) The creditors of each different class referred to in subsection (7) shall rank equally among themselves and they shall be paid in full where the assets are sufficient so to do; and where the assets are insufficient, the payments shall abate in equal proportion.

75. Restriction on voluntary winding up.- Notwithstanding anything to the contrary contained in section 203 of the Companies Act, no banking company which holds a licence granted under section 31 may be voluntarily wound up unless the Bangladesh Bank certifies in writing that the company is able to pay in full its debts to its creditors; and without prejudice to the provisions contained in section 218 and 220 of the Companies Act, the High Court Division shall, on application of the Bangladesh Bank, order the winding up of the company by the High Court Division if at any state during the voluntary winding up proceedings the company is not able to pay any of its debts.

76. Restriction on compromise or arrangement between banking companies and creditors.- (1) Notwithstanding anything contained in any other Act for the time being in force, the High Court Division shall not sanction any compromise or arrangement between a banking company and its creditors or any class of them or between such company and its members or any class of them, or any amendment in such compromise or arrangement, unless the Bangladesh Bank is of the opinion that the Compromise, arrangement or the amendments therein are capable of being worked out and are not detrimental to the interests of the depositors of the banking company concerned.

(2) Where an application under section 230 of the Companies Act is made in respect of any banking company or in respect of the conduct of any of its directors, the High Court Division may direct the

Bangladesh Bank to make an inquiry in relation to the affairs of the banking company and the conduct

of its directors; and when such a direction is given, the Bangladesh Bank shall make such inquiry and

submit its report to the High Court Division.

77. Moratorium in respect of a banking company and reconstruction or amalgamation of banking

companies.- (1) Notwithstanding anything contained in the forgoing provisions of this chapter or in any

other Act or any agreement or any other instrument, for the time being in force, where it appears to the

Bangladesh Bank that there are reasons to make an order of moratorium in respect of a banking

company, it may apply to the Government for the making of such order.

(2) The Government, after considering and approving an application made under subsection (1), may

make an order of moratorium staying the commencement or continuance of all actions and legal

proceedings against the company, including the suspension of its business,for for a fixed period of time

and on such conditions as it thinks fit:

Provided that the Government may extend the period so however that the total period does not exceed

six month.

(3) Except as otherwise provided in the order made under subsection (2) or in any direction made by the

Government thereafter, the banking company shall not, that order being in force, make any payment to

any depositor or discharge any liabilities or obligations to any of its creditors.

(4) If during the period the order given under subsection (1) is in force the Bangladesh Bank is satisfied

that in the public interest or in the interest of the depositors or in order to secure the proper management

of the banking company or in the interest of the banking system of the country as a whole it is necessary so to do, it may prepare a scheme for the reconstruction of the banking company, or for the amalgamation of the banking company with any other banking institution, henceforth in this chapter referred to as the transferee bank.

(5) The aforesaid scheme may contain all or any of the following items, namely:-

a) the constitution, name, registration, procedure, capital, assets, power, rights, interests, authorities, liabilities, duties and obligations of the banking company on its reconstruction or, as the case may be, of the transferee bank;

b) in the case of amalgamation of the banking company, the transfer to the transferee bank of the business, properties, assets and liabilities of the banking company on such conditions as are specified in the scheme;

c) any change in the Board of Directors, or the appointment of a new Board of Directors, of the banking company on its reconstruction or, as the case may be, of the transferee bank and the authority by whom, the manner in which, and the conditions on which, such change shall be made and in the case of appointment of a new Board of Directors, the period for which such appointment shall be made;

d) the alteration of the memorandum and the articles of association of the banking company on its reconstruction or, as the case may be, of the transferee bank for the purpose of altering the capital thereof or for such other purposes as may be necessary to give effect to the reconstruction or amalgamation;

e) the continuation by or against the banking company on its reconstruction or, as the case may be, the transferee bank, of all actions and proceedings filed by or against the banking company concerned and pending immediately before the date of the order under subsection (2);

f) the reduction of the interest or rights which the members, depositors and other depositors of the banking company have in or against the banking company before its reconstruction or amalgamation to such extent as the Bangladesh Bank considers necessary in the public interest or in the interests of the members, depositors and other creditors of the banking company or for the maintenance of the business of the banking company;

g) payment in cash to depositors and other creditors in full satisfaction of their claims-

i) in respect of their interest or right in or against the banking company before its reconstruction or amalgamation; or

ii) where their interest or rights in or against the banking company has or have been reduced under clause f), in respect of such interest or right as so reduced;

h) The allotment of shares in the banking company on its reconstruction or, as the case may be, in the transferee bank to the members of the banking company for all the shares of the banking company held by them before its reconstruction or amalgamation or where has been made a reduction in accordance with clause f), for those reduced shares;.

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Dated 30th September, 1993

Act No.27 of 1993

An Act made to provide for the granting of licences to financial institutions, their control and to make other incidental provisions relating thereto

Whereas it is expedient to provide for the granting of licences to financial institutions, their control and to make other incidental provisions relating thereto;

Now, therefore, it is enacted as follows:-

Chapter I
Preliminary

1. Short title and commencement.- (1) This Act may be called the Financial Institutions Act, 1993.
(2) It shall be deemed to have come into force on first Bhadra, 1400/ 6th August, 1993, respectively.

2. Definitions.- Unless there is anything repugnant in the subject or context, in this Act-

a) "financing business" means the business carried on by any financial institution;
b) "financial institution" means such non-banking financial institutions, which-

i) make loans and advances for industries, commerce, agriculture or building construction; or
ii) carry out the business of underwriting, receiving, investing and reinvesting shares, stocks, bonds, debentures issued by the Government or any statutuary organization or stocks or securities or other marketable securities; or
iii) carry out instalment transactions including the lease of machinery and equipments; or
iv) finance venture capital; and
shall include merchant banks, investment companies, mutual associations, mutual companies, leasing companies or building societies;
c) "credit" means any financial loan on the basis of interest or any loan repayable at a premium, but shall not include loans granted under the condition to issue a debenture or other security to a company or other statutory organization;
d) "creditor" means any person entitled to have returned money deposited by him or any other person;
e) "credit facilities" means-
i) the promise of a financial institution to grant advances and other facilities or to bear liabilities on behalf of a borrower;
ii) the bearing, on behalf of a borrower, of his other liabilities by a financial institution;
f) "company" means any company registered under the Companies Act, 1913 (VII of 1913);
g) "Companies Act" means the Companies Act, 1913 (VII of 1913);

h) "auditor" means any person who, subject to the provisions of this Act, has been appointed to audit the accounts and transactions of financial institutions;

i) "director" shall also include such persons as perform by order or direction any duty of a director of a financial institution and shall also include alternate and deputy directors;
j) "regulation" means any regulation made under this Act;
k) "Bangladesh Bank" means the Bangladesh Bank established under the Bangladesh Bank Order, 1972 (PO No.126 of 1972);
l) "investment company" means a company primarily or wholly engaged in the buying and selling of securities of other companies, and shall include companies which have at any time invested eighty per cent of its paid-up capital in other companies, but shall not include any banking or insurance company or organization which is a member of the stock exchange;
m) "building society" means a society which collects savings and grants loans for the construction of buildings and the buying of properties;
n) "person" means any company, institution or organization;
o) "banking company" means any banking company established under the Banking Companies Act, 1991 (Act No.14 of 1991);
p) "merchant bank" means a bank which assumes the responsibilty for the securities of other organizations or companies and gives advice on the amalgamation, or other commercial enterprises, of such customers;
qu) "mutual association" means a savings association which does not issue capital, stocks and the depositors and borrowers of which are its owners and controllers;
r) "mutual company" means an organization which is devoid of capital and the net profit of which is distributed among the owners and borrowers in proportion to the business activities;
s) "leasing company" means a company which leases machines and implements as its business or part of its business or finances such leasing.
3. Act to override other laws.- Notwithstanding anything contained in any other law for the time being in force, the provisions of this Act shall have effect.

Chapter II

Licensing of financial institutions

4. Licensing of financial institutions.- (1) No person shall carry on any financial business without a licence to run a financial institution issued by the Bangladesh Bank.
(2) Every financial institution in existence on the commencement of this Act shall, before the expiry of six months from such commencement, apply in writing to the Bangladesh Bank for a licence under this section:
Provided that nothing in sub-section (1) shall be deemed to prohibit a financial institution in existence on the commencement of this Act from carrying on business, if-

a) its application under this section is under consideration, or
b) it has not, by a notice, been informed by the Bangladesh Bank that a licence can not be granted to it.

(3) Before granting a licence under this section, the Bangladesh Bank may require to be satisfied with regard to a proposed financial institution in respect of the following matters, namely:-
a) the financial situation;
b) the characteristics of the management;
c) the sufficiency of the capital structure and the earning capacity;
d) the purposes mentioned in the memorandum;
e) the public interest;
(4) The Bangladesh Bank may impose on any licence to run a financial institution such conditions as it thinks fit;
(5) The Bangladesh Bank may at any time, after giving opportunity for a hearing, alter any condition of a licence to run a financial institution and may add new conditions.

5. Investigations on suspect persons employed in the financing business.- The Bangladesh Bank may, if it appears to it or if it has reason to believe that any person carries on the business of financing in contravention of the provisions of section 4,-

a) order any information, document, file, book, account and record in possession, in the custody or under the control of the said person to be submitted to it;
b) confer on any person the power to enter and search any premises of such person and to seize the documents, files, books and accounts and records concerned.

6. Minimum capital.- (1) The Bangladesh Bank shall prescribe the minimum capital of every financial institution.
(2) No financial institution shall be granted a licence under this Act, if the amount of its issued capital and paid-up capital is less than the minimum capital prescribed under sub-section (1) and existing licences, if any, shall be cancelled.

7. Restrictions on the opening of branches.- (1) No financial institution may, without the prior consent in writing of the Bangladesh Bank, open at any place in or outside of Bangladesh a branch or office, nor change the location of an existing branch or office.
(2) The Bangladesh Bank shall approve of or reject an application of a financial institution for the opening of a branch or office under sub-section (1) on consideration of the matters mentioned in section 4 (3) and the decision of the Bangladesh Bank in this matter shall be final.

8. Cancellation of a licence.- (1) The Bangladesh Bank may cancel the licence of a financial institution granted under this Act on account of the following reasons, namely:-

a) if it does not carry on the business for which it had been established;
b) if the financial institution goes into liquidation or if its business is closed;
c) if it furnishes false or misleading informations or documents in order to receive a licence;
d) if it carries on its business in a manner detrimental to the interests of the depositors;
e) if its assets are not sufficient to pay the claims of its depositors;
f) if it carries on business maintaining an amount of paid-up capital which is less than the amount of the minimum capital;
g) if the conditions of the licence are contravened;
h) if the financial institution or any of its directors is convicted for an offence under this Act.

(2) Notwithstanding anything contained in sub-section (1), no licence of a financial institution shall be cancelled without granting, through no more than fifteen days' notice in writing before the cancellation of the licence of the financial institution, an opportunity to show the reasons for which its licence should not be cancelled.
(3) Where the licence of a financial institution has been cancelled, the financial institution concerned shall be immediately informed and a notice of the cancellation shall be published in the Gazette.
(4) Beginning from the date on which a notice under sub-section (3) has been published, the financial institution concerned shall cease to carry out any financial transaction except, subject to the consent of the Bangladesh Bank, such measures as may be required to conveniently suspend its business.
(5) The provision of sub-section (4) shall not be prejudicial to the rights or claims of any person on any financial institution or the rights or claims of any financial institution or any person.

Chapter III
Reserve fund, dividends, balance-sheet

9. Reserve fund.- Every financial institution shall maintain a reserve fund in such manner as may be prescribed by regulations.

10. Restriction on the payment of dividends.- No financial institution shall pay any dividend on its shares, unless all its capitalised expenses including preliminary expenses, organization expenses, commission for share selling and brokerage, losses and other items have been completely written off.

11. Display of balance-sheet.- Every financial instituition shall display a copy of its last audited balance-sheet together with the names of its directors all year through in a conspicous place in each of its offices and branches and shall, within six months before the end of the year concerned, publish the said balance-sheet in at least one daily newspaper.

12. Supply of information.- The Bangladesh Bank may direct any financial institution to supply any information and every financial institution shall be bound to supply the information so directed within such period and in such manner as the Bangladesh Bank may determine.

Chapter IV

Business rule

13. Acknowledgement of receipt of deposits.- Where a financial institution receives from any person a deposit, it shall, as a proof of having received the money, immediately make out a receipt to such person.

14. Restrictions regarding credit facilities, etc. .- No financial institution shall-

a) accept any such deposit as is repayable on demand through cheque, draft or order of the depositor;
b) deal in gold or any foreign coins;
c) grant credit facilities in excess of thirty per cent or, subject to the consent of the Bangladesh Bank, of hundred per cent of its capital to any particular person, firm, corporation or company or any such company, person or group as controls or exerts influence on such person, ,firm, corporation or company;
d) grant credits in excess of 50 per cent of its credit facilities or in excess of such percentage of its credit facilities as the Bangladesh Bank may determine from time to time;
e) grant any unsecured advance, credit or credit facilities to any firm in which any of its directors, individually or jointly, is interested directors unless the total amount of such facilities does not exceed 10 per cent of its paid-up share capital and reserves;
f) grant, in the manner mentioned in clause e), advances, credits or credit facilities in excess of Taka 500 000 to any person or group of persons other than those stated in the said clause.
Explanation.- In this sub-section, "director" includes also the wife, husband, father, mother, son, daughter, son-in-law, daughter-in-law, father-in-law and mother-in-law of a director.

(2) "Unsecured advance", "unsecured credit" or "unsecured credit facilities" as mentioned in sub-section (1) (e) mean any advance, credit or credit facilities granted without security or surety, and shall include, in the case of advances, credits or credit facilities granted against securities or sureties, that part of the credit which excedes the market value of the securities or sureties and, in the case that, in the opinion of the Bangladesh Bank, securities or sureties have no market value, the amount settled by the said Bank.
(3) No financial institution shall grant any advance or credit allowing its own shares as securities or grant credits or advances to any other institution for the purpose of buying and selling its own shares.
(4) Where there arises any loss as a result of the granting of any unsecured advance, credit or credit facilities in contravention of the provisions of sub-section (1), all the directors of the financial institution shall, jointly and individually, be responsible for the compensation.

15. Restrictions regarding the business of financial institutions.- (1) No financial institution shall, alone or in a body, be engaged in any wholesale or retail business including export and import trade otherwise than for the purpose of carrying on its financing business.
(2) No financial institution shall carry on any business other than the business of financing and such business as has been mentioned in this Act.

16. Restrictions on investments.- No financial institution shall expend or use more than 25 per cent of its paid-up capital and reserves for the acquisition or holding of any kind of shares of financial, commercial, agricultural or industrial institutions or of any similar institution and shall, as fast as possible, sell to the institutions concerned the shares acquired in the interest of realizing the credits granted by it:
Provided that any financial institution may, subject to its application and on consent of the Bank,

expend or use up to 50 per cent of its paid-up capital and reserves for the acquisition and holding of the abovementioned kind of shares.

17. Restriction on the possession of immovable property.- No financial institution may acquire or possess immovable properties exceeding in value 25 per cent of its paid-up capital and reserves:
Provided that nothing contained in this section shall be applicable in the case of immovable property required for the granting of facilities to employees of the financial institution and in the case of property acquired in the interest of realizing unrealized credits granted by it.

18. Power of the Bangladesh Bank to regulate certain matters.- The Bangladesh Bank may by order regulate the following matters, namely:-

a) the highest rate of interest to be paid by financial institutions on various kinds of deposits,
b) the highest amount of credit to be taken by financial institutions from any person,
c) the last date for repayment of credits granted by financial institutions,
d) the highest rate of interest to be paid on various kinds of credit granted by financial institutions and the manner in which to calculate such rate,
e) the upper limit of credits granted by financial institutions in favour of any person,
f) the reserves to be maintained by financial institutions at the Bangladesh Bank,
g) other matters to be regulated in the public interest or for the development of monetary policy.

Chapter V

Maintenance of minimum liquid assets

19. Maintenance of liquid assets.-

(1) Every financial institution shall maintain such liquid assets as the Bangladesh Bank may determine from time to time.
(2) For the purposes of this section, "liquid assets" means-

a) notes and coins current in Bangladesh,
b) net balances of the banks of Bangladesh,
c) the amount of call money in Bangladesh,
d) Bangladesh Treasury Bills,
e) and shall include such other assets as the Bangladesh Bank may determine.

Chapter VI

Inspection

20. Inspection- (1) Notwithstanding anything to the contrary contained in the Companies Act, the Bangladesh Bank may at any time, by one or more of its officers, carry out an inspection of any financial institution and its ledgers and accounts.
(2) The Bangladesh Bank may at any time, if it has reason to believe that any financial institution is engaged in such business as is detrimental to the interests of its depositors and debtors, or that

its assets are not sufficient to pay the claims of the public, or that it is involved in any activities incompatible with the provisions of this Act, carry out, by one or more of its officers, an examination, not being prejudicial to the provision of sub-section (1), of the ledgers, account-books and other documents of such financial institution.
(3) For the purpose of applying the powers under the sub-sections (1) and (2), the Bangladesh Bank may appoint any auditioner besides the auditioner or auditoners appointed by the financial institution under section 144 of the Companies Act.
(4) Every financial institution affected by an inspection or examination under this section shall co-operate with the officers of the Bangladesh Bank entitled to have access to its ledgers, account-books and other documents and shall be bound to furnish, in the interest of carrying out the examination, any information and opportunity:
Provided that such ledgers, account-books and other documents shall not be submitted at such time or in such place as may obstruct the normal daily activities of the financial institution concerned.

21. Information on inability to meet demands.- If any financial institution has reason to be doubtful about its ability to meet the demands of its customers or if any financial institution is forced to suspend the demands of any of its customers, it shall inform the Bangladesh Bank about the matter.

22. Measures to be taken by the Bangladesh Bank in the case offailures of a financial institution.- (1) If any financial institution informs the Bangladesh Bank about its inability to meet its demands in accordance with the provisions of section 21 or if the Bangladesh Bank has, on an inspection under section 20, reason to believe that a financial institution carries on its business in a manner which is detrimental to the interests of its depositors, or that it has become financially insolvent or that a financial institution is in a situation to be almost unable to pay its dues, or that a financial institution has contravened, or failed to comply with, the conditions of a licence granted to it, the Bangladesh Bank may, after giving reasonable opportunity to the financial institution concerned to submit a statement, take, by order, all or any of the following measures, which such institution shall be bound to observe, namely:-

a) it may direct the actions to be done or not to be done in connection with its financing business;
b) it may direct the appointment, at its expense, of any person for the proper management of its business;
c) it may assume the responsibility for the control and management of its business or direct any other person therefore.

(2) The Bangladesh Bank may, by itself or in view of an application, alter or withdraw any measure taken under sub-section (1) and may impose such conditions on such alteration or withdrawal as may be required.
(3) Notwithstanding anything contained in this section, the Bangladesh Bank may apply to the High Court Division for the winding-up of any financial institution for the reasons mentioned in this section.
(4) Where the Bangladesh Bank assumes the responsibility for the control of a financial institution, it shall control it so long as it is not satisfied that it is no longer necessary to control its business in order to protect the interests of its depositors, and such institution shall be bound to grant the Bangladesh Bank every facility required in order to facilitate such control or general management of the financial institution.
(5) The Bangladesh Bank shall determine the remuneration to be paid to any person appointed to control or manage a financial institution under this section or the other conditions etc. of his work,

and the financial institution shall bear the expenses thereof and such other expenses as may arise through its control.

Chapter VII

Submission of statement of accounts and audit of accounts

23. Submission of statement of accounts to the Bank.- The directors of every financial institution shall submit to the Bangladesh Bank a copy of the profit and loss account and balancesheet prepared in accordance with the Companies Act.

24. Appointment of an auditor and duties of the auditor.- (1) Notwithstanding anything contained in the Companies Act, every financial institution shall annually, subject to the consent of the Bangladesh Bank, appoint one auditor.
(2) If a financial institution fails to appoint an auditor, or if it is, in the opinion of the Bangladesh Bank, necessary to appoint an additional auditor together with the auditor appointed under sub-section (1), the Bangladesh Bank may appoint an auditor for such institution and shall fix the remuneration due to him.
(3) An auditor appointed under this section shall have the duty to audit the accounts of the year for which he has been appointed and to prepare a report on the basis thereof.
(4) The Bangladesh Bank may, in addition to those stated in sub-section (3), impose such other duties on the auditor as it may determine, and the auditor shall receive an additional remuneration for the discharge of such additional duties.
(5) The report of the auditor prepared under this section shall be attached to the balancesheet and profit and loss account and a copy thereof shall be send to the Bangladesh Bank.
(6) Where an auditor discharging his duty as an auditor of a financial institution is satisfied to the effect that-

a) the provisions of this Act have been seriously contravened or have not been complied with or that a financial institution has committed a criminal offense of fraud or dishonesty;
b) on account of losses the capital of a financial institution has fallen under eighty five per cent;
c) there has occurred any serious irregularity including that the payment of the creditors' demands is no longer guaranteed; or
d) that there exists any doubt as to the sufficiency of the assets to meet the demands of the creditors;

he shall without any delay inform the Bangladesh Bank on the said matters.

25. Managing directors etc. not being qualified.- (1) No person who is, or at any time has been, adjudicated insolvent, or has suspended payment of his creditors, or has compounded with his creditors, or who has been convicted by a criminal court of an offence involving moral turpitude may be or continue to be director of a financial institution or be appointed for the management of a financial institution.
(2) No director of a financial institution declared suspended under this Act or person directly involved in the management of such financial institution may, without the prior approval of the Bangladesh Bank, be appointed to the office of a director of another financial institution or to any office which may be connected with the management of another financial institution.
(3) Notwithstanding anything contained in any other law for the time being in force, no person who is director of any other financial institution, of a banking company or of a insurance company shall be qualified to be director of a financial institution.

26. Removal of a chairman, principal executive officer, board of directors or of any director.- (1) Where the Bangladesh Bank is satisfied that it is necessary to remove a chairman or director or principal executive officer of a financial institution in order to prevent its affairs being conducted in a manner prejudicial to the interests of the financial institution or its depositors or to secure in the public interest the proper management of the financial institution, it may, after committing its reasons to writing, issue a direction that such chairman, director or principal officer be removed from his office.
(2) Before issuing a direction undere sub-section (1), the person affected shall be given reasonable opportunity to make a representation.

Chapter VIII

Moratorium in respect of financial institutions, reconstruction etc.

27. Moratorium, reconstruction and amalgamation.- (1) Where it appears to the Bangladesh Bank that there are reasons to make, in the interest of the depositors, an order of moratorium in respect of a financial institution, it may make an order of moratorium suspending the business of such financial institution for a period of no more than six months:
Provided that the Bangladesh Bank may extend such period for a further period of no more than six months.
(2) If during the period the order given under sub-section (1) is in force the Bangladesh Bank is satisfied that in the public interest or in the interest of the depositors or in order to secure the proper management of the financial institution or in the interest of the finance system of the country as a whole it is necessary so to do, it may prepare a scheme for the reconstruction of the financial institution, or for the amalgamation of the financial institution with another financial institution, henceforth in this chapter referred to as the transferee institution.
(3) The aforesaid scheme may contain all or any of the following items, namely:-

a) the name, registration, capital, assets, power, rights, interests, authorities, facilities, liabilities and duties of the financial institution on its reconstruction or, as the case may be, of the transferee institution;
b) in the case of amalgamation of the financial institution, the transfer to the transferee institution of the business, properties, assets and liabilities of the financial institution on such conditions as are specified in the scheme;
c) any change in the Board of Directors, or the appointment of a new Board of Directors, of the financial institution on its reconstruction or, as the case may be, of the transferee institution and the authority by whom, the manner in which, and the conditions on which, such change shall be made and in the case of appointment of a new Board of Directors, the period for which the appointment shall be made;
d) the alteration of the memorandum and the articles of association of the financial institution on its reconstruction or, as the case may be, of the transferee institution for the purpose of altering the capital thereof or for such other purposes as may be necessary to give effect to the reconstruction or amalgamation;
e) the continuation by or against the financial institution on its reconstruction or, as the case may be, the transferee institution, of all actions and proceedings filed by or against the financial institution concerned and pending immediately before the date of the order of moratorium under sub-section (1);
f) the reduction of the interests or rights which the members, depositors and other creditors of the financial institution have before its reconstruction or amalgamation to such extent as the Bangladesh Bank considers necessary in the public interest, or in the interest of the members,

depositors and other creditors of the financial institution, or for the maintenance of the business of the financial institution;
g) payment in cash to the depositors and other creditors in full satisfaction of their claims-
i) in respect of their interests or rights in or against the financial institution before its reconstruction or amalgamation; or
ii) where their interests or rights in or against the financial institution have been reduced under clause f), in respect of such interests or rights as so reduced;
h) the allotment of shares in the financial institution on its reconstruction or, as the case may be, in the transferee institution to the members of the financial institution for all the shares of the financial institution held by them before its reconstruction or amalgamation or where has been made a reconstruction in accordance with clause f), for those reduced shares and where cash is claimed instead of shares or where it is not possible to allot shares to any member, the payment in cash to those members in full satisfaction of their claims-
i) in respect of their interest in shares in the financial institution before its reconstruction or amalgamation; or
ii) where such interest has been reduced under clause f), in respect of their interest in those reduced shares;
i) the continuance of the services of all the employees of the financial institution on its reconstruction or, as the case may be, in the transferee institution at the same remuneration and on the same conditions, which they were getting or under which they were employed before an order of moratorium under sub-section (1) has been given:
Provided that before the expiry of the period of three years from the date on which a scheme under this section is sanctioned by the Government-
i) the financial institution on its reconstruction shall determine for its employees the same remuneration and the same benefits as are, at the time of such determination, enjoyed by employees of corresponding rank of a comparable financial institution, and in respect of settling whether financial institutions are comparable or whether employees are holding corresponding ranks the decision of the Bangladesh Bank shall be final;
ii) the transferee institution shall determine for the employees of the former financial institution the same remuneration and the same benefits as are applicable to its own employees subject to the qualifications and experience of the said employees being comparable to those of its own employees, and if any doubt or difference arises as to qualification or experience, that doubt or difference shall, before the expiry of a period of three years from the date on which the remuneration and other benefits have been determined, be referred to the Bangladesh Bank whose decision thereon shall be final;
j) notwithstanding anything contained in clause h), where any of the employees are specifically mentioned in the scheme, or where any of the employees have, at any time before the expiry of one month following the date on which the scheme is sanctioned by the Government, expressed their intention of not becoming employees of the financial institution on its reconstruction or of the transferee institution, the payment to such employees of compensation, pension, gratuity, provident fund and other retirement benefits;
k) any other rule or condition for the reconstruction or amalgamation of the financial institution;
l) incidental, consequential and supplemental matters required to carry out the reconstruction or amalgamation.

(5) The Bangladesh Bank shall send a copy of the scheme prepared under this section in draft to the financial institution, the transferee institution and any other financial institution concerned, for suggestions and objections within such period as it may specify.
(6) The Bangladesh Bank may make such modifications in the draft scheme as it may consider necessary after considering the suggestions and objections received in the light of the invitation under sub-section (5).

(7) The Bangladesh Bank shall, after proceeding in accordance with sub-section (5) and (6), place the scheme before the Government for its sanction, and the Government shall sanction the scheme without any modifications or with such modifications as it may consider necessary, and the scheme as sanctioned by the Government shall come into force on such date as the Government may specify on this behalf:
Provided that different dates may be specified for the commencement of different provisions of the scheme.
(8) Upon the coming into force of the scheme or any provision thereof, the scheme or such provision shall be binding on any of the following persons and institutions, namely:-
a) the financial institution, the transferee institution and any other financial institution concerned with the amalgamation;
b) the members, depositors and other creditors of the financial institution concerned;
c) the said financial institution and the employees of the transferee institution;
d) any trustee involved in the management of ant retirement fund or any other fund, kept by the said financial institution or the transferee institution or any person having any right or liability in relation to that financial institution or transferee institution.
(9) The properties, assets and liabilities of the financial institution shall, from the date on which the scheme comes into force and to such extent as may be stated in the scheme, be properties, assets and liabilities of the transferee institution.
(10) If any difficulty arises in giving effect to the provisions of the scheme, the Government may by order do anything not inconsistent with such provisions which appears to it necessary for the purpose of removing that difficulty.
(11) Where a scheme for amalgamation of a financial institution under this section has been approved, any business acquired by the transferee institution under the scheme or under any provision thereof shall, after coming into operation of the scheme or such provision, be carried on in accordance with the law governing the activities of the transferee institution:
Provided that, in order to give full force to the scheme, the Government may, on the recommendation of the Bangladesh Bank, by notification in the official Gazette, exempt for a period of no more than seven years that business from the application of any provision of that law.
(12) Nothing in this section shall prevent the amalgamation by a single scheme of several financial institutions in respect of each of which an order of moratorium has been made.
(13) The provisions of this section and of any scheme made under it shall have effect notwithstanding anything contained in any other provision of this Act or any other Act or any agreement or any other kind of instrument for the time being in force.

28. Amalgamation of financial institutions.- (1) No financial institution may, without the prior approval of the Bangladesh Bank, be amalgamated with any other financial institution or acquire the majority of shares in any other financial institution.
(2) The Bangladesh Bank may, in the interest of considering an application for prior approval under sub-section (1), call for any information from the applicant, and it shall not cancel an application without giving reasonable opportunity for a hearing to the applicant.

29. Winding up of financial institutions by the High Court Division.- Notwithstanding anything contained in the Companies Act, the High Court Division may, on the basis of an application of the Bangladesh Bank, order the winding up of a financial institution, if-

a) the licence of the financial institution has been cancelled;
b) the financial institution is unable to pay its debts;
c) the financial institution has been punished for the contravention of any provision of this Act.

Offences and punishments

30. Punishment for carrying on the business of financing without holding a licence.- Whoever carries on the business of financing without holding a licence under this Act or continues to carry on the business of financing after the annulment of his licence shall be punishable with imprisonment for a term which may extend to two years, or with a fine which may extend to five hundred thousand Takas, or both.

31. Punishment for not cooperating in an investigation under section 5.- (1) If any suspect engaged in the business of financing at the time of an investigation under section 5 intentionally refuses to produce any informations, documents, files, books, accounts or records required for the investigation to the officer conducting the investigation or refuses to cooperate in the investigation, he shall be punishable with imprisonment for a term which may extend to one year, or with a fine which may extend to two hundred thousand Takas, or both.
(2) If any person accused under sub-section (1) disregards an order to deposit at a court any informations or records mentioned in the said sub-section, he shall be punishable with the punishments mentioned in the said sub-section.

32. Punishment for giving false informations in order to receive a licence.- Whoever intentionally gives false or erroneous informations in an application for a licence under this Act shall be punishable with imprisonment for a term which may extend to three years, or with a fine which may extend to one million Takas, or both.

33. Punishment for not complying with the conditions of a licence.- If any person fails to comply with any condition of a licence granted under this Act, he shall be punishable with a fine which may extend to one million Takas, and if he fails to comply with the conditions concerned after having been adjudicated culpable, with a fine amounting to one hundred thousand Takas for every day during which the offence continues.

34. Punishment for contravention of the provisions of section 7.- If any financial institution carries on the business of financing in its branches in contravention of the provisions of section 7, it shall be punishable with a fine amounting to one hundred thousand Takas for every day during which the offence continues.

35. Punishment for contravention of the provisions of section 14.- If any financial institution grants credit facilities in contravention of the provisions of section 14, it shall be punishable with a fine which may extend to two million Takas.

36. Punishment for failure to maintain liquid assets.- If any financial institution fails to maintain liquid assets in accordance with the provisions of section 19, it shall be punishable with a fine at the rate of one per cent for every day during which the offence continues.

37. Punishment for failure to produce account books etc. during an investigation under section 20.- If any financial institution fails to produce any account books, accounts, informations or any other necessary documents during an inspection under section 20, it shall be punishable with a fine which may extend to five hundred thousand Takas.

38. Punishment for disregarding the regulations of the Bangladesh Bank.- If any financial institution disregards the measures taken by the Bangladesh Bank under section 22, it shall be punishable with a fine amounting to two million Takas.

39. Punishment for persons who, being disqualified in acordance with section 25, are connected with financial institutions.- If any person who is disqualified in accordance with the provisions of sub-section (1) and (2) of section 25 is connected with any financial institution in contravention of the said provisions, he shall be punishable with a fine which may extend to one million Takas, or with imprisonment for a term which may extend to three years, or both, and if any person becomes director of any financial institution in contravention of sub-section (3) of the said section, he shall be punishable with a fine amounting to one hundred thousand Takas.

40. Punishment for falsely introducing oneself as a financial institution.- If any institution, not holding a licence under this Act, introduces itself, and carries on business, as a financial institution holding a licence, each owner, shareholder, director, manager, secretary or other officer or agent of the said institution shall be punishable with a fine which may extend to one million Takas, or with imprisonment for a term which may extend to three years, or both, unless he can prove that the said contravention did occur without his knowledge, or that he tried to the best of his abilities to prevent the said contravention, or that he was in no way involved in the said contravention.

41. Punishment for adding anything untrue in account books etc. of financial institutions.- (1) If any director, manager, auditor, responsible person, officer or employee of a financial institution intentionally adds, or abets to add, anything untrue in the account books, accounts, reports, business papers or other documents, heretoafter referred to as the said documents, of the said institution, or conceals or destroys anyhthing in the said documents, he shall be punishable with a fine which may extend to one million Takas, or with imprisonment for a term which may extend to three years, or both.
(2) If any person intentionally gives any false information in any statement, report or other document called for or submitted in accordance with the requirements of, or under, or for the purpose of, any provision of this Act or intentionally holds back any necessary information in any such statement, report or document, he shall be punishable with the punishments mentioned in sub-section (1).

42. Punishment for offences for which no punishment has been provided for.- Whoever does, or desists from doing, anything which comprises non-compliance with any provision of this Act or with any order or direction passed thereunder and for which no punishment has been expressly provided in this Act shall be punishable with a fine which may extend to one hundred thousand Takas.

43. Power of the Bangladesh Bank to impose fines.- (1) If any person has committed a punishable offence under the sections 31, 33, 34, 35, 36, 37, 38, 39 and 42, the Bangladesh Bank may, not filing a suit against him, give him opportunity to show the reason for which he should not be punished with a fine and may, if it is not satisfied with his explanation or if he has not given any explanation, punish him with a fine which may extend to the highest amount fixed by the said Bank.
(2) If the person concerned pays the fine within fourteen days from the date on which it had been imposed under sub-section (1), no legal proceeding shall be taken against him for the offence committed by him: but if he fails to pay the fine within the said period, the Bangladesh Bank shall file a suit at a court against the person concerned for the offence committed by him.

Chapter IX

Miscellaneous

44. Cognizance of offence.- (1) No court other than a sessions court shall try any offence under this Act.
(2) No court shall take cognizance of any offence under this Act without a complaint in writing by the Bangladesh Bank or by an officer authorized in this behalf by the Bangladesh Bank.

45. Publication of list of financial institutions.- (1) The Bangladesh Bank shall, immediately after the granting of a licence to a financial institution, publish by notification the name and address of the said institution.
(2) The Bangladesh Bank shall annually before the month of July supply to the Government a list of the financial institutions which have received a licence under this Act.

46. Alteration of memorandum of a financial institution.- (1) Notwithstanding anything contained in the Companies Act, no application for the confirmation of the alteration of the memorandum of a financial institution shall be maintainable unless the Bangladesh Bank certifies that there is no objection to such alteration.
(2) If any financial institution contravenes the provision of sub-section (1), it shall be punishable with a fine amounting to fifty thousand Takas for every day, beginning with the date on which the contravention occurred.

47. Actions taken in good faith.- No suit or other legal proceeding shall lie against the Government or the Bangladesh Bank or against any of its officers or employees for anything which is in good faith done or intended to be done under this Act, or for any damage caused or likely to be caused by anything intended to be done in good faith.

48. Power to exempt in certain cases.- The Bangladesh Bank may, after consultation with the Government, declare, by notification in the official Gazette, that any or all of the provisions of this Act shall not apply to any financial institution or to any particular financial institution either generally or for such period as may be specified in the notification.

49. Power to make rules.- (1) For the purpose of this Act, the Bangladesh Bank may, after consultation with the Government and by notification in the official Gazette, make rules.
(2) In particular, and without prejudice to the generality of the foregoing power, by such rules-

a) may be determined the fees which are to be determined under this Act;
b) may be controlled the advertisement of financial institutions.

50. Amendment of PO No.127 of 1972.- The Articles 49, 50, 51, 52, 53, 54, 55, 56, 57 and 58 of Chapter V of the Bangladesh Bank Order, 1972 (PO No.127 of 1972) shall be abolished.

51. Repeals and savings.- (1) The Financial Institution Ordinance, 1993 (Ordinance No.6, 1993) stands herewith repealed.
(2) Notwithstanding such repeal, any action done or any measure taken under the repealed ordinance shall be deemed to have been done or taken under this Act.

Merchant Bank: Functions, Services, and Examples

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What Is a Merchant Bank?

A merchant bank is a financial institution that conducts underwriting, loan services, financial advising, and fundraising services for large corporations and high-net-worth individuals (HWNIs).

Merchant banks specialize in international trade, providing services for multinational corporations. Unlike retail or commercial banks, merchant banks do not provide financial services to the general public. Some of the largest merchant banks in the world include J.P. Morgan Chase, Goldman Sachs, and Citigroup.

Key Takeaways

- Merchant banks are non-depository financial institution that specializes in international trade.
- Merchant banks provide loan services, financial advising, and fundraising services for large corporations and high-net-worth individuals.
- Merchant banks do not generally provide services for the general public, although they may have retail and commercial arms.
- Some of the world's largest banks include J.P. Morgan Chase, Goldman Sachs, and Citigroup.

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Merchant Bank

Understanding Merchant Banks

Merchant banks are non-depository financial institutions and companies that deal with international finance for multinational corporations. These banks differ from other types of financial institutions.

As such, most of their services are not targeted at the general public. While they may offer some banking services to wealthy individuals, merchant banks are more oriented toward corporate clients.

The term merchant bank is used to describe investment banks in the United Kingdom but has a more narrow focus in the United States. Merchant banks may act like investment banks in the U.S. but tend to focus on services tailored to multinational corporations and high-net-worth individuals who do business in more than one country.

Functions of a Merchant Bank

Merchant banks provide financial and advisory services to help corporate clients conduct business. They often work with companies that may not be large enough to raise funds from the public through an initial public offering (IPO).

Financing and Loans

Merchant banks traditionally perform international financing and underwriting including real estate, trade finance, and foreign investment. They may also issue letters of credit (LOCs) and in the transfer of funds.

Merchant banks can also provide more creative forms of financing. They can help corporations issue securities through private placement, which requires less regulatory disclosure and are sold to sophisticated investors.

International Transactions

If a multinational corporation operates in many different countries, a merchant bank can finance business operations in all of those countries and manage the currency exchanges. When a company seeks to make a major purchase in another country, it will seek a merchant bank that can transfer the funds to make the purchase using a letter of credit.

Example of Merchant Banking

Let's say Company ABC–based in the United States—wants to buy Company XYZ in Germany. ABC would hire a merchant bank to facilitate the process. That bank would advise Company ABC on how to structure the transaction. It may also help ABC in the financing and underwriting process.

Using the example above, the sellers in Germany would receive a letter of credit issued by the merchant bank hired by Company ABC as payment for the purchase. The merchant can also help Company ABC work through the legal and regulatory issues required to do business in Germany.

Although they don't deal with the general public, some of the biggest merchant banks also have retail and commercial banking operations.

Merchant Banks vs. Investment Banks

There's a very fine line between merchant and investment banks. Investment banks underwrite and sell securities to the general public through IPOs. The bank's clients are large corporations that are willing to invest the time and money necessary to register securities for sale to the public. Investment banks also provide advisory services to companies about mergers and acquisitions (M&A) and provide investment research to clients.

While merchant banks are fee-based, investment banks have a two-fold income structure. They may collect fees based on the advisory services they provide to their clients, but may also be fund-based, meaning they can earn income from interest and other leases.

Regardless of how a company sells securities, there are some minimum disclosure requirements to inform investors. Both IPOs and private placements require a company audit by an external certified public accountant (CPA) firm, which provides an opinion on the financial statements. Audited financial statements must include several years of financial data along with disclosures. Potential investors can use this information about the risks and potential rewards of buying the securities.

Merchant Banks vs. Investment Banks

Merchant Banks

- Underwrite and sell securities for private placements.
- Fee-based income structures.
- Clients tend to be private, pre-IPO companies.

Investment Banks

- Underwrite and sell securities to the public.
- Income based on fees and advisory services.
- Most clients are large public companies.

Frequently Asked Questions

What Is a Merchant Bank Account?

A merchant bank account is a bank account for business clients. These accounts are set up to receive debit and credit cards or other forms of electronic payment.

What Does Merchant Services Mean on a Bank Statement?

Merchant services providers are financial intermediaries between a bank and its business clients. They may help businesses handle payments processing, cash advances, online transactions, check writing and cashing, or other necessary services to maintain cash flow.d

Can I Open an Account at a Merchant Bank?

Merchant banks are non-depositary institutions that do not provide the same types of consumer services that are offered by a retail bank. Although merchant banks may also serve wealthy individuals, their services are more focused on providing financing and investment to commercial enterprises.

The Bottom Line

Merchant banks are institutions that provide loans and capital for business enterprises. They may also provide consulting services, or help their clients structure large international transactions. Merchant banks provide different services from both retail and investment banks.

Investment Banking

Investment Banking is an American synonym of merchant banking. It is a financial institution that assists individuals, corporations and governments in raising capital by underwriting and/or acting as the client's agent in the issuance of securities. An investment bank may also assist companies involved in mergers and acquisitions, and provide supplementary services such as market making, trading of derivatives, fixed income instruments, foreign exchange, commodities, and securities. It also provides advisory services on corporate matters to the firms they lend to.

In the Bangladesh context, financial institutions that carry out some distinct activities are being addressed as merchant banks. The core functions of merchant banks in Bangladesh include issue management, underwriting and Portfolio management services. The securities and exchange commission, based on SRO No 59 of 24 April 1996, and a decision taken by it on 17 August 1997, invited letters of intent from 14 institutions for registration of merchant banks. Prior to this decision, 7 institutions submitted such letters of intent and SEC gave registration to a total of 19. Presently, a total of 50 merchant banks are operating in the country, and their aggregate paid-up capital amounts to about Tk 36 billion. Among them 43 are full-fledged merchant banks. Merchant banks in Bangladesh are actively governed by the Securities and Exchange Commission (SEC) and submissively by the Bangladesh Bank.

Investment banks act as intermediaries between issuers and investors. The issuer sells securities to investment bankers who in turn sell the securities to investors. The investment banks own the securities until they are resold. For firms seeking to raise long-term funds, investment banks in Bangladesh provide assistance through a number of functions that involves.

Issue Management function of merchant Banking helps capital market to increase the supply of securities and companies to raise money from the market in order to expand their operations. A Issue Manager provides assistance a Private Limited Company intended to be converted into Public Limited Company by way of obtaining necessary permission from the relevant authorities, preparing prospectus for public issue of shares and debentures, supporting itself in the collection of application money, inspection of applications, arranging for lottery relating to allotment and so forth.

The other important function of Merchant Bank is underwriting operation. It is an arrangement whereby the underwriter undertakes to subscribe the unsubscribed portion of shares/debentures offered by any Public Limited Company. This encourages the prospective issuers to offer shares/debentures to the public for subscription and they can raise fund from the public for implementation of their industrial undertakings. Underwriters take on the risk of distributing the securities. If they fail to find enough investors, they will have to hold some securities themselves. Underwriters make their income from the price difference between the price they pay the issuer and what they collect from investors or from broker-dealers who buy portions of the offering.

A prime function of Merchant Banks is providing portfolio management services. Management of a portfolio is the process of selecting asset classes and their weights in the portfolio, maintaining diversification, executing trades, keeping records, researching, borrowing for leveraging return etc. This process is quite dynamic and requires instant adjustments when the market patterns shift to new directions. Most importantly, to complete the process sufficient involvement of people with many different skills (i.e. researching, record keeping etc) must be ensured. There is at least two keys aspects of successful portfolio management: experience of portfolio managers, execution efficiency.

Merchant Banks carry out other important services like Corporate Advisory that refers to the activity of advising organisations, including corporations, institutions and government bodies, on mergers and acquisitions and other transactions that involve a change in ownership of a company or business.

In Bangladesh a Merchant bank is said to be a full-fledged merchant bank that performs all the aforementioned activities covering Issue Management, Underwriting, and Portfolio Management and providing Corporate Advisory Services. BRAC EPL Investments Limited is one of the full-fledged merchant Banks of Bangladesh that delivers a whole range of Investment Banking services including traditional merchant banking activities such as Issue Management, Corporate Advisory, Corporate Finance, Underwriting and Portfolio Management. IDLC Finance is another leading full-fledged merchant Bank of Bangladesh commencing its Merchant Banking operations backs in 1999.

One of the major investment banks in Bangladesh, the Investment Corporation of Bangladesh (ICB), plays a leading role in developing the capital market in the country. Major functions of ICB include Merchant Banking operations and operations of unit funds and mutual funds. It has an Investors' Account Scheme, which provides small investors with credit facilities for buying and selling shares listed with the Dhaka and Chittagong stock exchanges. It also helps investors achieve reasonable returns on investment in sound shares and provides institutional support to small investors for purchase and sale of shares. Under the scheme, small investors are to hold accounts with ICB for loans for purchase of securities. The interest charged is 15.0% per annum. On behalf of account holders, ICB purchases and sells securities and maintains the profit and loss accounts. An investor has the option of taking or not taking the loan. If no loan is taken, the investor can withdraw funds from the account to the extent in excess of the margin requirement. When an investor takes a loan, he/she can withdraw the amount appearing in the account as unutilised balance. Also, an investor can withdraw securities when his/her account is closed after clearing dues outstanding in the account. Under the scheme, ICB gives the custodian service in safekeeping securities of the account holders, and also collects allotment letters, share certificate, and dividends.

ICB launched its Unit Fund Scheme on 10 April 1981. This is an open-end mutual fund, through which small and medium savers get an opportunity to invest their savings at any time of the year. The fund is divided into units known generally as ICB units, each of which bears a certain value in the assets of the fund. These units are sold to the public. Bangladeshi citizens living abroad and foreigners residing in the country can also purchase ICB units. Unit holders are the owners of the fund, while ICB takes the responsibility of managing the fund and loading and unloading securities in their interest. ICB floated its first mutual fund in 1980 and the number of its mutual funds increased to 8 by 2000.The total paid up capital of the mutual funds is Tk 175 million. In 2001, the corporation disclosed its decision to issue the 9th mutual fund of Tk 100 million.

In addition to ICB, a number of commercial banks also carry out investment banking functions in Bangladesh. The Securities and Exchange Commission (SEC) has set the minimum paid-up capital requirement for full-fledged merchant banks to Tk 25 crore. Through the Merchant Bankers and Portfolio Manager Rules 1996, Securities and Exchange Commission specified the minimum paid-up capital requirement for different merchant banking activities. For issue management the minimum paid-up capital would be Tk 2.5 crore, for under-writing issues and portfolio management, the minimum paid-up capital would be Tk 12.50 crore. The SEC has a code of conduct for issue managers, underwriters and portfolio managers and is empowered to suspend or cancel the certificate of registration for its violation. [Jamal Uddin Ahmed]

Financial Crime & Fraud

Corporate Fraud? Definition, Types, and Example

What Is Corporate Fraud?

Corporate fraud refers to illegal activities undertaken by an individual or company that are done in a dishonest or unethical manner. Often, this kind of business fraud is designed to give an advantage to the perpetrating individual or company. Corporate fraud schemes go beyond the scope of an employee's stated position and are marked by their complexity and economic impact on the business, other employees, and outside parties.

Key Takeaways

- When companies engage in activities that are dishonest or illegal, it is referred to as corporate fraud.
- There are many forms of corporate fraud including falsified accounting and misrepresenting services or products.
- The Enron scandal from 2001 is a well-known example of corporate fraud.

How Corporate Fraud Works

Corporate fraud can be challenging to prevent and tricky to catch. By creating effective policies, a system of checks and balances, and physical security, a company may limit the extent to which fraud can take place. Corporate fraud is considered a white-collar crime.

Types of Corporate Fraud

Though it may be conducted in a variety of ways, corporate fraud frequently is performed by taking advantage of confidential information or access to sensitive assets and then leveraging those assets for gain. The fraud is often hidden behind legitimate business practices or exchanges to disguise the illicit activity. Multiple stakeholders involved in corporate fraud also allows for elaborate fraud schemes to be protected by a group of complicit actors.

For example, a company's financial accounting records may be altered to present an image of high revenue and profits compared with the actual financial results. These actions might be taken to hide shortcomings such as a net loss, slow revenue, declining sales, or hefty expenses. Falsified accounting might be done to make the company more attractive to potential buyers or investors, or ultimately protect a public company's stock or valuation from dropping.

Other forms of corporate fraud may aim to disguise or misrepresent a service or product the company is developing or has in service, hiding its flaws or defects. Rather than investing in repairing, refurbishing, or redesigning the product, those responsible for the product attempt to deflect or disguise these issues. This might be done if the department or company does not have the finances to correct the problem or if revealing the issue might drive away customers and investors.

If a company or individual claims it is putting some of its funds towards investments or other types of monetary reserves that are intended to gain in value, but in actuality, those funds have been expended or diverted elsewhere, this counts as a type of corporate fraud.

Example of Corporate Fraud

The deceptive accounting and business practices that led to the downfall of Enron is an example of corporate fraud. Due to the widespread use of loopholes and other disguising tactics, the company hid debt from failed deals, the sum reaching into the billions of dollars. To maintain the charade, those responsible pressured their auditors to hide their deception, which included the destruction of financial documents.

Accounting Fraud? Definition and Examples

Accounting fraud is the intentional manipulation of financial statements to create a false appearance of corporate financial health. Furthermore, it involves an employee, accountant, or the organization itself misleading investors and shareholders. A company can falsify its financial statements by overstating its revenue, not recording expenses, and misstating assets and liabilities.

Key Takeaways

- Accounting fraud is the illegal alteration of a company's financial statements in order to manipulate a company's apparent health or to hide profits or losses.
- Overstating revenue, failing to record expenses, and misstating assets and liabilities are all ways to commit accounting fraud.
- The Enron scandal is one of the most famous examples of accounting fraud in history.

Understanding Accounting Fraud

For accounting fraud to take place, a firm must deliberately falsify financial records. Consider a firm that makes an estimate that must be revised later. No accounting fraud has taken place because the errors were not deliberate. Now suppose the CEO of a publicly-traded company knowingly makes false statements about the firm's prospects. The Securities and Exchange Commission (SEC) may well charge that CEO with fraud. However, it is not accounting fraud because no financial records were falsified.

Always be careful when alleging accounting fraud. Fraud requires intent, which can be difficult to prove.

Overstating Revenue

A company can commit accounting fraud if it overstates its revenue. Suppose company ABC is actually operating at a loss and not generating enough revenue. To cover up this situation, the firm might claim to be producing more income on financial statements than it does in reality. On its statements, the company's profits would be inflated. If the company overstates its revenues, it would drive up the firm's share price and create a false image of financial health.

Unrecorded Expenses

Another type of accounting fraud takes place when a company does not record its expenses. The company's net income is overstated, and its costs are understated on the income statement. This type of accounting fraud creates a false impression of how much net income a company is receiving. In reality, it may be losing money.

Financial Statement Manipulation

Financial statement manipulation is a type of accounting fraud that remains an ongoing problem in corporate America. Although the Securities and Exchange Commission (SEC) has taken many steps to mitigate this type of corporate malfeasance, the structure of management incentives, the enormous latitude afforded by the Generally Accepted Accounting Principles (GAAP), and the ever-present conflict of interest between the independent auditor and the corporate client continues to provide the perfect environment for such activity.1

Due to these factors, investors who purchase individual stocks or bonds must be aware of the issues, warning signs, and the tools that are at their disposal in order to mitigate the adverse implications of these problems.

Key Takeaways

- The manipulation of financial statements to commit fraud against investors or skirt regulation is a real and ongoing problem, costing billions of dollars each year.2
- Managers may also "cook the books" in order to qualify for certain executive compensation that relies on certain financial performance metrics being met.
- Because generally accepted accounting standards can be flexible and open for interpretation by a company's management, fudging numbers can be difficult to detect.

How Financial Statements Are Manipulated

Reasons Behind Financial Statement Manipulation

There are three primary reasons why management manipulates financial statements. First, in many cases, the compensation of corporate executives is directly tied to the financial performance of the company. As a result, they have a direct incentive to paint a rosy picture of the company's financial condition in order to meet established performance expectations and bolster their personal compensation.

Second, it is a relatively easy thing to do. The Financial Accounting Standards Board (FASB), which sets the GAAP standards, provides a significant amount of latitude and interpretation in accounting provisions and methods. For better or worse, these GAAP standards afford a significant amount of flexibility, making it feasible for corporate management to paint a particular picture of the financial condition of the company.

Third, it is unlikely that financial manipulation will be detected by investors due to the relationship between the independent auditor and the corporate client. In the U.S., the Big Four accounting firms and a host of smaller regional accounting firms dominate the corporate auditing environment. While these entities are touted as independent auditors, the firms have a direct conflict of interest because they are compensated, often quite significantly, by the very companies that they audit. As a result, the auditors could be tempted to bend the accounting rules to portray the financial condition of the company in a manner that will keep the client happy—and keep its business.

How Financial Statements Are Manipulated

There are two general approaches to manipulating financial statements. The first is to exaggerate current period earnings on the income statement by artificially inflating revenue and gains, or by deflating current period expenses. This approach makes the financial condition of the company look better than it actually is in order to meet established expectations.

The second approach requires the exact opposite tactic, which is to minimize current period earnings on the income statement by deflating revenue or by inflating current period expenses. It may seem counterintuitive to make the financial condition of a company look worse than it actually is, but there are many reasons to do so: to dissuade potential acquirers; getting all of the bad news "out of the way" so that the company will look stronger going forward; dumping the grim numbers into a period when the poor performance can be attributed to the current macroeconomic environment; or to postpone good financial information to a future period when it is more likely to be recognized.

Specific Ways to Manipulate Financial Statements

When it comes to manipulation, there are a host of accounting techniques that are at a company's disposal. *Financial Shenanigans* (2018) by Howard Schilit outlines seven primary ways in which corporate management manipulates the financial statements of a company.

8. **Recording Revenue Prematurely or of Questionable Quality**
    1. Recording revenue prior to completing all services
    2. Recording revenue prior to product shipment
    3. Recording revenue for products that are not required to be purchased
9. **Recording Fictitious Revenue**
    1. Recording revenue for sales that did not take place
    2. Recording investment income as revenue
    3. Recording proceeds received through a loan as revenue
10. **Increasing Income with One-Time Gains**
    1. Increasing profits by selling assets and recording the proceeds as revenue
    2. Increasing profits by classifying investment income or gains as revenue
11. **Shifting Current Expenses to an Earlier or Later Period**
    1. Amortizing costs too slowly
    2. Changing accounting standards to foster manipulation
    3. Capitalizing normal operating costs in order to reduce expenses by moving them from the income statement to the balance sheet
    4. Failing to write down or write off impaired assets
12. **Failing to Record or Improperly Reducing Liabilities**

1. Failing to record expenses and liabilities when future services remain
2. Changing accounting assumptions to foster manipulation

13. **Shifting Current Revenue to a Later Period**
    1. Creating a rainy day reserve as a revenue source to bolster future performance
    2. Holding back revenue
14. **Shifting Future Expenses to the Current Period as a Special Charge**
    1. Accelerating expenses into the current period
    2. Changing accounting standards to foster manipulation, particularly through provisions for depreciation, amortization, and depletion3

While most of these techniques pertain to the manipulation of the income statement, there are also many techniques available to manipulate the balance sheet, as well as the statement of cash flows. Moreover, even the semantics of the management discussion and analysis section of the financials can be manipulated by softening the action language used by corporate executives from "will" to "might," "probably" to "possibly," and "therefore" to "maybe." Taken collectively, investors should understand these issues and nuances and remain on guard when assessing a company's financial condition.

Financial Manipulation via Corporate Merger or Acquisition

Another form of financial manipulation may happen during the merger or acquisition process. One classic approach occurs when management tries to whip up support for a merger or acquisition based primarily on the improvement in the estimated earnings per share of the combined companies. Let's look at the table below in order to understand how this type of manipulation takes place.

Detecting Financial Statement Fraud

By

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On Dec. 2, 2001, energy behemoth Enron shocked the world with its widely-publicized bankruptcy after the firm was busted for committing egregious accounting fraud.1 Its dubious tactics were aimed at artificially improving the appearance of the firm's financial outlook by creating off-balance-sheet special purpose vehicles (SPVs) that hid liabilities and inflated earnings. But in late 2000, The Wall Street Journal caught wind of the firm's shady dealings, which ultimately led to the then-largest U.S. bankruptcy in history.2 And after the dust settled, a new regulatory infrastructure was created to mitigate future fraudulent dealings.

Key Takeaways

- Financial statement fraud occurs when corporations misrepresent or deceive investors into believing that they are more profitable than they actually are.
- Enron's 2001 bankruptcy in 2001 led to the creation of the Sarbanes-Oxley Act of 2002, which expands reporting requirements for all U.S. public companies.
- Tell-tale signs of accounting fraud include growing revenues without a corresponding growth in cash flows, consistent sales growth while competitors are struggling, and a significant surge in a company's performance within the final reporting period of the fiscal year.
- There are a few methods to inconsistencies, including vertical and horizontal financial statement analysis or by using the total assets as a comparison benchmark.

2:12

Detecting Financial Statement Fraud

What Is Financial Statement Fraud?

The Association of Certified Fraud Examiners (ACFE) defines accounting fraud as "deception or misrepresentation that an individual or entity makes knowing that the misrepresentation could result in some unauthorized benefit to the individual or to the entity or some other party." Put simply, financial statement fraud occurs when a company alters the figures on its financial statements to make it appear more profitable than it actually is, which is what happened in the case of Enron.

Financial statement fraud is a deliberate action wherein an individual "cooks the books" to either mislead investors.

According to the ACFE, financial statement fraud is the least common type of fraud in the corporate world, accounting for only 10% of detected cases. But when it does occur, it is the most costly type of crime, resulting in a median loss of $954,000. Compare this to the most common and least costly type of fraud—asset misappropriation, which accounts for 85% of cases and a median loss of only $100,000.3

Nearly one-third of all fraud cases were the result of insufficient internal controls.4 About half of all the fraud reported in the world were executed in the United States and Canada, with a total of 895 reported cases or 46%.5

The FBI counts corporate fraud, including financial statement fraud, among the major threats that contribute to white-collar crime. The agency states that most cases involve accounting schemes where share prices, financial data, and other valuation methods are manipulated to make a public company appear more profitable.6

Types of Financial Statement Fraud

And then there's the outright fabrication of statements. This, for instance, famously occurred when disgraced investment advisor Bernie Madoff collectively bilked some 4,800 clients out of nearly $65 billion by conducting an elaborate Ponzi scheme that involved wholly falsifying account statements.7

Financial statement fraud can take multiple forms, including:

- Overstating revenues by recording future expected sales
- Inflating an asset's net worth by knowingly failing to apply an appropriate depreciation schedule
- Hiding obligations and/or liabilities from a company's balance sheet
- Incorrectly disclosing related-party transactions and structured finance deals

Another type of financial statement fraud involves cookie-jar accounting practices, where firms understate revenues in one accounting period and maintain them as a reserve for future periods with worse performances, in a broader effort to temper the appearance of volatility.

The Sarbanes-Oxley Act of 2002

The Sarbanes-Oxley Act of 2002 is a federal law that expands reporting requirements for all U.S. public company boards, management, and public accounting firms. The Act, often abbreviated as Sarbanes–Oxley or SOX, was established by Congress to ensure that companies report their financials honestly and to protect investors.

The rules and policies outlined in SOX are enforced by the Securities and Exchange Commission (SEC) and broadly focus on the following principal areas:

5. Corporate responsibility
6. Increased criminal punishment
7. Accounting regulation
8. New protections

The law is not voluntary., which means that all companies must comply.8 Those that don't adhere to the are subject to fines, penalties, and even prosecution.

Financial Statement Fraud Red Flags

Financial statement red flags can signal potentially fraudulent practices. The most common warning signs include:

- Accounting anomalies, such as growing revenues without a corresponding growth in cash flows.
- Consistent sales growth while competitors are struggling.
- A significant surge in a company's performance within the final reporting period of a fiscal year.
- Depreciation methods and estimates of assets' useful life that don't correspond to those of the overall industry.
- Weak internal corporate governance, which increases the likelihood of financial statement fraud occurring unchecked.

- Outsized frequency of complex third-party transactions, many of which do not add tangible value, and can be used to conceal balance sheet debt.
- The sudden replacement of an auditor resulting in missing paperwork.
- A disproportionate amount of management compensation derived from bonuses based on short-term targets, which incentivizes fraud.

Financial Statement Fraud Detection Methods

While spotting red flags is difficult, vertical and horizontal financial statement analysis introduces a straightforward approach to fraud detection. Vertical analysis involves taking every item in the income statement as a percentage of revenue and comparing the year-over-year trends that could be a potential flag cause of concern.

A similar approach can also be applied to the balance sheet, using total assets as the comparison benchmark, to monitor significant deviations from normal activity. Horizontal analysis implements a similar approach, whereby rather than having an account serve as the point of reference, financial information is represented as a percentage of the base years' figures.

Comparative ratio analysis likewise helps analysts and auditors spot accounting irregularities. By analyzing ratios, information regarding day's sales in receivables, leverage multiples, and other vital metrics can be determined and analyzed for inconsistencies.

A mathematical approach known as the Beneish Model evaluates eight ratios to determine the likelihood of earnings manipulation, including asset quality, depreciation, gross margin, and leverage. After combining the variables into the model, an M-score is calculated. A value greater than -2.22 warrants further investigation, while an M-score less than -2.22 suggests that the company is not a manipulator.

The Bottom Line

Federal authorities have put laws in place that make sure companies report their financials truthfully while protecting the best interests of investors. But while there are protections in place, it also helps that investors know what they need to look out for when reviewing a company's financial statements. Knowing the red flags can help individuals detect unscrupulous accounting practices and stay one step ahead of bad actors attempting to hide losses, launder money, or otherwise defraud unsuspecting investors.

Securities Fraud? Definition, Main Elements, and Examples

What Is Securities Fraud?

Securities fraud, also referred to as stock or investment fraud, is a type of serious white-collar crime that can be committed in a variety of forms but primarily involves misrepresenting information investors use to make decisions.

The perpetrator of the fraud can be an individual, such as a stockbroker. Or, it can be an organization, such as a brokerage firm, corporation, or investment bank. Independent individuals might also commit this type of fraud through schemes such as insider trading.

Key Takeaways

- Securities fraud is an illegal or unethical activity carried out involving securities or asset markets in order to profit at the expense of others.
- This type of fraud is a serious crime usually involving the investment world.
- Examples of securities fraud include Ponzi schemes, pyramid schemes, and late-day trading.
- Securities fraud can also include false information, pump-and-dump schemes, or trading on insider information.

Understanding Securities Fraud

The Federal Bureau of Investigation (FBI) describes securities fraud as criminal activity that can include high-yield investment fraud, Ponzi schemes, pyramid schemes, advanced fee schemes, foreign currency fraud, broker embezzlement, hedge-fund-related fraud, and late-day trading.1 In many cases, the fraudster seeks to dupe investors through misrepresentation and to manipulate financial markets in some way.

This crime includes providing false information, withholding key information, offering bad advice, and offering or acting on inside information.

Types of Securities Fraud

Securities fraud takes on many forms. In fact, there is no shortage of methods used to trick investors with false information. High-yield investment fraud, for example, may come with guarantees of high rates of return while claiming there is little to no risk. The investments themselves may be in commodities, securities, real estate, and other categories. Advance fee schemes can follow a more subtle strategy, where the fraudster convinces their targets to advance them small amounts of money that are promised to result in greater returns.

Sometimes the money is requested to cover processing fees and taxes for the funds that allegedly await to be disbursed. Ponzi and pyramid schemes typically draw upon the funds furnished by new investors to pay the returns that were promised to prior investors caught up in the arrangement. Such schemes require the fraudsters to continuously recruit more victims to keep the sham going for as long as possible.

One of the newer types of securities fraud is Internet fraud. This type of scheme is also referred to as a pump-and-dump scheme, in which people use chat rooms and forums to spread false or fraudulent information concerning stocks. The intention is to force a price increase in those stocks—the pump, and then when the price reaches a certain level, they sell them off—the dump.

The FBI warns that security fraud is often noted by unsolicited offers and high-pressure sales tactics on the part of the fraudster, along with demands for personal information such as credit card information and Social Security numbers.1 The Securities and Exchange Commission (SEC), the FBI, and other federal and state agencies investigate allegations of securities fraud. The crime can carry both criminal and civil penalties, resulting in imprisonment and fines.

Examples of Securities Fraud

Some common types of securities fraud include manipulating stock prices, lying on SEC filings, and committing accounting fraud. Some famous examples of securities fraud are the Enron,2 Tyco,3 Adelphia,4 and WorldCom scandals.5

Here, bad actors try to manipulate the price of a stock for their own gain by spreading false information, often via Internet or newsletter, and then getting out of their position after that false information has been acted upon by unsuspecting investors. For instance, during the summer months of the stock below, a pump and dump scheme was initiated by using a "wrong number" scam. A message was left on victims answering machines that talked of a hot stock tip and was constructed so that the victim would think that the message was an accident.

As seen in the above chart, the price rose from around $0.30 to nearly $1.00, a more than 200% increase in a one-week period. This drastic increase was seen along with an equally large increase in volume. The stock had seen an average daily trading volume before the price increase of less than 250,000, but during the scam, the stock traded up to nearly 1 million shares on a number of trading days. The unsuspecting investors would have bought into the stock at around $1.00. As seen above, it fell to around $0.20, an 80% decline in value for those unfortunate investors.

What Is Insider Trading, and When Is It Legal?

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Updated March 07, 2022

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Investopedia / Mira Norian

What Is Insider Trading?

Insider trading involves trading in a public company's stock or other securities by employees with non-public, material information about the company. Insider trading can be either illegal or legal depending on when the insider makes the trade and the laws of the country the person is in.

In the U.S., insider trading is illegal when the material information is still non-public, and those who commit it face harsh consequences.

Key Takeaways

- Insider trading is the buying or selling of a publicly traded company's stock by someone who has non-public, material information about that stock.
- Material nonpublic information is any information that could substantially impact an investor's decision to buy or sell the security that has not been made available to the public.
- This form of insider trading is illegal and comes with stern penalties including both potential fines and jail time.
- Insider trading can be legal as long as it conforms to the rules set forth by the SEC.

1:43

Insider Trading

Understanding Insider Trading

The U.S. Securities and Exchange Commission (SEC) defines illegal insider trading as:

The buying or selling a security, in breach of a fiduciary duty or other relationship of trust and confidence, on the basis of material, nonpublic information about the security.1

Material information is any information that could substantially impact an investor's decision to buy or sell the security. Non-public information is information that is not legally available to the public.

The question of legality stems from the SEC's attempt to maintain a fair marketplace. An individual who has access to insider information would have an unfair edge over other investors, who do not have the same access and could potentially make larger, unfair profits than their fellow investors.

Illegal insider trading includes tipping others when you have any sort of material nonpublic information. Legal insider trading happens when directors of the company purchase or sell shares, but they disclose their transactions legally. The Securities and Exchange Commission has rules to protect investments from the effects of insider trading. It does not matter how the material nonpublic information was received or if the person is employed by the company.

For example, suppose someone learns about nonpublic material information from a family member and shares it with a friend. If the friend uses this insider information to profit in the stock market, then all three of the people involved could be prosecuted.1

The best way to stay out of legal trouble is to avoid sharing or using material nonpublic information, even if you overheard it accidentally.

Pyramid Scheme: How Does It Work

A pyramid scheme is a fraudulent and unsustainable investment pitch that relies on promising unrealistic returns from imaginary investments. The early investors actually get paid those big returns, which leads them to recommend the scheme to others. Investors' returns are paid out of the new money flowing in. Eventually, no new investors can be found and the pyramid collapses.

In a variation of the pyramid scheme, investors at each level charge initiation fees that are paid by the next layer of investors. A portion of those fees is paid on to those in the top layers of the pyramid. Eventually, no one is left to recruit. The pyramid collapses.

Often called pyramid scams, these operations are illegal in the U.S.1

Key Takeaways

- A pyramid scheme funnels earnings from all recruited participants on lower levels of an organization to participants on higher levels.
- It is a felony in the U.S. to recruit participants into pyramid schemes.
- Pyramid schemes rely on income from recruitment fees and not, as participants may believe, from the sale of actual goods or services with real value.
- Multi-Level Marketing operations (MLMs) are legitimate business programs in which distributors earn money from the sale of tangible goods and from commissions on their recruited distributors' purchases and sales.
- Pyramid schemes often masquerade as MLMs but their focus is on fees from recruits, not revenue from product sales.

How Pyramid Schemes Work

Pyramid schemes are so named because their compensation structures resemble a pyramid. The scheme starts with a single point on top where the original members exist and becomes progressively wider toward the bottom as people are recruited by every level of recruits.

Image by Julie Bang © Investopedia 2019

Say that the scheme's founder Mike sits alone at the top of the pyramid. He recruits 10 people with some promise of a big return on their money. They're represented by the level directly below him on the pyramid.

Each of those new, 10 members, or participants, pays Mike a certain fee to take part in the opportunity he's offered them. Then, each of those members is encouraged to recruit 10 more members, for a total of 100 members.

Now each of those 100 new recruits must pay fees to the tier-two recruiters, who must send a percentage of their earnings up to Mike. This recruitment and payment cycle repeats over and over again for as long as possible. As it does, money continues to flow upward to those in the levels above.

The emphasis in pyramid schemes is on recruiting new members. Seldom is the sale of any product or service actually involved, though it may have been implied to attract recruits. There is no identifiable source of income other than that coming from those recruited.2

According to the hard-sell pitches made at recruitment events, those bold enough to take the pyramid plunge will receive substantial cash from the recruits below them. However, in practice, the prospective member pools tend to dry up over time. By the time a pyramid scheme invariably shuts down, the top-level operatives may walk away with loads of cash while the majority of lower-level members are left empty-handed.

Note

According to the U.S. Securities and Exchange Commission (SEC), investors should be aware of these features of pyramid schemes:

- No genuine product or service
- Promises of high returns in a short time period
- Easy money or passive income
- No demonstrated revenue from retail sales
- Buy-in required
- Complex commission structure
- Emphasis on recruiting3

Types of Pyramid Schemes

Multi-Level Marketing Pyramid Scheme

Multi-level marketing (MLM) is a legal business program. This business model involves the sale of actual goods or services by distributors or participants in the MLM. Distributors get paid for those products and services of the MLM that they sell. They can also receive income from sales made by distributors that they've recruited and from people those recruits then bring in.4

However, some pyramid schemes disguise themselves as MLMs. The Federal Trade Commission warns people to take note of, and avoid, MLM promoters who:

- Make extraordinary claims of enormous earning potential
- Try to persuade people that recruiting others is where the real money lies
- Pressure people to get involved without learning more about the company
- Make it clear that an opportunity will be lost unless people get in immediately

Another warning sign is seeing existing distributors who continue to buy products that they can never sell so that they can qualify for some kind of reward.4

Chain Emails

Chain emails persuade naive recipients to donate money to everyone listed within an email. After making their donations, the donors are invited to delete the first name on the list and replace it with their own.

They're instructed to forward the email along to their own groups of contacts, in the hope that one or more of them will send cash their way. In theory, recipients will keep collecting donations until their name is deleted from the list.

Ponzi Schemes

Ponzi schemes are investment cons that work by robbing Peter to pay Paul. They may not necessarily adopt a pyramid scheme's hierarchical structure but they do promise high returns to existing investors.

Ponzi schemes typically involve a single, initial investment only from investors. Then, those investors wait for the promised return on their money. That is provided by new money from other investors persuaded to take part by the leader of the scheme. Most Ponzi participants end up losing everything when money for this sort of scheme dries up.

Investment advisor Bernard Madoff, arguably the most notorious Ponzi scheme artist, was sentenced to 150 years in prison for operating a multibillion-dollar Ponzi scheme.5 Madoff convinced many high-profile individuals to invest with him, falsified portfolios and relevant paperwork, and paid off early investors with money received from later investors. Most investors lost everything. Madoff died in prison on April 14, 2021.

Example of a Pyramid Scheme

In recent years, the SEC filed charges to stop a pyramid scheme masquerading as an MLM program. The company, which was called CKB, solicited investors all over the world, and in particular, focused on Asian-American communities in New York and California.3

The SEC alleged that CKB posed as a very profitable MLM company that made money selling online educational courses for children. Unfortunately, this classic pyramid scheme involved little or no retail sales. Its only source of revenue was the money it procured from new investors.3

How Pyramid Schemes Collapse

Pyramid schemes are viable as long as new, paying participants continue to buy in. The pyramid base must continue to grow. When the pool of available and willing participants disappears, the entire structure collapses.

It's impossible for pyramid schemes to function for long terms. People will invariably lose their money. Even high-level early participants may lose money near the end, due to waiting periods that delay payments from lower level recruits.

Is a Pyramid Scheme Illegal in the United States?

Essentially, yes. In the U.S., it is a felony crime to recruit any person to take part in a pyramid scheme. This crime may result in four years in prison and a fine of $5,000.1

How Do Pyramid Schemes Succeed?

The success of pyramid schemes is usually limited to founders and early-stage members. These people fraudulently attract new, fee-paying members eager to make a promised quick and large monetary return. These members then recruit more fee-paying members. This cycle continues. The income flows up to the founders and earlier members. The scheme typically collapses once no more fee-paying members can be found to support the existing members with their payments.

Are Pyramid Schemes the Same as Multi-Level Marketing Programs?

No, they are not the same. MLMs are legal, legitimate businesses whose distributors earn money from the sale of actual products and from commissions on products sold by distributors that they recruit. However, sometimes, pyramid schemes pose as MLMs to attract people who are likely to want to work with the MLM model.

The Bottom Line

Pyramid schemes are illegal in many countries. The pyramid model of profiting from a network of contacts often forces individuals to recruit their family members, friends, and acquaintances. This ultimately can strain relationships. Investors would be wise to avoid such schemes.

Ponzi Scheme vs. Pyramid Scheme: What's the Difference?

By
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Updated November 30, 2021
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Ponzi Scheme vs. Pyramid Scheme: An Overview

Ponzi and pyramid schemes have many similar characteristics based on the same concept: unsuspecting individuals get fooled by unscrupulous investors who promise them extraordinary returns in exchange for their money. Unlike a regular investment, these schemes can offer consistent profits only as long as the number of investors continues to increase. Once the number tapers off, so does the money.

Ponzi and pyramid schemes are self-sustaining as long as cash outflows can be matched by monetary inflows. The basic differences arise in the type of products that schemers offer their clients and the structure of the two ploys, but both can be devastating if broken down.

Key Takeaways

- Ponzi and pyramid schemes involve unscrupulous investors taking advantage of unsuspecting individuals by promising them extraordinary returns in exchange for their money.
- With Ponzi schemes, investors give money to a portfolio manager and are paid out with the incoming funds contributed by later investors.
- With a pyramid scheme, the initial schemer recruits other investors to recruit others (and so on) where new recruits pay the person who recruited them for the right to participate or perhaps sell a certain product.
- These schemes promise big results and often fail to provide financial documents to investors.
- Contact local authorities, the SEC, and/or the FTC if you suspect you've been a victim of any type of financial fraud, including Ponzi and pyramid schemes.

Ponzi Schemes

Ponzi schemes are based on fraudulent investment management services. They promise investors higher returns than traditional investments by paying returns to investors from money taken from new investors.

Here's how it works. Investors contribute money to the portfolio manager (the person running the scheme) who promises them a high return. When those investors want their money back, they are paid out with the incoming funds contributed by later investors.

The person who organizes this type of fraud is in charge of controlling the entire operation. But rather than put the money into a type of investment that earns interest, they merely transfer funds from one client to another and forgo any real investment activities.

Warning Signs of a Ponzi Scheme

So how do you know if you're involved in a Ponzi scheme? There are several telltale signs, including:

- Promises of high returns. Be wary if your portfolio manager makes claims that your profits will net you substantially higher returns than those of traditional investments.
- Little to no risk. Every investment offers some degree of risk. So there should be some alarm bells when someone says you'll be completely shielded and your money is protected.
- Lack of registration and licenses. Legitimate investments are regulated and managers are licensed. Make sure you ask to see any documents and credentials of anyone who is offering big results for your money.
- Complicated investment strategies. If you can't understand how your money generates returns, it's probably too good to be true.
- Missing paperwork and payments. You should be concerned if you aren't receiving any statements and/or if you don't get the payments that you're promised.

Examples of Ponzi Schemes

- **Bernie Madoff:** The most famous Ponzi scheme in recent history—and the single largest fraud of investors in the United States—was orchestrated for more than a decade by Bernard Madoff, who defrauded investors in Bernard L. Madoff Investment Securities LLC. Madoff built a large network of investors from whom he raised cash, pooling his almost 5,000 clients' money into an account he withdrew from. But he never actually invested the money, and once the 2007-2008 financial crisis took hold, he could no longer sustain the fraud. The total loss to investors was estimated to be around $65 billion.12 The controversy sparked a period in late 2008 that is known as Ponzi Mania, in which regulators and investment professionals were on the hunt for other Ponzi schemes.
- **JSG Capital Investments:** The U.S. Attorney's Office of the Northern District of California said two men were indicted in 2016 by a grand jury for wire fraud. Jaswant Singh Gill and Javier Carlos Rios of JSG Capital Investments were accused of promising investors that they would buy pre-IPO shares of private companies. Instead, the two men used the money for their own use and paid them interest to prevent individuals from getting suspicious. More than $5.5 million was diverted while the two men were accused of raising $9.3 million from their investors.3

Money managers should be able to offer verifiable financial data; true investments can be easily checked.

Pyramid Schemes

A pyramid scheme works a little differently than a Ponzi scheme. This scheme is structured so that the initial schemer must recruit other investors who will continue to recruit other investors, and those investors will then continue to recruit additional investors, and so on.

People at the top of the pyramid tend to profit the most. And because they earn more money, they're able to entice more people to join. As more people join, more money finds its way into the pyramid, which gets funneled in from new investors to the people higher up. But those at the bottom lose out, especially if they can't get others to join.

There may sometimes be an incentive that is presented as an investment opportunity, such as the right to sell a particular product or multilevel marketing (MLM). Each investor pays the person who recruited them for the chance to sell this item. The recipient must then share the proceeds with those at the higher levels of the pyramid structure.

Warning Signs of a Pyramid Scheme

You may be able to guess when you're in a pyramid scheme if the following is true:

- Recruitment. This is the main way of drawing people into the scheme. And you can't join (and thus, earn money) unless you pay a fee. In most cases, you'll also be promised more money if you recruit others.
- Fast cash. Most pyramid schemes promise to pay you big returns in a short amount of time. In many cases, these returns usually come from money paid by new recruits.
- Passive income. There are many schemes that promise to pay you money without any actual work. Again, this money is almost always coming from new recruits to the pyramid.
- Lack of documentation. Like the Ponzi scheme, there is almost never any documentation that proves how the revenue is generated. Be sure to ask for financial statements, which should be audited by a financial professional.
- Hard to understand the commission structure. If you can't understand where your profits are coming from or how anyone in the scheme is paid, then it's probably too good to be true.

Examples of Pyramid Schemes

- **Business in Motion:** This scheme required investors in Canada to pay $3,200 to join the scheme. This allowed them to purchase vacation packages that they could then resell to others for a higher fee, thus earning a bigger return. In order to keep the money coming for those at the top, the scheme required more people to join. But the vacation deals weren't even the cheapest on the market, which concerned many of the people involved. Canadian authorities charged the organizer, who was ordered to pay $6.5 million to roughly 2,000 people in a 2014 class action lawsuit.4
- **Herbalife:** One of the largest accused pyramid schemes was with the nutritional company Herbalife (HLF). The company is an MLM that develops and markets dietary supplements with operations in more than 90 countries. Federal regulators in the United States said that the company deceived consumers about the potential for returns. The claim also stated that Herbalife compensated its distributors for bringing others into the scheme, asking these new players to purchase products before the program began. Even though it was labeled as an illegal pyramid scheme and paid out more than $200 million in damages, Herbalife's products still sell, and the stock price looks healthy.5

Other types of investment fraud include affinity fraud, microcap fraud, and pump-and-dump scams.

Key Differences

Ponzi and pyramid schemes are both similar investment frauds perpetrated by one or more individuals seeking personal gain. They both involve deceiving others by promising substantial income or returns on an investor's initial investment. But there are inherent differences between the two.

One key difference is that pyramid schemes are harder to prove than Ponzi schemes. They are also better protected because the legal teams behind corporations are much more powerful than those protecting an individual.

Another thing that sets these two types of schemes apart is that the Ponzi scheme only requires investors to put up their money in exchange for returns. Pyramid schemes, on the other hand, require investors to pay a fee or purchase products in order to participate and earn returns.

What to Do If You Are the Victim of a Scheme

Don't allow yourself to be duped if someone asks you to invest your hard-earned money with promises of big returns. But if you are enthralled by the idea and there is a chance that it may be legitimate, get a second opinion. Use a lawyer or certified public accountant (CPA) to scour the documents for inconsistencies.

But it is equally as important to investigate those who manage investors' money. There are a number of ways that you can report the perpetrators of Ponzi and pyramid schemes—or any other type of financial fraud:

- Contact your local law enforcement agency and file a report.
- You can also call the Securities and Exchange Commission (SEC) to ask if there are open investigations into a money manager or prior instances of fraud.
- Check with the Federal Trade Commission (FTC) by phoning the agency or filing a complaint online.

What Are the Main Differences Between a Ponzi and Pyramid Scheme?

Ponzi and pyramid schemes are two different types of financial fraud. But there are key points that make them distinct from one another. Ponzi schemes can be easier to detect while pyramid schemes can be hidden to make them look legitimate.

Ponzi schemes simply require a cash investment to earn returns. Pyramid schemes, on the other hand, need you to pay a fee and/or purchase products and services in order to participate and earn income.

How Do You Tell if You're in a Ponzi Scheme?

There are several warning signs of a Ponzi scheme. First, the investment manager will promise you substantially higher returns that any traditional investment with little to no risk. The investment may not be registered and the individual may not even be licensed by state and federal authorities, which is a requirement. Investment strategies are often too complicated to understand and you may not receive any statements. Finally, if you begin missing any of your regular payments, you may be the victim of a Ponzi scheme.

How Does a Pyramid Scheme Work?

Pyramid schemes are a form of financial fraud. They can be disguised as financial opportunities that make them appear legitimate. Pyramid schemes offer big returns for little investment capital and often promise a way to earn income passively. They require individuals to pay an entrance fee and/or purchase products/services in order to participate. These people are then required to bring in more people to the scheme. People at the top are paid the most, receiving a portion of the money that the new recruits contribute. Those at the bottom of the pyramid make little to nothing, especially when no new individuals are recruited.

How Do You Report a Ponzi or Pyramid Scheme?

If you believe that you've been a victim of a Ponzi or pyramid scheme (or any other form of financial fraud), contact your local authorities. You can also file complaints with the Securities and Exchange Commission or the Federal Trade Commission by phone or through their websites.

The Bottom Line

There are two additional important factors to consider: The only guilty party in the Ponzi and pyramid scheme is the originator of the corrupt business practice, not the participants (as long as they are unaware of the illegal business practices). Secondly, a pyramid scheme differs from a multi-level marketing campaign, which offers legitimate products.

Money Laundering: What It Is and How to Prevent It

Learn how the prevention of money laundering has become an international effort

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What Is Money Laundering?

Money laundering is the illegal process of making large amounts of money generated by criminal activity, such as drug trafficking or terrorist funding, appear to have come from a legitimate source. The money from the criminal activity is considered dirty, and the process "launders" it to make it look clean.

Money laundering is a serious financial crime that is employed by white-collar and street-level criminals alike.1 Most financial companies today have anti-money-laundering (AML) policies in place to detect and prevent this activity.2

Key Takeaways

- Money laundering is the illegal process of making "dirty" money appear legitimate instead of ill-gotten.
- Criminals use a wide variety of money-laundering techniques to make illegally obtained funds appear clean.
- Online banking and cryptocurrencies have made it easier for criminals to transfer and withdraw money without detection.
- The prevention of money laundering has become an international effort and now includes terrorist funding among its targets.
- The financial industry also has its own set of strict anti-money laundering (AML) measures in place.

1:30

Click Play to Learn How Money Laundering Works

How Money Laundering Works

Money laundering is essential for criminal organizations that wish to use illegally obtained money effectively. Dealing with large amounts of illegal cash is inefficient and dangerous. Criminals need a way to deposit money in legitimate financial institutions, yet they can only do so if it appears to come from legitimate sources.

The process of laundering money typically involves three steps: placement, layering, and integration.

- **Placement** surreptitiously injects the "dirty money" into the legitimate financial system.
- **Layering** conceals the source of the money through a series of transactions and bookkeeping tricks.
- In the final step, **integration**, the now-laundered money is withdrawn from the legitimate account to be used for whatever purposes the criminals have in mind for it.

Note that in real-life situations, this template may differ. Money laundering may not involve all three stages, or some stages could be combined or repeated several times.3

There are many ways to launder money, from the simple to the very complex. One of the most common techniques is to use a legitimate, cash-based business owned by a criminal organization. For example, if the organization owns a restaurant, it might inflate the daily cash receipts to funnel illegal cash through the restaurant and into the restaurant's bank account. After that, the funds can be withdrawn as needed. These types of businesses are often referred to as "fronts."

Banks are required to report large cash transactions and other suspicious activities that might be signs of money laundering.4

Variants of Money Laundering

One common form of money laundering is called smurfing (also known as "structuring"). This is where the criminal breaks up large chunks of cash into multiple small deposits, often spreading them over many different accounts, to avoid detection. Money laundering can also be accomplished through the use of currency exchanges, wire transfers, and "mules"—cash smugglers, who sneak large amounts of cash across borders and deposit them in foreign accounts, where money-laundering enforcement is less strict.

Other money-laundering methods include:

- Investing in commodities such as gems and gold that can be moved easily to other jurisdictions;
- Discreetly investing in and selling valuable assets such as real estate, cars, and boats;
- Gambling and laundering money at casinos;
- Counterfeiting; and
- Using shell companies (inactive companies or corporations that essentially exist on paper only).

What Is Electronic Money Laundering?

The Internet has put a new spin on the old crime. The rise of online banking institutions, anonymous online payment services, and peer-to-peer (P2P) transfers with mobile phones have made detecting the illegal transfer of money even more difficult. Moreover, the use of proxy servers and anonymizing software makes the third component of money laundering, integration, almost impossible to detect—money can be transferred or withdrawn with little or no trace of an Internet protocol (IP) address.

Money also can be laundered through online auctions and sales, gambling websites, and virtual gaming sites, where ill-gotten money is converted into gaming currency, then back into real, usable, and untraceable "clean" money.

The newest frontier of money laundering involves cryptocurrencies, such as Bitcoin. While not totally anonymous, they are increasingly being used in blackmail schemes, the drug trade, and other criminal activities due to their relative anonymity compared with more conventional forms of currency.5

AML laws have been slow to catch up to newer types of cybercrimes, since most of the laws are still based on detecting dirty money as it passes through traditional banking institutions and channels.

How to Prevent Money Laundering

Governments around the world have stepped up their efforts to combat money laundering in recent decades, with regulations that require financial institutions to put systems in place to detect and report suspicious activity. The amount of money involved is substantial. According to the United Nations Office on Drugs and Crime, global money-laundering transactions account for roughly $800 billion to $2 trillion annually, or some 2% to 5% of global gross domestic product (GDP), although it is difficult to estimate the total amount due to the clandestine nature of money laundering.3

In 1989, the Group of Seven (G-7) formed an international committee called the Financial Action Task Force (FATF) in an attempt to fight money laundering on an international scale. In the early 2000s, its purview was expanded to combating the financing of terrorism.6

The United States passed the Bank Secrecy Act in 1970, requiring financial institutions to report certain transactions, such as cash transactions above $10,000 or any others that they deem suspicious, on a suspicious activity report (SAR) to the Department of the Treasury.14 The information that the banks provide to the Treasury Department is used by the Financial Crimes Enforcement Network (FinCEN), which can share it with domestic criminal investigators, international bodies, or foreign financial intelligence units.7

While these laws were helpful in tracking criminal activity, money laundering itself wasn't made illegal in the United States until 1986, with the passage of the Money Laundering Control Act.8 Shortly after the Sept. 11, 2001, terrorist attacks, the USA Patriot Act expanded money-laundering efforts by allowing investigative tools designed for the prevention of organized crime and drug trafficking to be used in terrorist investigations.1

The Association of Certified Anti-Money Laundering Specialists (ACAMS) offers a professional designation known as a Certified Anti-Money Laundering Specialist (CAMS). Individuals who earn CAMS certification may work as brokerage compliance managers, Bank Secrecy Act officers, financial intelligence unit managers, surveillance analysts, and financial crimes investigative analysts.9

Why Is It Important to Combat Money Laundering?

Anti-money laundering (AML) seeks to deprive criminals of the profits from their illegal enterprises, thus eliminating the main motivation for them to engage in such nefarious activities. Illegal and dangerous activities, such as drug trafficking, people smuggling, terrorism funding, smuggling, extortion, and fraud, endanger millions of people globally and impose tremendous social and economic costs upon society. As the proceeds of such activities are legitimized by money laundering, combating money laundering may result in a reduction in criminal activity and hence a significant benefit to society.

What Is an Example of Money Laundering?

Say that cash has been earned illegally from selling drugs, and the drug dealer wishes to buy a new car with the proceeds. Because it is difficult and suspicious to try to purchase a vehicle entirely in cash, the dealer needs to launder the money to have it appear legitimate. The drug dealer also owns a small laundromat, a highly cash-intensive business. The cash from the drug deal is mingled with the laundromat's cash and then taken to a bank for deposit. Then, drawing a check from the laundromat's account, the dealer is able to buy the car without suspicion.

Another common form of money laundering in casinos is to buy chips from the casino with cash, and to receive checks in return for the chips from the casino, often without gambling at all or placing minimal bets.

How Can You Tell If Someone Is Laundering Money?

There are several red flags to look out for that may point to money laundering. Some of these include suspicious or secretive behavior by an individual around money matters, making large transactions with cash, owning a company that seems to serve no real purpose, conducting overly-complex transactions, or making several transaction just under the reporting threshold.

What Are Some Ways in Which Real Estate Is Used for Money Laundering?

Some common methods used by criminals for money laundering through real estate transactions include undervaluation or overvaluation of properties, buying and selling properties in rapid succession, using third parties or companies that distance the transaction from the criminal source of funds, and private sales.10

How Are Cryptocurrencies Being Used in Money Laundering?

The U.S. Financial Crimes Enforcement Network (FinCEN) noted in a June 2021 report that convertible virtual currencies (CVCs)—another term for cryptocurrencies—have grown to become the currency of choice in a wide range of online illicit activities.11

Apart from being the preferred form of payment for buying ransomware tools and services, online exploitative material, drugs, and other illegal goods online, CVCs are increasingly used to layer transactions and obfuscate the origin of money derived from criminal activity. Criminals use a number of money-laundering techniques involving cryptocurrencies, including “mixers” and “tumblers” that break the connection between an address (or crypto “wallet”) sending cryptocurrency and the address receiving it.

Procedure for Liquidation or Winding up of Company in Bangladesh: Steps

Step 1 | File and Winding up or Liquidation Petition to the Court

A company may be wound by the court in certain circumstances: if the company through the special resolution decided that it must be wound up by the court; or if default is made in filling the statutory report or in holding the statutory meeting; or if the number of members reduced below the required number as per the Company Law; or the company is incapable of paying its debts; or if the court is of opinion that it is just and equitable to wind up the company.

When a company is deemed to unable to pay its debts is considered by section 242 of the Companies Act 1994. These will be if a creditor to whom the company is indebted for a sum and the company neglects to pay the sum for three weeks or if execution or other process issued on a decree or order of any court in favor of a creditor of company is returned unsatisfied in whole or in part or if it is proved to satisfaction of court that the company is unable to pay its debts and court shall take into account the contingent and prospective liabilities of company.

Section 316-321 of the Companies Act 1994 deals with winding up subject to supervision of court. When a company has by special or extraordinary resolved to wind up voluntarily the court may make an order that the voluntary winding up shall continue but subject to supervision of court and such terms as the court thinks just. Where an order is made for winding up subject to supervision, the liquidator may, subject to any restriction imposed by the court, exercise all the powers as if the company was being wound up altogether voluntarily.

It is to be noted that, according to section 247 of the 1994 Act, a winding up of a company by the court shall be deemed to commence at the time of the presentation of the petition for the winding up.

Step 2 | Draft and Prepare Winding Up Documents

In case of voluntary winding up, the second step is to prepare documents. These are Declaration of Solvency, (which shall include information such as the company has no debts among other things) and Profit and Loss Account and Audited Balance. These documents shall have to be approved by the majority directors of the company.

Step 3 | Documents Needs to be submitted to RJSC

The approved Declaration of Solvency then must be filed with the RJSC (Registrar of Joint Stock Companies and Firms) within 5 weeks.

Step 4 | Pass a Special Resolution in the Company

The next step is to pass a special resolution through the extraordinary general meeting to approve the decision of winding of the company and the appointment of the liquidator. This (the content of the meeting) shall also be filed with the RJSC. The above stated special resolution must be advertised, within 10 days of its passing, in the official Gazette, and in a newspaper circulating in the district where the registered office of the company is located.

Step 5 | Appointment of the Liquidator

After that, the liquidator shall accept the appointment and this must also be notified to the RJSC and the same shall be informed to the Deputy Commissioner of Taxes (having the jurisdiction) within 30 days of the said appointment.

<u>Step 6 | Preparation of Final Report by the Liquidator</u>

The liquidator shall prepare a Final Account showing how the winding ups has been conducted and the assets distributed. After that, an extra ordinary general meeting shall be called by the liquidator. The notice of the meeting must be given by way of advertisement which must not be less than one month before the meeting. Such an advertisement shall be given in the official Gazette, and in a newspaper circulating in the district where the registered office of the company is located. A special resolution shall be passed in the extraordinary general meeting with regards to the disposal of the books and papers of the company.

Step 7 | Filling all the Documents respectively to RJSC

Finally, there is a duty to hold a final meeting and the submission of the documents to the Registrar. Now the company winded up.

Case Study: The People’s Leasing Case:

Hollowing out of People's Leasing: An insider job

The company owed Tk1,242 crore to individual depositors as of December 2018

Individual depositors on Wednesday rushed to the office of People’s Leasing and Financial Services (PLFS) to withdraw money following a government move to liquidate the non-bank financial institution.

They, however, did not find anyone to meet, as no high official was present.

The company owed Tk1,242 crore to individual depositors as of December 2018.

On June 27, the finance ministry in a letter asked the Bangladesh Bank (BB) to take necessary steps to liquidate the institution.

It also directed the central bank to file a complaint with the Anti-Corruption Commission (ACC) against all officials involved in the money embezzlement of PLFS.

The instruction came after BB on May 21 proposed the ministry to lay off PLFS, which failed to pay back money to depositors.

This is the first financial institution that has been put in liquidation in the country's history.

The total loss of PLFS stood at Tk 2,324 crore at the end of December 2018. Its capital shortfall stood at Tk 2,013 crore. PLFS owed Tk 798 crore to different banks and financial institutions.

The size of its total loan portfolio was Tk1,145.18 crore, of which 67.46 percent was classified as of December last year.

Who is responsible for the downfall of PLFS?

An investigation by the central bank in 2014 revealed massive corruption by directors, involving Tk670 crore.

They embezzled the money from the institution in different ways between 2004 and 2013, when M Moazzam Hossain was its chairman.

Later in 2015, the central bank removed five board members.

Of them, Humaira Alamin, Arafin Shamsul Alamin and Nargis Alamin are also directors of Shamsul Alamin group.

The two others are Motiur Rahman and Khabir Uddin Miah.

Moazzam was identified by the central bank as one of the main culprits for dragging the institution into collapse.

Moazzam, in collusion with other directors swindled Tk123 crore from PLFS in the name of purchasing a disputed land at the city's Green Road.

The land was purchased from two dubious companies - Jenith and Jefair.

The money was used for adjusting default loan accounts of directors, according to the BB findings.

The central bank had asked PLFS to file a case with money loan court as well as a criminal case against Moazzam.

The company filed a case only with the money loan court against its former chairman.

PLFS neither got registry of the land nor got back the money.

Moazzam, who resigned from PLFS in November 2015, is now a director of a new generation bank - South Bangla Agriculture and Commerce (SBAC) Bank.

Motiur Rahman, who was among the five PLFS directors removed for their involvement in irregularities, has a defaulted loan of around Tk100 crore with the firm.

His wife is now a director of SBAC Bank.

Shamsul Alamin group took over Tk100 crore from PLFS when its three directors were in the board of the financial institution for 10 years until 2015.

Moreover, the group was involved in bringing out Tk123 crore in the name of purchasing land in collusion with Moazzam, according to central bank's findings.

Alamgir Shamsul Alamin, who is also president of the Real Estate and Housing Association of Bangladesh (REHAB), is the managing director of the business group.

Besides, he holds the post of managing director of Paramount Properties, where Moazzam is a director. PLFS had a loan of Tk65 crore to the group as of May last year.

Of the three directors of Shamsul Alamin group, who were in the PLFS board, are Almagir's family members. Humaira is his wife, Arafin is his younger brother and Nargis is Arafin's wife.

Contacted, Alamgir said they were repaying the money regularly and ready to pay the full amount.

The group was in the board of PLFS for 10 years, he said.

Asked who are responsible for the current situation of PLFS, he said 'off course who ran the company'.

Former PLFS director Khabir defaulted with a loan of above Tk100 crore with the company.

He took the credit against 11 unknown names between 2009 and 2010, when he was on its board.

Khabir has a jewelry business named Al Hassan Jewelry and Diamond.

During a visit to his jewelry shop at Gulshan in the city, he refused to talk to this correspondent.

Some influential clients who did not repay their loans have intensified the deterioration of PLFS.

For instance, Md Syful Islam, who was holding directorship of Islami Bank Bangladesh Ltd (IBBL) - the largest private bank in the country - even a month ago, is among the PLFS defaulters.

He took Tk4.5 crore from the institution in 2009 and in the last eight years, he turned defaulter for three times, taking the total outstanding loans to over Tk10 crore.

Syful - also a managing partner of an audit firm named Syful Shamsul Alam & Co - was holding the directorship of IBBL as the representative of Blue International.

The company he was representing in IBBL board has 2 percent holdings with the bank worth around Tk100 crore.

He quit the IBBL directorship a month ago citing personal ground.

Syful took the loan from PLFS in 2009 for purchasing a 98-katha land in Savar on the outskirts of the city and for constructing a building on his own land at Bashundhara Residential Area in the city where he owns a 15-katha land worth some Tk8 crore.

Just two weeks before taking the IBBL directorship on May 30, 2016, he rescheduled his loan for a second time by compromising required down payment with special consideration of the central bank.

The first installment payment started in June 2016 but he did not pay regularly and eventually turned defaulter again in February 2017.

PLFS then served him a notice through the central bank to vacate his directorship with the Islami Bank as bank company act does not allow a defaulter to hold a directorial position.

Contacted Sami Huda, managing director of PLFS, said Syful did not pay his loan despite repeated commitments with the company.

“As he failed to pay back the money, we marked him as defaulter and wrote to the central bank to vacate his directorship from the Islami Bank,” he said.

Intraco Group

The Chittagong-based business conglomerate started business with PLFS in 2005 by taking working capital of Tk26 crore for five years.

However, it did not repay the loan in 13 years even after availing special facilities including interest waiver beyond the banking norms.

In 2016, the company was allowed for a third time to reschedule its loans with special benefits. PLFS waived all the interest amount of Tk13 crore to get back the money fast to meet up its liquidity crisis at that time.

The company was given five years to pay off only the principal amount of Tk 25 lakh. Even during the period, no interest would be charged against the principal amount, which completely beyond the banking practice.

Despite getting such unique offer, the company did not continue the payment and turned defaulter in March last year. As the company could not continue the installment payment, the special facility was cancelled by PLFS.

As a result, all the interest from the year 2016 was calculated and the outstanding loan amount stood at around Tk 50 crore as of March last year, according to PLFS.

Hakim Ali, who is known for establishing first four-star hotel named Hotel Agrabad in Chittagong, is chairman of Intraco group.

His son, Mohammed Riyadh Ali, is managing director of the business group, while his wife Monowara Hakim Ali is a director.

Monowara is also president of Chittagong Women Chamber Of Commerce and Industry. Monowara and Riyadh both have personal guarantee against the loan accounts with PLFS.

[**Jebun Nesa Alo** 10 July, 2019, 08:15 pm,The Business Standard]

Bangladesh Financial Intelligence

Bangladesh Financial Intelligence Unit (BFIU) is the central agency of Bangladesh responsible for analyzing Suspicious Transaction Reports (STRs), Cash Transaction Reports (CTRs) & information related to money laundering (ML) /financing of terrorism (TF) received from reporting agencies & other sources and disseminating information/intelligence thereon to relevant law enforcement agencies. BFIU has been entrusted with the responsibility of exchanging information related to money laundering and terrorist financing with its foreign counterparts. The main objective of the BFIU is to establish an effective system for prevention of money laundering, combating financing of terrorism and proliferation of weapons of mass destruction.

BFIU was established in June 2002, in Bangladesh Bank (Central bank of Bangladesh) named as 'Anti Money Laundering Department'. To enforce and ensure the operational independence of FIU, Anti Money Laundering Department has been transformed as the Bangladesh Financial Intelligence Unit (BFIU) in 25 January, 2012 under the provision of Money Laundering Prevention Act, 2012 and has been bestowed with operational independence. BFIU has also achieved the membership of Egmont Group in July, 2013.

Legal Framework

BFIU works under the provisions of Money Laundering Prevention Act, 2012 and Anti-Terrorism Act, 2009 (including amendments in 2013).

………………………………………

Law cannot *be* nude simple. nor can it be made easy. However, it is our strong conviction that law does not have to be made any more difficult than it already is. and it is on that premise that we have written this basic text for undergraduate students. The purpose of *Comprehensive Business Law: Principles* and *cases* is to make the myriad topics of business law comprehensible to the beginning student by using plain language, relevant and realistic examples, pertinent cases, and an easy writing style. While we do not intend to familiarize students with all the technical intricacies of the law, we do hope to stimulate their interest in those intricacies and to make them aware of how the law affects their lives.

No matter what discipline a business student selects as a major field of study, that student will encounter many legal issues during his or her professional life. A substantial number of those issues will undoubtedly fall with in the areas covered in this text—among them, contracts, sales, commercial paper, debtor-creditor relations, agency, partnerships, corporations, government regulations, property protection, and international business. This text cannot supply the solutions to all the potential legal problems involved in the seare as, but it can help one in recognizing the legal issues that such problems present and in deciding when to seek the appropriate help. The study of this book will not make anyone into a lawyer, but it should make one aware of when a lawyer is needed.

Glossary

A

Abandoned property, Property that owner has .... with no intention of ever again reclaiming any rights or interests in it.

Abet To assist or support in the performance of an at or the attainment of a purpose,

Acceptance clause A clause in a contract that advances the date for payment on the occurrence of a condition or the breach of a duty.

Acceptance of payment The speeding up of the due date for payment for a contract or for a commercial instrument

Accept To agree to, as in an offer,

Acceptance Compliance with the terms of an offer: the action of a buyer in taking the goods tendered by a seller; the act whereby a drawee agrees to honor a negotiable instrument upon due presentment.

AcceptorA person who accepts a negotiable instilment or otherwise agrees to be primarily liable rot the instrument.

Accession The acquisition of additional property due to the growth or increase of property already possessed.

The definitions given here are accurate as far as they go, but space limitations prevent complete technical definitions. A student who wants a more detailed definition is advised to consult a legal dictionary such as *Black's* Law *Dictionary* or *Balanchine's Law Dictionary.*

Administrator (administrator) A man (woman) who has been empowered by an appropriate court to handle the estate of a deceased person; a manager of the affairs of another person. in the name of the person so managed.

Admission Agreement or concession concerning evidence or pleadings without the need to introduce proof

Adverse possession A method for gaining tide to property by possession/occupancy for a predetermined statutory period. Adverse possession requires that the possessor occupy the property openly, notoriously, hostilely. and continuously for a period specified by state statute.

Advisory opinion A formal opinion issued by a court at the request of a legislative body or of a government officer concerning a hypothetical fact situation.

Affidavit A written. sworn statement declaring the facts contained in the statement to be true.

Affirmative defense A defense to a cause of action that must be raised by the defendant.

After-acquired property Property gained or possessed following a certain date or event; that which is attained later.

Agency A legal relationship in which one person is empowered and authorized to represent another, normally in the formation of contracts.

Agent A person authorized to act for or on behalf of another in the formation of contracts.

Aid To assist; to provide a person with things necessary to the attainment of a desired end.

Alien Foreign; owing allegiance to another government.

Alleged Asserted to be true or factual without any snowing of proof.

Allonge A piece of paper permanently attached to a negotiable instrument to accommodate additional endorsements when the original instrument has no more room for endorsements.

Alluvion An increase in land by the gradual deposit of substances from the flow of water against the short. The land so added becomes the property of the owner of the land where the new substances are deposited.

Ambiguity Doubtful meaning or uncertainty due to obscurity or *lack* of distinctness.

Amortize To provide for the gradual extinction of a debt or obligation by periodic contributions to a

Annuitant The beneficiary of an annuity.

Annuity A sum of money payable periodically, commonly annually, to a named person; the unman that creates the obligation to pay the annuitant the periodic payments.

Answer Any sort of pleading filed by the defendant in a cause of action, but especially the written state. meat that sets forth the defenses asserted.

Antedated Predated; given an earlier date than the date on which the event occurred (normally used with reference to a negotiable instrument;.

Anticipatory breach A refusal or rejection by one party to a contract before the time for performance that permits the other party to treat the repudiation as an immediate breach of the contract. Also known as *anticipatory repudiation.*

Antitrust laws Legislation opposed to the formation or use of trusts or combinations; statutes designed to protect commerce from unfair trade practices or monopolies.

Apparent authority Authority that the agent appears to possess because of the conduct of the principal and on which the third person relies as being authorized; authority that the agent does not in fact possess but that the third person has been caused to believe does exist.

Appellant A party who takes an appeal from one court to another.

Appellate court A court that has the authority to review the action of inferior courts upon proper appeal or writ; a reviewing court.

Appellee The party in a case against whom an appeal has been taken.

Appraisal right The right in certain extraordinary corporate activities to have a security evaluated and the appraised value paid to the owner.

Appurtenant Belonging to; annexed to; adjoining and necessary to the enjoyment of.

Arbitration A nonjudicial settlement of a case or controversy whereby the parties submit the issues to an independent person chosen by the parties or appointed by statutory authority.

Arraignment The calling of a defendant before the court to answer to a charge of having committed a crime.

Arson At common law, the intentional burning of the house or outbuilding of another person. Today a number of state statutes also include as arson the

malicious burning of one's own house or

Accommodation party Aparty who signs a commercial paper for the purpose of lending his or her name to another party to the instrument.

Accord An agreement between two or more parties on the degree of performance that will operate as a full discharge of an obligation.

Accord and satisfaction The making of a new agreement between two or more parties and the performance of that agreement by the parties (normally used in the area of disputed claims).

Account To furnish a justifying explanation or analysis for monies spent or actions taken.

Accretion An addition by growing.especially in the area of real property. where land increases by natural actions and causes.

Actionable Affording grounds for an action. suchas a suit at law.

Actual causethe act that brings about some end result,

Actual fraud See **Fraud.**

Adhesion Aform attachment: a sticking together. When used in reference to a contract. it means a contract whose terms are not open to negotiation — the offered must "take it or leave it."

Adjudicate To determine through a judicial proceeding.

Adjunct Added or joined to another.

Administrative lawthe branch of public law that deals with administrative agencies and their actions.

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malicious burning of one's own house or

Articles of incorporation The legal document that must be filed with a designated state official in order to do business as a corporation. The articles must comply with state statutes and must be approved by the state before the corporation legally exists..

Assault An intentional threat to harm another by use of force, together with the apparent means to accomplish the threat, which causes fear that the harm will occur.

Assignee The grantee, or recipient, of an assignment.

Assignment The legal transfer to another of one's rights under a contract.

Assignment for the benefit of creditors An assignment by a debtor of the debtor's assets to a trustee to be used in the satisfaction of the claims of creditors.

Assignor A person who makes an assignment.

Association A voluntary joining together of two or more persons to achieve a common goal.

Assumption of the risk A legal defense to a ton action in which the plaintiff is said to have voluntarily chosen to face the risk or danger that occurred and therefore has no right to complain of its occurrence.

Assurance A guaranty; a promise; a statement that inspires confidence that the assured thing will occur.

Attach To seize property in order to bring it within the jurisdiction of the court.

Attachment The act of attaching; a writ or judicial order directing the taking of persons or property in order to assure jurisdiction by the court.

At will Without a set time period; for as long as is mutually agreeable.

Auction A public sale in which the property being sold goes to the highest bidder.

Avoid To cancel an obligation or duty.

Avulsion The removal of land from the property of one person and the addition of that land to the property of another person by the action of water.

Award The decision entered by an arbitrator or other nonjudicial person in the matter submitted for resolution.

B

Ball Security given for the appearance of a defendant' prisoner in order to secure a release from imprisonment pending the trial.

Bailee The person to whom property is delivered In a bailment, with the understanding that that

person will return the property at a later time or will dispose of it according to the directions of the bailor.

Bailment A delivery of goods from one party to another in trust, with no transfer of title occurring.

Bailor The person who delivers the property involved in a bailment to the bailee. A bailor does not need to be the *owner* of the bailed goods in order to create a valid bailment.

Bankruptcy An area of law designed to give an "honest debtor" a fresh start; the proceedings undertaken against a person or a firm under the bankruptcy laws.

Bar The complete and permanent destruction of an action at law; also, the entire body of attorneys permitted to practice law in a particular jurisdiction.

Bargain (Noun) an agreement between parties that specifies what each is to receive and what each is to perform or deliver. (Verb) to come to terms.

Battery The unauthorized touching of the person of another without legal excuse or the consent of the person so touched.

Beneficiary A person for whom a trust is created; a person designated to receive the proceeds of an insurance policy; a person who receives advantages or profits from another.

Benefit An advantage, profit, or gain; a legal right received from another.

Bona fide occupational qualification (BFOQ) A legally justifiable limitation concerning the ability to perfonn a particular job.

Bona fide purchaser A person who purchases in good faith. for value. and without notice of any defects or defenses affecting the sale or transaction.

Bond A written evidence of indebtedness, usually hearing interest. issued by a public or private corporation. and payable at a fixed future date.

Book value The value of a business, arrived at by deducting liabilities from assets.

Boycott A concerted refusal to have any dealings with a person or a firm; a conspiracy to disrupt the business of a person or firm.

Breach The breaking of a duty or right, whether by act or omission; the failure to honor a promise, or any pan of a promise. that forms the basis of a contract.

Bribe Anything of value given or accepted with the corrupt intention of influencing a person in the performance of a public duty or the carrying out of any official actions.

Bulk sale The sale of all or a substantial part of a merchant's stock in trade not made in the ordinary course of business. Also known as *bulk transfer.*

Burden of proof The legal duty to prove the truth of facts in dispute in a cause of action in order to prevail in the cause; the amount of proof necessary to carry one's case, such as "beyond a reasonable doubt," or "clear and convincing evidence."

Burglary The crime of breaking into a building with an intent to steal; at common law, the act of breaking into a dwelling at night with an intent to commit a felony.

Buyer in the ordinary course of business A purchaser who buys goods or services from a merchant seller in a standard (as opposed to an extraordinary) transaction.

Bylaws The rules and regulations adopted by a corporation or other association for the purpose of self-regulation, especially of day-to-day matters not covered by other documents.

C

Cancel To delete or annul; to strike out or obliterate; to revoke.

Cancellation Any action shown on the face of a contract that indicates an intent to destroy the obligation of the contract.

Capacity Legal ability to perform an act or to assume an obligation: legal measurement of power, competence, or ability.

Capital contribution The money invested in a business venture by the owners in return for their shares of ownership: the value of any assets invested in a business venture in lieu of money.

Carrier see common carrier.

Cases and controversies Judicial proceedings between parties involving an actual fact situation on justifiable issues, and excluding advisory opinions or hypothetical situations.

Cash Money; legal tender; official currency.

Cashier's check A check that is issued by a bank and drawn against the bank's own funds and *that* is accepted upon issue.

Cash value The actual market value a thing is worth in a private sale for cash, with no portion of the payment deferred.

Causa mortis In contemplation of death (normally used in reference to a gift made by the donor because of the donor's expectation of death).

Caveat emptor Literally, let the buyer beware, meaning that the buyer needs to exercise caution since he or she assumes any and all risks in the transaction.

Caveat venditor Literally, let the seller beware, meaning that the seller is responsible for any and all defects or deficiencies in the goods being sold.

Certification The act of certifying something, such as a check, in order to guarantee the signature and the amount appearing on its face.

Certiorari Literally, to be made informed of; the name of a writ issued by a court in order to review the action of an inferior court in *a* proceeding.

Charging order A court order that allows a judgment creditor to receive the profits otherwise owed to the debtor from the operation of a business in which the debtor has an interest. especially the profits of a partnership in which the debtor is a partner.

Charitable subscription A written and signed commitment to contribute money to a charity.

Charter A grant by the government that authorizes the creation and operation of a corporation.

Chattel Articles of personal (as opposed to real) property; any interest in property that is less than a freehold or a fee interest in land.

Chattel mortgage A mortgage used to create a lien on some right or

for the payment of a debt or the performance of an obligation.
Chose in action see Things in action.
Circumscribe To restrain the range or activity of something clearly and definitely.
Civil rights The personal rights and freedoms guaranteed to the citizens of the united states by the constitution.
Class action A lawsuit filed by some members of a group on behalf of all the members of the same group.
Clear and convincing proof A measure of the burden of proof that must be satisfied in a vivil case, which is more than a mere preponderance of the evidence but less than the degree of proof required in a criminal case; proof that is very convincing but not necessarily conclusive.
Clearinghouse An association of banks and financial institutions that clears items, adjusting and paying items among the banks in the city or region.
Closed shop A Business in which the employees must be members of a labor union in order to hold their employment.
Codicil An addition to a preexisting will used to explain, modify, or supplement the will.
Coinsurance clause A clause on fire insurance policies that requires that the insured maintain a predetermined percentage of the risk, based on the value of the property, or suffer a reduced coverage from the insurer in the event of a loss.
Collateral Supplementary: additional: added to; secondary. A collateral promise is made secondarily and is added to the primary, or original, promise made by another. Collateral also

refers to security, things that are given as further assurance that a promise or performance will be forthcoming.

Collective bargaining Contract negotiations between the management of a company and representatives of labor, or the employees, which determines such things as working conditions, wages, hours, and so on.

Comity The informal and voluntary recognition of the sovereignty of another nation.

Commercial frustration Excuse of performance in a contract when the contract depends on the existence of a person or thing and the person or thing ceases to exist; excuse of performance when a contract becomes impossible to perform because of an act of God or a change in the law.

Commercial paper Negotiable instruments; checks, Drafts, notes, and certificates of deposit, instruments that are used as credit instruments and/or as sub stitutes for money and that are governed by Article 3 of the UCC.

Commercial unit The size or quantity of packaged goods called for in a contract, such as a drone eggs. **a ton of coal, and so on.**

Commission A fee paid to an agent or employee for the performance of some task or service, especially, a fee paid as a percentage of the total monies to be received.

Common carrier A person or firm offering to the general public, for compensation, the service of transporting people or goods.

Common law Unwritten law, the law as developed by the use of precedent and stare decisis, whereby the court uses the opinions in earlier, similar cases to reach a verdict in a current case.

Common stock The basic and only necessary ownership class of stock.

Communication The exchange of knowledge or information between parties: a statement made by one party to another.

Community property Property held jointly by a husband and wife; normally, property acquired during the marriage and excluding gifts or inheritances received by one spouse only.

Comparative negligence A means of measuring negligence whereby the negligence of the plaintiff is compared with that of the defendant, and the award to the plaintiff is reduced by the amount of negligence attributed to the plaintiff.

Compensation Indemnification: payment for ser- vices rendered: payment for damages suffered

Compensatory damages Those damages necessary to compensate the injured party or to make the injured party whole; actual damages.

Competitors Persons who offer to perform the same, or a very similar, service and who normally attempt to distinguish their own services on the basis of price, quality, or other differences.

Complaint The first formal filing of a plaintiff in a civil case, setting out the alleged cause of action and a prayer for relief.

Composition An agreement between a debtor and his or her creditors whereby each creditor agrees to accept less than is owed in exchange for an earlier payment, and a discharge is granted to the debtor upon the performance of the agreed consideration.

Conclusive presumption A presumption whose establishment precludes any further evidence or argument to the contrary.

Concurrent jurisdiction Jurisdiction among sev eral different courts, with the appropriate court being decided by the party who files suit.

Condemnation The process by which privately held land is taken for a public use despite the owner's objection and lack of consent. See also Eminent domain.

Condition An event whose occurrence will create the obligation to perform a contractual promise or will excuse the performance of a contractual promise.

Conditional sales contract A sales contract in which the transfer of title to the buyer is subject to a condition, most commonly the payment of the full purchase price by the buyer.

Condition precedent A condition that must occur before the obligation to perform will exist.
Conditions concurrent Conditions that are mutually dependent and that must occur at or very near the same time.
Condition subsequent A condition whose occurrence will excuse the performance of a contractual obligation.
Confession of judgment A judgment in which the defendant has given the plaintiff written permission to enter a judgment in favor of the plaintiff against the defendant in the event of a lawsuit.
Confirmation The supporting of a statement with proof; the ratification of a contract that was avoid- able; a firming up or finalizing of an agreement that was in doubt.
Confiscation A taking of private property by the government in violation of international law. Conforming In agreement; matching the description; acceptable.
Confusion A blending, intermixing, or commingling that causes the individual parts to become obscured. Consent Voluntary approval of or agreement with the conduct done by, or proposed to be done by, another.
Consent decree A decree entered by agreement of the parties and in the form of a solemn contract.
Consequential damages Indirect damages; dam- ages that arise as a consequence of an act or omission and not as a direct result.
Consideration The legal benefit conferred or the of a contract; the legal measure of value given in a contract.
Consignee A person to whom goods are shipped.
Consignment A bailment for the sale of goods. The consignor ships goods to the consignee so that the consignee can sell those goods to purchasers.
Consignor A person who ships goods to another person.
Consolidate To combine; to join together, to merge. Conspicuous Reasonably calculated to be seen and noticed; expected to convey the information to be imparted; obvious to the eye.
Conspiracy A combining of two or more persons for the purpose of performing an unlawful act or of violating public policy.
Constitution A written document that is the supreme law of the jurisdiction it purports to govern. Constructive condition A condition imposed by law.
Construction eviction An inability of the purchase or lessee to obtain possession or occupancy because of an outstanding claim.
Constructive fraud An act or omission that operates as would a virtual fraud to the detriment of another or to the detriment of public policy even though the actor did not intend it to be a fraud.
Constructive notice Information of which a person should have been aware from a review of all the facts and circumstances; information that a person is treated as knowing, whether actually known or not.
Constructive trust A trust imposed by law to pre- vent the unjust enrichment of the purported owner of the "trust" property.
Consumer A user; a person who utilizes economic goods, especially for personal or household use.
Consumer goods purchased for personal or household use, in contrast to goods purchased for inventory or equipment use.
Consumer price index Measurement of how the price of a group of consumer goods changes between two time periods.
Contingent Possible but not assured or definite: subject to the occurrence of a condition.
Contract A legally enforceable agreement between two or more persons, supported by adequate consideration and having the requisite legal form. Contract of adhesion

plaintiff that, taken together with the negligence of the defendant, makes up the proximate cause of the accident: a defense to a lawsuit for negligence in which the defendant shows that the plaintiff was at fault in the occurrence.

Conversion

The unauthorized and wrongful exercise of dominion and control over the personal property of another to the harm of that other person.

Convert

To change the nature of, as from realproperty to personal property.

Conveyance Copyright

A transfer of legal or equitable title. A legally protected, exclusive right to sell, to publish, or to reproduce artistic, musical or literary works for the life of the author plus fiftyyears.

Corporate charter The right to conduct business granted to the corporation by the state in which the firm was incorporated, as evidenced by the formal legal papers and documents shown as the charter. Corporation.

An artificial person created under the statutes of a state or federal government, organized for the purpose set out in the application for cor- porate existence.

CorpusLiterally, body; the principal sum contrib- uted, as to a trust, as distinguished from the income generated by that principal sum.

Counteroffer A reply to an offer in which the offeree rejects the original offer and substitutes a new offer, whereby the former offeree becomes the offeror. Court of equity A separate court system developed at common law to administer justice and fairness in cases that were not actionable "at law."

CovenantA promise, often in writing and under seal, pledging that something has been done or will be done.

Covenant not to compete A clause in a contract. whereby one party agrees not to compete with the other party after the termination of the contract.

CoverIn the law of sales, to purchase similar goods from another source upon the breach of a sales contract by the seller; in insurance, to agree to insure a named asset or thing of value.

CreatorA person who establishes a trust by transferring assets (the corpus) to a trustee for the welfare of the beneficiary.

Credit The ability to purchase goods or services on

time; the opposite of a debt, or a debt looked at from the perspective of the creditor.

Creditor A person to whom a debt is owed. Creditor beneficiary A third party who is des ignited to receive the benefits of a promise or a performance in satisfaction of a legal obligation owed by one of the parties to the contract.

CrimeAn act or conduct against society or the state that is subject to penal sanctions.

Criminal law The body of law that is designed to protect society at large rather than the individual members of society. Criminal law provides for penal treatment of convicted offenders of the law.

Any punishment or penalty that is disproportionate to the offense. that amounts to barbaric treatment, or that shocks the community standards. Cumulative voting A voting method that allows

Cruel and unusual punishmentvoters to take the total number of votes they are authorized to cast and allocate them in any manner they see fit. They may cast all their votes for one candidate or allocate them in any proportion among the various candidates.

Cure In the law of sales, the right of the seller to correct any nonconformity of the goods tendered to the buyer in order to avoid a breach of contract. Current rate The interest rate that financial institutions are currently charging on loans.

Cypress doctrine Literally, as near as possible: a doctrine utilized in equity to carry out the wishes of a testator or of a trustee when the original wish is impossible or when it violates public policy (used especially in the area of charitable trusts when the original beneficiary has been improperly described or has ceased to exist).

D

Damages Compensation and/or indemnification recovered in a court proceeding for injuries suffered by one person at the hands or by the conduct of another.

D/b/a Abbreviation for "doing business as": the name under which a business is conducted.

Deadlock A tie; a standstill.

DebtAn amount of money owed to another; anobligation.

Debtor A person who owes an obligation to acreditor.

Debtor in possession A term used in bankruptcy proceedings to signify that the debtor in a reor-

Deposition
Testimony of a witness taken outside of a trial and reduced to a writing and authenticated. A deposition may be used to preserve the testimony of a witness who is not available at trial or to impeach the testimony offered by a witness during the trial.
Depositor A person who makes a deposit a bank customer who places funds into an account with the bank for later personal use.
Derivative action
A suit filed by a shareholder on behalf of the corporation to enforce a corporate cause of action. Destination contract A contract for the transportation of goods by a common or independent carrier in which the seller remains liable for any losses or damages to the goods until the goods have reached a named destination.
Deterrent Something that discourages or prevents the occurrence of an act.
Detriment Loss or harm suffered to a person or a
person's property; the forbearance of a legal right. Diligence Prudence; care; attention to details and surroundings.
Directors Persons elected by the shareholders of a corporation to act as a board in managing the affairs of that corporation; managers: supervisors. Disaffirm To revoke a prior commitment or promise; to decline to perform what one had previously agreed to perform (most often used in the area of contract law when the disaffirming party asserts a lack of capacity to have entered the contract that is being repudiated).
Discharge To release from obligation or liability: to excuse from any further duty to perform. Disclaim To deny; to renounce; to disavow. Disclaimer A statement by a seller, often in writing that attempts to deny the existence of certain war- ranty protections that are normally afforded to the buyer. Disclosed principal A principal whose existence and identity are made known to the third person with whom the agent is dealing.
Disclosure
A revealing of what would otherwise

be unknown. Discovery A pretrial procedure for allowing the parties to the litigation to narrow the issues by making one another aware of certain requested
Discretion wise conduct; caution; exercise of care and concern.

Dishonor A refusal to accept and/or to pay a negotiable instrument upon due and proper presentment to the drawee or maker.

Dissent The minority opinion in a court case; the'ramming of the judges who disagreed with themalooty position.

Dissolution The termination of existence of a corp,u,mon or partnership, at least in the form pre, ,00sly known and followed. Dissolution does notnecessarily mean that the business will cease to°relate, only that the prior form no longer exists.

Diversification The addition of variety, as by theink fusion of a new product line or entry into a newbusiness area; an expansion into new fields and awes of interest.

Diversity of citizenship A jurisdictional aspect oftrials in federal courts wherein the parties on the(filletcm sides of a lawsuit are residents of differentstates.

Divest To take away from, to deprive; the oppositeof invest.

Dividends A portion of a corporation's profits paidout to its shareholders on a pro rata basis, as voted In The board of directors; in insurance, the refundpremiums paid into the company by thepoll.' holders, who are also the owners of the instbali,11COMPCMY.

Document An instrument that may be used as

Document of title Written evidence of the legalof a particular asset.

Domestic Relating to a home, a domicile, or theplace of birth or origin.

Domicile The legal home or residence of a person;the state of incorporation of a corporation.

Donee The recipient of a gift or a bequest.

Donee **beneficiary** A third party who receives thebenefits of a contract between two other panics forno reason except the donative intent of the donor.

Donor A person who gives a gift or makes a bequest.

Double jeopardy A second prosecution for the sameoffense or conduct. which is prohibited by theConstitution.

Drawee The person against whom an order instrument is drawn and who is expected to acceptthe instrument and to pay it upon maturity andproper presentment.

Drawer The person lovho issues an **and**who gives the order to pay the nimitiloriothe drawee.

Due diligence The degree of prudent that can reasonably be expected from an **prudent person** under the

Due process A measure of the approplialeiley, till a legal proceeding from the perspective of builtcourt and the individual; the proper exert ire power and authority by the court and the legislaturewithin the rules and principles established by courts.

Duress An unlawful imposition whereby a personloses the free exercise of his or her will because ofan improper threat made upon the person or uponany other person or thing that is of sufficient importance to the person to constrain the exercise offree will.

Duty That which a person is expected and requiredto perform, a legal obligation to perform in a certainmanner or to refrain from performing in a certainmanner.

E

Easement The right to use the land of anotherperson, as for ingress and egress; a limited right touse and enjoy the land of another.

Emancipate To free from the control or power ofanother; to release from parental care and to makelegally independent.

Embezzlement The fraudulent appropriation ofmoney by a person entrusted with the money.

Eminent domain The power of a government bodyto take private property for a public use or benefit,subject to compliance with due process requirementsand payment of a fair value.

Employee A person who occupies some permanentposition; a person who accepts a job for wages andoperates under the control of the employer.

Employer One who uses the services of another,usually by hiring the other person to perform forwages.

Employment The act of hiring employees; the workenvironment.

Encumbrance A claim or a right against propertyowned by another, such as a mortgage or a lien.

Endorsee A person to whom a document or instrument is endorsed.

Endorsement The signing of one's name on **the**

back of a negotiable instrument in order to properly negotiate it to the next holder: a provision added to an insurance contract that alters the nature or the risk of the basic policy.

Endorser A person Nvlio endorses. as by signinghis or her name on the back of a negotiable instrument in order to further negotiate it.

Endowment A life insurance policy that calls forthe payment of the face amount of the policy tothe insured at a certain age or date or for the paymentof the face amount to the beneficiary if the insureddies before that time; the establishment of a fundfor the use and benefit of a charitable institution.

Enjoin To order by means of an injunction.

Entity A separate being; a thing with a separate and independent legal existence.

Entrustment The transfer of possession to anotherperson of something that one owns or to whichone isentitled, without any transfer of title, as ina consignment.

Equal protection The requirement that the courtsand laws of a state shall apply to all persons withinthe jurisdiction of the state in like manner, withoutregard to any extraneous factors such as race, age,or sex, the equality of treatment of all persons whocome before the court

Equipment The fixed assets of a business, excludinglands and buildings; those assets that a businessneeds to carry out its commercial function.

Equitable Fair; just; being a matter for a court ofequity and not for a court of law.

Equity Abranch of the legal system designed toprovide remedies where no remedy existed at common law; a system designed to provide "fairness"when there was no suitable remedy "at law."

Escheat The reversion of lands to the state whichoccurs when a decedent has no legal heirs.

Escrow Aconditional delivery of a deed or of property to a trustee or escrow holder, who in turndelivers it to the grantee upon final performance.

Estate The assets of a bankrupt; the assets owned by a decedent at the time of death; the interests aperson holds in land.

Estoppel A legal bar that prevents a person fromalleging or denying a fact because that person'sprevious conduct or statements preclude the denialof facts contrary to the conduct or statements.

Eviction The deprivation of one's right to possess land by court action or order.

Evidence Any type Of proof presented at trial tosupport a position advocated by the presenting party.

Examiner A person appointed by the court to lookinto t heaffairs and the financial condition of adebtor in a bankruptcy proceeding.

Exchange To trade; to give something to another,receiving something of equivalent value from theother; to trade foreign currency for domestic currencyand domestic currency for foreign currency.

Exclusive-dealing contract A contract that, by itsterms, obligates the promisee to deal with only thepromisor in a designated area of trade or commerce.

Exclusive jurisdiction The right of one court tohear a particular case or controversy, to the exclusionof any and all other courts.

Exculpatory clause A part of an agreement inwhich a prospective plaintiff agrees in advance notto seek to hold the prospective defendant liable forcertain things for which that person would otherwisebe liable.

Excuse The reason given for not having donesomething that was to have been done; the rationalization of a nonperformance.

Executed contract Acontract that has been fullyperformed by all parties to it.

Execution The full and complete carrying out ofsome act; a legal remedy for the enforcement of acourt's verdict or judgment.

Executor (executrix) The man (woman) namedand appointed in a will by a testator to carry outthe administration of the estate as established bythe will.

Executor contractA contract that has been lessthan fully performed, with performance still to occur.

Exemplary damages See **Punitive damages.**

Exempt Excused from a duty or obligation generally

imposed on other persons in similar circumstances.

Ex parte For one party only; without notice to theother side.

Expelled Ejected; put out; removed.

Expert A person qualified to testify or to speak asan authority on a given subject because of specialskill, training, or knowledge in the subject area.

Export To send out of the country, especially goodsor articles of commerce.

Ex post facto Literally, after the fact An ex postfacto law is enacted after the action has occurredand often is designed to be retroactive.

Express Actually stated; clear and definite.

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Export To send out of the country, especially goods or articles of commerce. Ex post facto Literally, after the fact An ex post facto law is enacted after the action has occurred and often is designed to be retroactive.

Express Actually stated; clear and definite.

Express condition tioned in a contract.

Express warranty

A condition specifically men

A statement about the quality or condition of goods that the seller gives to the buyer at the time of the sale and that is intended as a part of the contract.

Expropriation A taking of private property by government that is not in violation of international

law.

Extension An addition to something that already exists, as in the granting of additional time to com- plete a performance or to make a payment. Extraterritoriality The state of being exempt from the jurisdiction of local laws or local jurisdiction.

F

Face value The value dictated by the face of an instrument or document without reference to any external documents.

Fact Something actual; an actual occurrence.

Factor's lienA claim or encumbrance on property held by a consignee for compensation owed by the principal.

False imprisonment The unlawful arrest or detention of a person without permission, a warrant, or legal justification for doing so.

Farm goods Goods produced by or used in the operation of a farm.

Fellow servant doctrine A common law defense to a claim for damages by an employee injured on the job; a rule that protects the employer from liability to an employee for job-related injuries caused by a fellow employee.

Felony A crime punishable by death or incarceration in a penitentiary.

Fiduciary One who holds a special position of trust or confidence and who is thereby expected to act with the utmost good faith and loyalty.

Ling The act of placing upon file; the act of de- positing something in the custody of a public official to be held as a matter of recordnance charge The consideration paid for the privilege of paying over time rather than paying cash at the time of contract performance; interest on a loan.

Financing statement A legal document signed by the parties to a secured transaction that describes the collateral involved and that is filed with the appropriate state officials.

Firm offer An offer made by a merchant to a mer chant calling for an irrevocable period in which the offer may be accepted and during which the offer may not be revoked even though there is no consideration for holding it open.

FixtureAn item that was personal property but that has become so permanently attached to real property as to be a part of the real property. Forbearance A refraining from acting, the condition of not doing what one would otherwise legally be entitled to do.

Foreclosure A legal proceeding designed to bar or to extinguish the rights of a mortgagor to the property mortgaged. Foreign bill A negotiable bill of exchange drawn in one state or country upon a drawee in another state or country. Foreign corporation

A corporation incorporated in one state or country and doing business in another state or country.

Foreseeable Capable of being anticipated as the reasonable result of a particular course of action or of a lack of action.

Forfeiture

The loss of a right or privilege as a penalty

for certain conduct.

Forgery The fraudulent making or altering of a written document or instrument with the intent of affecting the rights and duties of another; the signing of another person's name without permission or authority.

Formal

Of a particular form, as required by law, in order to be valid and enforceable.

Formal will

A testamentary document prepared in strict conformity with the state statute for the preparation of such a document and published and witnessed in its execution.

Franchise A special privilege granted by a corpo-

ration to conduct business under the corporate name. Fraud The intentional misstatement of a material fact made for the purpose of inducing the other party to enter an agreement in reliance on the misstated fact; the intentional concealment of a defect whose existence should have been made known to the other party. Fraudulent conveyance

A transfer of property made with the intent of defrauding **a** creditor, of hindering a creditor's efforts to obtain the property transferred, or of placing such properly beyond thereach Of the creditor.

Fungible Virtually identical: interchangeable; descriptive Of things that belong to a class and that are not identifiable individually.

Future advances clause A clause commonly use din *secured* transactions that provides for currently pledged collateral to cover any future credit extended by the covered creditor without need to resort to a subsequent security agreement.

G

Garnishment A legal proceeding in which assets of a debtor that are in the hands of a third person are ordered held by the third person or turned over to the creditor in full or partial satisfaction of the debt

General partnership See **Partnership.**

Gift An intentional, gratuitous transfer of property from a donor to a donee.

Good faith Honesty in fact in the transaction; a lack of evil intent or motive.

Goods Tangible, personal property; things that have a physical being and are movable.

Goodwill The reputation of a business; the name value of a business; an intangible asset based on community perceptions.

Grace period An insurance term designating the time period **permitted** after a premium payment is due during which the insured may tender the premium and retain the insurance coverage.

Grand **jury** A jury *convened* for the purpose of hearing evidence to decide if there is probable cause **to** believe that a crime has been committed and to issue indictments if it finds the requisite probable *cause.*

Grant To bestow on, confer on, or deliver to someone other than the party making the grant.

Grant deed A deed that transfers an estate in land but with no warranties made by the grantor in the transfer.

Grantee The recipient of a grant.

Grantor **The** person who makes the transfer in a grant.

Gratuitous Without consideration; not governed bycontract law.

Guarantor One who offers a guaranty by agreeing 10 pay the debts of *another if* **that person does** am pay: a collateral **obligor.**

Guaranty A promise to pay the debts or &Int of another **on condition that the creditor first** ate to collect **the debt from the debtor and be untie** to do so.

Guardian A person legally responsible for to care of **Affairs of another who lacks the less** capacity to **do.**

H

Habeas corpus Literally, you should have be boa,- the technical **name for a number of common taw** writs used **to bring a person before a coon and** subject to **its jurisdiction; the right to obtain** such a**writ as a protection against unlawful impisonmerrt,**

Habitability Suitability of premises for human, occupancy.

Handwritten Manually subscribed; written by hand, **as opposed to being typed. preprinted. Or** otherwise **inscribed by machine.**

Harm Physical or mental damage or injury. Heir A person who is designated by statute to receive the **assets that are not disposed of by a decedent's** will.

Holder A person who has legally acquired possession

Of **a negotiable instrument by endorsement and or** delivery.

Holder in due course A holder of a negotiable instrument who **acquired possession for value.** In good faith, **and without notice of any defects or** defenses **that affect liability on the instrument.**

Holographic Entirely handwritten.

Holographic will A type of will that is entirely handwritten by the testator, **personally and man-ually,** and is dated **and signed.**

Horizontal merger A merger between two or MOM firm sat the same level of **the distributive** chain- merger between **competing firms.**

Falacious; nominal as opposed **to sub-**stantial; of **false appearance.**

I

Impair To **lessen or** diminish: to make **Nvorse:**interfere**with a legal right or remedy.**

Impeach As an aspect of evidence. the veracity of a witness by using **evidence that** refutes the witness or his or her testimony.

Implied Assumed or gathered by a consideration of all the circumstances; not expressed; deduced. That authority actually given Implied authority by a principal to an agent but not expressed; the authority reasonably expected to be used and to be necessary in carrying out the purpose of the agency. Implied consent Agreement presumed to exist be- cause of the actions or inactions of a party to the agreement.

Implied contract

A contract imposed by law be-**cause of the conduct of the parties. Implied warranty**

A warranty protection that un- less properly disclaimed by the warrantor is imposed by operation of law because of the nature of thetransaction.

Import Goods or property brought into one country from another country.

Impossibility Something that cannot possibly be performed because of natural or legal restrictions. A person who assumes a name or an Imposter identity not his or her own for the purpose of deceiving another.

Impracticable Not capable of being performed by the means currently available; commercially unreasonable.

Incidental authority Actual authority possessed

by an agent in minor areas for which no specific directions were given. Incidental beneficiary

A person who happens to benefit from a contract between two other parties but who was not intended to benefit and who has no legal recourse if the contract is not performed. A clause in an insurance Incontestability clause policy that removes the right of the insurer to chal- lenge the application information after some pre- determined time period.

Incorporation The act of forming a corporation by

compliance with the applicable state statutes. Persons who originate a corporation. Reimbursement to a person for

Incorporators Indemnification

losses sustained; protection from losses or harm. A person hired to perform Independent contractor a task for another and who totally controls the means to be used in attaining the desired results, being subject to control of the employer only in regard to the ends to be attained.

IndictmentA formal accusation of criminal conduct issued by a grand jury and then tried before a petit

Informal Not according to any specific legal form Infringement A violation of a property right of another, especially in the areas of copyrights and patents; an unauthorized use of property belonging to another.
In gross or thing.
Personal; not annexed to another person
Inheritance Property that a person receives from
the estate of a decedent.
Injunction A writ issued by a court of equity or dering a person to do or to refrain from doing some specified act.
Injury Wrong or damages done to a person or a person's property or reputation.
In pari delicto Equally at fault; equally guilty.
In personal Against a particular person. Inquiry A request for information; a question con- cerning terms or conditions.
In rem Against a thing: done without regard to any particular person and thus done "against the entire world."
Insane Of unsound mind; deranged; mad. The term insane has many meanings in law, depending upon the circumstances in which it is used. In contract law, it may mean committed to an institution or unable to look out for one's best interests.
The state of being insane.
Insanity Insider A person in a position of power; one who has access to information not generally available to the public.
Insolvent A person unable to pay debts as they come due; one who has liabilities in excess of assets. A negotiable instrument that calls Installment note for periodic payments of a debt at predetermined times.
Insurable interest A legal or equitable interest in the insured property or life: a sufficient connection to the insured property or life to ensure that the contract is to provide for reimbursement of loss and is not a wagering proposition.
Insurance A method of providing for risk sharing among persons facing the same sort of risk by paying premiums into a fund to be used to reimburse those members of the group harmed by the occurrence of the risk.
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A right that may be represented

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A legal or equitable interest in the insured property or life; a sufficient connection to the insured property or life to ensure that the contract is to provide for reimbursement of loss and is not a wagering proposition.
Insurance A method of providing for risk sharing among persons facing the same sort of risk by paying premiums into a fund to be used to reimburse those members of the group harmed by the occurrence of the risk.
Insured Insurer A person protected by an insurance policy. A person who issues an insurance policy. An asset that does not have Intangible property physical form or existence.
Intangible right A right that may be represented by something such as a writing but that is of value in and of itself without regard to the writing. Integration
The act of making whole or entire; the entire writing or writings entered into by the parties as their final and complete contract agreement. Intended beneficiary A third party who was clearly

meant to benefit from the contract by one of the original parties to the contract.

Intent The purpose for which a person acts; meaning.

Intentional tort A private or civil wrong done willfully or with reckless disregard for the results that ensue.

Interest The cost imposed by a creditor for the use of money over time.

Interpretation The defining, discovering, and ex- planning of unclear language. Interrogatory

A series of written questions issued to a party and answered under oath as a portion of the pretrial discovery stage of a lawsuit.

Interstate Between two or more states or between one state and a foreign country.

Inter vivos Between living persons; during life. Intestate Without a will; a person who dies without leaving a will.

Intestate share

The amount a person inherits from the estate of a decedent who left no valid will; the inheritance provided for in the state statute of descent and distribution.

Intestate succession statute The state law governing the distribution of the estate of a decedent who left no valid will.

Intoxication Drunkenness; lack of sobriety; the condition of being under the influence of alcoholic beverages. A number of states also consider being under the influence of a narcotic or illegal controlled substance (drug) as intoxication.

In transit On the way; being delivered.

Intrastate

Wholly within the borders of one state. Invasion of privacy Infringement of the right to be left alone, free from disturbance by others. Inventory Stock in trade; goods held for the purpose of resale to customers in the ordinary course of business.

Investigation A detailed search; a legal inquiry or examination. Investment security Bonds, notes, certificates, and other instruments or contracts from which one ex- pacts to receive a return primarily from the efforts of others.

J

Joint and several liability The liability faced when a creditor may elect to sue each of the debes individually or to sue all of them together. Joint liability The liability faced when a credite must sue a collection of debtors together and individually.

Joint tenants Tenants who acquired tide to propemy at the same time, from the same person, in the same interest, and with the same rights to possesion and usage.

Joint venture A commercial undertaking by woor more persons with a limited time or purpose which is similar to a partnership but without the continuous nature of a partnership.

Judge (Noun) the officer who presides over a com of law or equity. (Verb) to decide judicially (property to adjudge).

Judgment The final finding, or opinion, of a coun at the conclusion of an action.

Judgment creditor A creditor who has obtained a court verdict that allows the enforcement of an execution.

Judgment NOV A judgment non obstade verdict

meaning notwithstanding the verdict: a judgment entered by the court in direct contravention of the jury verdict, normally so entered because the jury verdict is unreasonable under all the facts and circumstances of the case.

Judgment rate The interest rate imposed and to be paid on a judgment ordered by a court Judicial restraint A doctrine under which the court refuses to enter certain areas in official opinions the exercise of discretion by a court in determining which cases to hear or which cases to decide. Judicial review The examination and hearing of a case, especially by an appellate court. Junior secured party Any secured party whose security interest is subordinate to that of the priority secured party. Implied Assumed or gathered by a consideration of all the circumstances; not expressed; deduced. Implied authority by a principal to an agent but not expressed; the authority reasonably expected to be used and to be necessary in carrying out the purpose of the

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In gross or thing. Inheritance
Property that a person receives fromthe estate of a decedent.
Injunction A writ issued by a court of equity or dering a person to do or to refrain from doing some specified act.
Injury Wrong or damages done to a person or a person's property or reputation.

Impair delic to Equally at fault; equally guilty.
In personal Against a particular person. Inquiry A request for information; a question concerning terms or conditions.
In rem Against a thing: done without regard to any particular person and thus done "against the entire world."
Insane Of unsound mind; deranged; mad. The term insane has many meanings in law, depending upon the circumstances in which it is used. In contract law, it may mean committed to an institution or unable to look out for one's best interests.
Insanity Insider The state of being insane.
A person in a position of power; one who has access to information not generally available to the public.
Insolvent A person unable to pay debts as they come due; one who has liabilities in excess of assets, A negotiable instrument that calls Installment note for periodic payments of a debt at predetermined times.
Insurable interest A legal or equitable interest in the insured property or life; a sufficient connection to the insured property or life to ensure that the contract is to provide for reimbursement of loss and is not a wagering proposition.
A method of providing for risk sharing Insurance among persons facing the same sort of risk by paying premiums into a fund to be used to reimburse those members of the group harmed by the occurrence of the risk.
Insured Insurer A person protected by an insurance policy. A person who issues an insurance policy. An asset that does not have Intangible property physical form or existence. Intangible right
A right that may be represented

by something such as a writing but that is of value in and of itself without regard to the writing. Integration The act of making whole or entire; the entire writing or writings entered into by the parties as their final and complete contract agreement.
Intended beneficiary
A third party who was clearly meant to benefit from the contract by one of the original parties to the contract.
Intent The purpose for which a person acts; meaning.
Intentional tort A private or civil wrong done willfully or with reckless disregard for the results that ensue.
Interest The cost imposed by a creditor for the use of money over time.
Interpretation The defining, discovering, and explaining of unclear language.
Interrogatory A series of written questions issued to a party and answered under oath as a portion of the pretrial discovery stage of a lawsuit. Interstate Between two or more states or between one state and a foreign country.
Inter vivos Between living persons; during life. Intestate Without a will; a person who dies without leaving a will.
Intestate share The amount a person inherits from the estate of a decedent who left no valid will; the inheritance provided for in the state statute of descent and distribution.
Intestate succession statute The state law governing the distribution of the estate of a decedent who left no valid will.
Intoxication Drunkenness; lack of sobriety; the condition of being under the influence of alcoholic beverages. A number of states also consider being under the influence of a narcotic or illegal controlled substance (drug) as intoxication.
In transit On the way; being delivered.

Intrastate Wholly within the borders of one state. Invasion of privacy Infringement of the right to be left alone, free from disturbance by others. Inventory Stock in trade; goods held for the purpose of resale to customers in the ordinary course of business.
Investigation A detailed search; a legal inquiry or
examination. Investment security Bonds, notes, certificates, and other instruments or contracts from which one expects to receive a return primarily from the efforts of others.

J

Joint and several liability The liability faced whe a creditor may elect to sue each of the dens individually or to sue all of them together Joint liability The liability faced when a credit must sue a collection of debtors together and not individually.
Joint tenants Tenants who acquired title to property at the same time, from the same person, in the same interest, and with the same rights to possession and usage.
Joint venture A commercial undertaking by towor more persons with a limited time or purpose which is similar to a partnership but without the continuous nature of a partnership Judge (Noun) the officer who presides over a com of law or equity. (Verb) to decide judicially (property to adjudge).
Judgment The final finding, or opinion, of a count at the conclusion of an action.
Judgment creditor A creditor who has obtained a court verdict that allows the enforcement of an execution.
Judgment NOV A judgment non obstante verdict
meaning notwithstanding the verdict: a judgment entered by the court in direct contravention of the jury verdict, normally so entered because the jury verdict is unreasonable under all the facts and de constancies of the case.
Judgment rate The interest rate imposed and to be paid on a judgment ordered by a court Judicial restraint A doctrine under which the court refuses to enter certain areas in official opinions the exercise of discretion by a court in determining which cases to hear or which cases to decide Judicial review The examination and hearing of a case, especially by an appellate court. Junior secured party Any secured party whose security interest is subordinate to that of the priority secured party.

Lost property Property that is accidentally or un- intentionally lost by the owner and whose location is unknown and whose recovery is difficult. Loyalty Faithfulness; adherence to the concept of supporting another over any competing interests; single-minded support and purpose.

M

Maker In negotiable instruments, the person who promises to pay the note or certificate of deposit; the person who developes, creates, or causes to exist.
Mala in se Morally wrong: wrong in and of itself. Mala prohibit Made wrong by law; pertaining to statutory offenses.
Malfeasance The performance of an illegal act or a morally wrongful act; wrongful conduct. Mandamus The name of a writ issued by a court of competent jurisdiction ordering the performance of some act, in which the order is directed to an inferior court or to a person or a corporation. Marshaling of assets The arrangement of a debtor's assets in such a manner as to maximize the protection of the creditors; the gathering and grouping of the assets of the debtor.
Master A principal who has the right to control an agent.
Material Important, essential, or necessary.

Material factA fact that is a part of the basis of the bargain; a fact without which the contract as entered would not have been made.
Mechanics' lien A statutory protection given to certain builders, artisans, and providers of materials providing for a lien on the building and the land that they have improved.
Manresa "Guilty mind"; criminal intent; the mental intent that must be shown in order to convict a person of a crime.
Mental distress Suffering in the mind, as opposed to the body; such threats as remove free will. Merchant
A person involved in the trade or commerce of a particular type of goods; one who claims to be an expert in certain types of goods; one who employs an expert in certain types of goods. Merchantability An implied warranty of quality that warrants to the buyer that the goods are of fair average quality, are fit for their normal use and purpose, and are adequately contained, packaged, and labeled. Merge To blend; to come together; to combine into one thing,
Merger The absorbing of one thing into another so that only one remains after the merging; in contract law, the extinction of one contract by absorption into another; in corporate and antitrust law, the combining of two or more firms into one resulting
firm.
Midnight deadlineWith respect to a bank, mid- night of the next banking day after the day on which it receives the item in question or the notice on which it is acting. Mining partnership
A special form of co-venture that is neither a joint venture nor a partnership in the literal sense and that involves a joint effort to develop a mine or to develop oil or gas leases, with
a sharing of profits and a sharing of expenses, Minor One not yet of legal age; an infant in the law; one lacking the statutory age to be considered an adult.
Minority
The period before a person reaches the legal age of majority; the period of legal infancy; the justices who disagree with the majority opinion; the dissent. Misdemeanor
A criminal offense of less severity than a felony and normally punishable by fine or imprisonment in other than a penitentiary. Misdescription A false description of the subject matter of a contract that causes harm to one of the parties.
Misfeasance Improper performance of some act that
could be lawfully performed.
Mislaid property Property placed somewhere and then forgotten by the owner; property intentionally placed but not recovered.
Misrepresentation The misstatement of a material
fact in the formation of a contract, made without an intent to deceive.
Mistake An error regarding the truth of facts or of law that causes a person to act or to refrain from acting in a manner other than he or she would have acted had the truth been known.
Mitigation A reduction or a minimizing of loss, liability, or penalty imposed by law.
Money Legal currency issued by a recognized government entity; legal media of exchange.

Monopolize To assume complete control over to attempt to gain or to retain a monopoly.
Monopoly The power of a firm exclusively to carry on a business or a trade to the exclusion of all competitors.
Moot Mortgage Subject to argument: not settled or decided. A conditional transfer of property as se- curity for a debt; an estate in land created by the granting of the estate but intended as security and becoming void if the debt is repaid.
Mortgagee The person who receives a mortgage: the creditor. Mortgage insurance
An insurance policy takeout by a mortgagor to pay off the debt in the event that the insured risk occurs during the mortgage period.

Mortgage note A promissory note issued in con- junction with a mortgage specifying the terms for repayment of the loan by the debtor in order to cancel the mortgage.
Mortgagor The person who gives a mortgage as security; the debtor.

N

NationalizationThe act of a government in pro- claiming that a business or other property has be come the property of the government and that individual owners have been removed from or deprived of the property.
Navigable watersThe commercial waterways of a nation; those streams, rivers, and lakes capable of use in commerce.
NecessaryNeeded; inevitable; unavoidable. Necessity A controlling force or compulsion that allows for no other course of conduct.
Negligence A failure to exercise due care under circumstances that require due care and that results in harm to another person.
Negligence per se Negligence in and of itself with- out reference to any external factors.
Negligently Without proper caution and care. Negotiability The quality of being transferable by endorsement or delivery. Negotiable Transferable by endorsement and de- livery so as to give the recipient the rights of the transferor.

Not subject to being assigned. In contract law, certain rights are no assignable because of the personal nature of the duty. Nonconforming
Not in compliance with the terms of the agreement or description. Nonexempt assets. Those assets of the debtor that may not be protected and retained in a bankruptcy proceeding; those assets that will be liquidated in bankruptcy in order to satisfy the claims of creditors. No forfeiture clause A clause used in life insurance policies that specifies that certain rights and options of the insured will not be taken away should the policy lapse.
No justifiable No-par value stock Not properly subject to court action. Corporate stock not designated as having a par value; unvalued stock that is sold at some stated value, which is decided by the board of directors at the time of issue.
Notice The information of which a person should be aware on the basis of knowledge or general observation.
Notorious known. Novation The substitution of a new contract in place of a preexisting one, whether between the same parties or with new parties replacing one or more of the original ones Of general notice or knowledge; widely
Nuisance An annoyance or disturbance of a person's
use, occupancy, and enjoyment of property that makes the ordinary use or enjoyment uncomfortable or bothersome.

P

Perfection beyond challenge or defect; in secured transactions, the act of a creditor that serves as notice to the rest of the world that the security interest exists in his or her favor, as by filing.
The act of completing and of moving
Performance The carrying out of what one has agreed to do: the satisfaction of an obligation or contract.
Peril The risk or hazard against which an insurance policy is issued to the insured.
Perjury The making of false statements while under oath.
Persematters.
By itself: taken alone; unconnected to other Personal defense

In negotiable instruments, a de-fense that exists between the drawer or maker and the payee or some other party but that does not directly affect the instrument itself; a defense that attacks the underlying obligation but not the validity of the instrument.
Personal property Anything capable of bein gowned except land or anything permanently attached to land.
Personal representative The executor or administrator of a decedent's estate.
Petit jury "Twelve men good and true"; the ordinary jury called for in a civil or criminal trial; the finders of fact.
PlaintiffThe person who commences a civil cause of action by filing suit against the defendant.
Plea bargaining A device used in a criminal proceeding whereby the state accepts a guilty plea on a lesser offense in exchange for not bringing the defendant to trial on the greater offense with which he or she was originally charged.
Pledge A form of perfection in secured transactions whereby the debtor creates a bailment with the creditor, allowing the creditor to retain possession of the collateral until the debt is repaid.
Police power The authority conferred upon the government to enact the laws necessary to ensure domestic tranquility; the power inherent in the state to protect the lives, health, and property of its citizens by enacting and enforcing laws.
Political question Anon justifiable issue; a matter that is purely political in nature and as such is not Pooling agreement An agreement between two
or more parties to place funds into a common "pool" for allocation for certain uses, as for coverage of losses contemplated and faced by the members of the pooling group.
Possession The exercise of exclusive physical control over an asset regardless of ownership; physical dominion.
Possessory lien Astatutory claim on property evidenced by the physical control and possession of the creditor and perfected for as long as the creditor retains possession.
Postdated Dated for a time later than the time of issuance or creation.
Power The ability or the right to do something. Power does not necessarily mean right; a person may have the power to do a certain thing but doing so will involve the violation of a private civil duty. Preemption A seizing for oneself to the exclusion of all others; the right to purchase before others; in corporate law, the right of present stockholders to purchase a new issue of stock before the stock is offered to the general public.
Preference In bankruptcy, a transfer by the debtor to an unsecured creditor that allows that creditor to receive a greater percentage of his or her claim than is received by other creditors of the same class. Preferred stock A class of corporate stock that has
rights superior to those of common stock in the areas of dividends and the distribution of corporate assets. Premium The cost of insurance coverage paid by
the insured to the insurer. Prepayment clause
A contract clause that allows the debtor to pay the debt before it is due without penalty.
Preponderance of proof A degree of proof that
seems to outweigh that offered by the other side. Prescription In real property, the acquisition of an easement by the open, notorious, continuous, and hostile use of the property of another as a matter of right.
Presenter A person who presents; one who makes a presentment.
Presentment A demand upon the primary party
by the holder of a negotiable instrument for payment Price fixing An agreement between two or more competing merchants to charge a certain price for goods or services without regard to market pressures or concepts of competition; a per se violation of the Sherman Act when done in interstate commerce, Price leadership A position enjoyed by certain firms, by virtue of size, innovations, or ability, to set prices in certain channels of commerce with the understanding or

expectation that competing firms will price their products accordingly; the ability to direct the pricing policies of an industry.
Prima facie At first sight; on its face; something presumed to be true because of its appearance unless disproved by evidence to the contrary.
Primary liability The liability of the person to be looked to first for payment, who, in commercial paper, is the maker of promise paper or the drawer on order paper.
Principal In agency law, the person who appoints
an agent and bestows authority upon the agent for the purposes set out in the agency agreement. Priority Precedence; higher rights; the right to come before another.
Privacy See Invasion of privacy.
Private trust A trust created for a private purpose and having certain named or readily identifiable beneficiaries.
Privilege A benefit or advantage enjoyed by some members of a group beyond that enjoyed by the general public; the right enjoyed by certain persons to have particular types of communications treated as confidential, not subject to disclosure.
Privet of contract The relationship of two or more persons by virtue of the existence of the contract between them.
Probate (Noun) the legal procedure for establishing that a given written document was the last will and testament of a decedent and that the document is valid. (Adjective) relating to wills and the proof thereof.
Probate court
A court having jurisdiction over the states of decedents.
Procedural law The body of law that governs how legal proceedings are to be conducted.
Proceeds The property, especially money, received from the sale or disposal of assets.
Profits The excess in income over expenditures; the gain made in the sale of assets or services: the from acting in a certain way made in such a way that the promise is aware of the commitment. PromiseOne to whom a promise is made. Promis or One who makes a promise.
Promissory estoppels A doctrine that prohibits a promise from denying the making of a promise or from escaping the liability for that promise because of the justifiable reliance of the promise that the promise would be kept.
Promissory note A written promise to pay a certain
sum of money at a future time unconditionally. Promoter A person who begins the process of forming a corporation by procuring subscribers for the stock or by taking other affirmative steps toward incorporating.
PropertyAnything capable of being owned; any- thing that has value.
Property insurance Insurance that covers personal property or buildings and fixtures against certain predetermined risks and hazards.
Proprietorship The designation for an unincorporated business that has a single owner/manager. Proportionately; according to percentages.
Pro rata Prospectus A document presented by a corporation or its agents announcing the issue of corporate securities, stating the nature of the securities and the financial status of the issuing firm, and asking the general public to purchase the securities covered. Protest A formal notice of dishonor of a negotiable instrument made before and attested to by a notary public or a consul of an embassy; a formal declaration of dissent or disagreement regarding some act that has occurred or that is about to occur. Provable Capable of being proved; susceptible to being proved.
Proximate cause An act that naturally and for eseeably leads to harm or injury to another or to an event that injures another.
Proxy A person appointed and designated to act for another, especially at a public meeting, such as a meeting of the shareholders of a corporation; the document or instrument used to appoint someone to act in a representative capacity as a proxy. Proxy solicitation

A request contained in the notice of a shareholders' meeting that the shareholder allow some person to act as a proxy for that shareholder at the meeting.

Public corporation

R

Receivership An equitable remedy whereby the court appoints a receiver to manage the property involved pending the outcome of the case. Reckless Lacking proper caution; negligent; careless. Reclaim To obtain the return of something; to get
back. Reconcile To make consistent; to settle or resolve; to put into balance or harmony.
Recoupment A withholding of something that is
due; a reduction in the amount allegedly owed because of a counterclaim or a setoff.
Redeem To buy back; to remove a security interest or a mortgage by paying the total debt due. Redemption The act of redeeming or repurchasing; the revocation of a conditional sale by performance of the condition that provided for the revocation. Reformation An equitable remedy whereby the court "reforms" a contract in order to remove a mistake and to make the agreement conform to the terms to which the parties originally agreed. Registered agent A person designated by a foreign corporation as the proper person upon whom to serve process. Registration statement A formal statement com- plying with statutory information standards that is filed by a corporation in order to offer an issue of securities for sale.
Regulation An authoritative rule that deals with procedures; an executive rule or order that has the effect of law.
Reimbursement Repayment for expenditures incurred; indemnification.
Rejection A refusal to accept what is offered. Relative (Noun) kin; family member; a relation by blood or marriage.(Adjective) not capable of exact statement; comparative.
Release The surrender of a right or claim by the person possessing it to the person who would be obligated to perform; the surrender of a legal claim. Relevant market The total market in which a firm operates, including its geographic scope and all competing or substitute products.
Reliance Dependence; Dependence; expectation of truth or occurrence.
Reelection Land that is uncovered by the gradual receding of water.
Remainder beneficiary The person who is to re- ceive the benefit after the expiration of a prior interest granted in the property, with both interests created at the same time and in the same instrument.
Remand To send a case back to an inferior court for further action; to return a prisoner to custody pending trial.
Remedy A method for enforcing a right or pre- venting a violation of a right; the result of a successful
action.
Remitter The person to whom a bank draft or cashier's check is issued before it is delivered to the payee; the purchaser of such a bank draft or cashier's check.
Remuneration Salary; wages; compensation. Renunciation The abandonment of a right by the possessor of the right..
Reorganization The restructuring of an insolvent corporation so that the interests of its creditors can be protected and the corporation can continue to exist.
A feeling of regret or contrition for
Repentance past wrongdoing.

Replevin An action taken to acquire possession of goods that are not necessarily unique but that are currently unavailable in the open market; in the law of sales, a remedy of the buyer when cover is not available and specific performance is not appropriate.

Replevin To take goods under a writ for replevin. Repossession The act of regaining possession; the act of taking possession of collateral upon the default of the debtor in a secured transaction.

Representation A statement made by an applicant for insurance coverage that allows the insurer to assess the risk and that, if false and material, may allow the insurer to cancel the policy; a statement made to influence the other party to act or to refrain from acting.

Repudiate To reject, refuse, deny, or disclaim; to refuse to acknowledge or pay.

Repudiation A rejection; a refusal; a denial of a right or a refusal to perform a duty.

Requirement contract A contract in which the seller agrees to provide as much of a product or service as the buyer needs during the contract term. Rescission An annulment or cancellation; a termination of a contract through restoration of the parties to the status quo.

Reservation of title A contract clause that leaves title to the sold object with the seller until the buyer has paid the entire purchase price. In secured trans- action law, such an effort is treated as a mere security interest Security Something of value given or pledged to assure the performance of an obligation or the re- payment of a debt.

S

Security agreement The document executed by
the debtor and the creditor in establishing a secured transaction.

Security interest An interest in personal property or fixtures that secures payment or performance of an obligation.

Seller A person who transfers property in a contract for the sale of property.

Servant A person employed to perform services for
a master under the control of the master. Service charge
A fee charged for the performance of a particular service, often added to a basic fee: the charge imposed by a bank on its customer for particular services, such as certifying a check or stopping payment on a check.

Service mark A distinctive symbol designating the service offered by a particular business or individual.. Service of process The delivery of a writ or summons to the party or to the address of the party to which it is directed.

Setoff A demand that the defendant has against
the plaintiff and that is deducted from the amount the defendant is to pay to the plaintiff in settlement of the claim.

Settlement An agreement that settles a dispute as to what each party owes the other.

Settlor One who creates a trust.

Several liability The liability faced by each of the parties when the plaintiff may sue any of them and recover the entire judgment from those sued, without having to sue all of the potential defendants. Share A proportional ownership of a corporate venture with proportionate rights to management, to profits of the corporation, and to corporate assets upon dissolution. Shareholder The owner of a share of a corporation's stock; an investor in a corporation whose investment is made up of ownership shares.

Shipment contract A contract whereby the seller agrees to put conforming goods into the hands of a shipper and the buyer assumes risk of loss during transit of the goods.

Short-swing profits Profits made by officers, 10 percent shareholders, insiders, and tippers by the purchase and sale of corporate securities within six months, by matching the high sale and the lowpurchase prices and by disregarding any loses Signature Any mark, symbol, or device used with the present intent to authenticate a writing. A forbearance from speaking.

Silence Slander An oral defamation of character; an oral communication that causes a person's reputation to be held up to scorn or ridicule and that is made to any person except the person so scorned orridiculed.
Sovereign One possessing supreme power within a given sphere; the government. The doctrine that protects Sovereign immunity the state from liability for the performance of its sovereign role; an absolute defense available to the state in lawsuits, provided the government was in- volved in a government function.
Special endorsement A type of endorsement used in negotiable instruments whereby the holder designates the next holder of the instrument and another endorsement is needed to further negotiate the
instrument.
Specific performance An equitable remedy pro- vided by the courts when monetary damages would be insufficient and the object of the contract is unique and in which the court orders performance of the contract exactly as agreed.
Standing The legal right to commence an action based on a showing that the plaintiff has a substantial legal interest that needs to be protected. Stare decisis "Let the decision stand"; the policy followed by the courts in deciding current cases on the basis of precedent, thereby not disturbing established policy.
Statement A declaration of matters of fact; an allegation.
Statute A law enacted by the legislative branch of the government.
Statute of FraudsA statute requiring that certain specified types of contracts be in writing in order to be enforceable in court.
Statute of limitations A statute that provides for a definite time period during which certain legal actions must be commenced and after which they will be barred.
Statutory Related to or created by statute. Statutory standard The general conduct expected of an individual as established by law; the legal measurement of conduct for a given set of
circumstances.
Statutory warranties The warranty protection sthe

quality standards to which a product must adhere in order to comply with the statutory provisions, Stipend A fixed sum of money paid periodically, Stock The capital fund of a corporation acquired by the sale and distribution of corporate shares; the different classes of shares that a corporation issues to its owners Stop payment order An order given by a drawer of a check to the drawee that a designated check be dishonored upon presentment to the drawee. An oral stop payment order is valid for fourteen days: a written one for six months.
Strict foreclosure A means of foreclosure that precludes the right of the debtor to redeem the property and that vests title in the creditor. Strict liability Liability without fault; liability for which there is no defense assert able by the defendant. Subject matter jurisdiction The power of a court to hear only the classes of cases and controversies that are within its jurisdiction, especially important in courts of limited jurisdiction.
Sublease The lease of all or part of the premises by the lessee for some portion of the unexpired lease period of the lessee's occupancy.
Subpoena ducestecum An order issued by a court to some designated party to produce specified documents at a trial.
Subrogate To substitute one person in place of another with reference to rights or claims.
Subscription The act of writing one's name on a legal document; a written contract in which the subscriber agrees to pay money in exchange for some designated benefit or purpose.
Subsidiary A corporation controlled by another corporation that owns a majority of the subsidiary corporation's stock. Substantial performance

Performance of a con- tract that is less than perfect but that is in compliance with the essential portions of the contract; a good- faith effort to perform a contract, with performance satisfactory and the deviations minor or technical. Substantive law The portion of the law that deals with and regulates rights.
Suit Any legal action in which a plaintiff seeks the enforcement of rights or the granting of remedies. Sum certain An amount of money to be paid on a negotiable instrument, with the total amount calculable from the information contained on the face of the instrument.
Indecent entered by the court when there is no substantial issue of fact present: a judgment by the court on the basis of depositions, discovery, and other non evidential matters.
Summons A writ requiring a sheriff to inform the person named that an action has been filed against that person and ordering the person to appear in court to answer the action. Supremacy clause The clause in the Constitution that specifies that the federal government is supreme to the state governments and that federal law controls over state law if the federal law is valid. Surety A person who promises to pay or to perform in the event that the principal fails to do so.
Surety ship contract A contract in which a surety agrees to answer for the debt of another upon the default of the other and in which the surety is entitled to indemnification upon the performance of the obligation.
Suspend To delay a performance temporarily, with the expectation that performance will occur later.

T

Tenancy An interest in or possession of land in any manner.
Tenancy in partnership A form of ownership of partnership property by the partners, with a right of survivorship.
Tenant One who possesses land belonging to another; the holder of a leasehold estate.
Tenants by the entireties An estate held by a husband and wife jointly by conveyance and that carries a right of survivorship.
Tenants in common Co-ownership of real property by two or more persons, with the owners having undivided interests in the land but with title passing to them from different grantors, at different times, or in differing amounts.
Tender An offer of performance. Term insurance
A form of life insurance with no investment properties or characteristics that provides coverage for a fixed time period and that is paid only if the loss occurs during that time period. Testament The disposition of a testator's personal property according to his or her wishes upon the death of the testator.
Testamentary Pertaining to a will.
Testamentary capacity The mental capability required by law in order to make a valid will; the state of being of sufficient age to execute a will and of being aware of the nature of the act.
Testator (testatrix)a will.
Things in action A man (woman) who makes A right to receive or to recover money or personal property as the result of a judicial proceeding.
Third-party beneficiary A person who is not a party to a contract but who will benefit from the performance of the contract; one who derives some gain or benefit from the contractual performance of the parties to the contract.
Time instrument A negotiable instrument payable at some future, determinable time and not payable upon demand. Time-price differential sales contract A contract with a difference in price based on the date of payment, with one price for an immediate payment and another price if the payment is at a later date. Tippee One who is not an insider but who receives from an insider information not yet available to the general public; one who receives a tip.
Title The legal right of ownership and possession of property.

Tort The breaching of a civil duty that is the proximate cause of harm to some person or the property of some person; failure to exercise due care. Tort favor A person who commits a tort. Tortious Wrongful; pertaining to torts. Trademark A distinctive mark or symbol used to identify a particular company or its products. Transferable Capable of being assigned, transferred, negotiated, or passed from party to party with all the rights of the original holder or party being retained.

Treason An attempt to overthrow the government by overt acts; betrayal of the government to a foreign government.

Treasury stock Stock that has been issued by a corporation and then reacquired by the corporation as a part of its treasury.

Treaty A written contract or agreement entered into by two or more nations for the general welfare of the nations involved.

Treble damages A statutory remedy in antitrust actions that allows the successful plaintiff to recover three times the damages suffered as a result of the antitrust violation. property, or rights of another; unlawful entry on another's land.

Trial court The court of first impression; the court in which a cause of action is initiated and that hears evidence and testimony in reaching its verdict, A legal relationship in which one party the trustee- holds legal title to the property, while another party- the beneficiary. holds equitable

Trust

title to the same property; a combination formed by several corporations by mutual agreement.

Trust deed A security agreement similar to a mort- gage in which a deed is conveyed to a trustee as security for the payment of a debt, with the trustee having the power of sale upon default in the re- payment of the debt.

Trustee The person responsible for performing the purpose of a trust and who administers the trust property for the beneficiary.

Trustee in bankruptcy The person appointed by the bankruptcy court to act as trustee of the debtor's property for the benefit and protection of the creditors.

Tying arrangement A contract that requires the buyer to purchase one product from the seller in order to be allowed to purchase a second, difficult- to-obtain product from the same seller.

U

Ultra vires Beyond the scope or legal power of a corporation as established by the corporation's charter or by state statute.

Unconditional Not subject to any conditions; under every set of facts or circumstances; in every instance. Unconscionable

Blatantly unfair and one-sided; so unfair as to shock the conscience.

Unconstitutional Contrary to a constitution; in violation of a constitution.

Underwriter The insurer; one who insures another against some risk.

Undisclosed principal A principal whose existence and identity are unknown to the third person at the time the third person is dealing with the principal's agent. Undue influence The control of the free will of another person by unfair or improper persuasion. Unenforceable Not subject to performance by Unfair trade practice Any commercial practice that does not allow for the free exercise of trade by competitors: a false, deceptive, or unfair method of gaining trade at the expense of others.

Unilateral One-sided. Unilateral contract A contract in which only one party makes a promise, with the other party's being expected to perform an act in order to accept and thereby create a contract.

Uninsured motorist An operator of a motor vehicle who is not covered by a valid automobile or vehicular liability insurance policy.

Union shop A place of employment where only members of a labor union are employed. Unjust enrichment The receiving of something of value to which the recipient is not entitled by law or equity: the possession of something to which one is not entitled.
Un liquidated Not agreed upon; in dispute; subject to controversy or disagreement. Unqualified endorsement A type of endorsement that does not qualify the liability of the endorser to the endorsee in the event that the instrument is dishonored.
Unsecured creditor A general creditor; a creditor who has not entered into a security agreement with the debtor and who does not have specific collateral to rely on in the event of a default by the debtor. Usage of trade A practice common to the trade or industry involved or having a generally recognized meaning within the trade or industry.
Usurious contract A contract that calls for the payment of interest at a rate higher than that per- mitted under state law.
Usury

V
The charging of an interest rate in excess of the statutory maximum; the charging of excessiveinterest.
Valid Legally enforceable; properly executed and formed; legally sufficient.
Value The worth of an object in terms of money; the consideration necessary to support a simplecontract.
VenueThe geographic area in which an action is held and from which the jurors are selected; the court in which an action may be commenced, based upon the convenience of the parties.

Vertical merger A merger between firms at different levels of the distributive chain..
Vest To grant a fixed right concerning present or future use; to place in the possession of some au- thority or person.
Vicarious Serving in place of someone or something else; acting as a substitute for.
Void Of no legal effect; invalid; null.
Voidable Capable of being avoided; cancelable at the option of the disadvantaged party.
Voidable preference The act of an insolvent debtor of paying one creditor of a class, allowing that creditor to obtain a larger percentage of the debt than other creditors of the same class, within four months of the bankruptcy petition.
Void dire The examination of a prospective witness or juror to determine that person's acceptability. Voluntary Of one's own free will; spontaneous; intentional.
Voting trust A commitment by stockholders of a corporation to place their shares in trust so that the shares can be voted as a bloc; a device used to increase the voting power of a group.

W
Waiver The voluntary surrender of a legal right; the intentional surrender of a right.
Waiver of defenses clause A clause in a contract whereby one party agrees in advance not to assert certain defenses should a breach occur.
Warehouseman A person engaged in the business of receiving and storing the goods of others for a fee. Warranty A representation that becomes a part of the contract and that is made by a seller of goods at the time of the sale as to the character, quality, or nature of the goods.. Warranty deed A deed that contains warranties of title from the grantor to the grantee.
Watered stock Shares of a corporation that are issued as fully paid when in fact the full par or stated value has not been paid by the purchaser.
Will A written document prepared by a testator to provide for the disposition of the testator's estate upon his or her death.

Winding up The termination of a business enterprise by marshaling and liquidating the assets and distributing the proceeds according to state law.

Workers' compensation A type of insurance required by statute to protect workers in the event of injury or illness arising on the job and used in lieu of workers' lawsuits against the employer for such injury or illness.
Working papers The papers prepared by an accountant in the course of employment that are used to prepare the final reports and that serve as evidence of the care and skill exercised by the accountant in the performance of the job.
Writ A legal instrument, prepared in the form of a letter and addressed to a sheriff, to some other officer of the court, or to the person directly affected, that requires the performance of a specified act under order of the court.
Write of execution A writ used to enforce the judgment of a court.
Writing A reduction to tangible form. Wrong A violation of the legal rights of some other person.

Z
Zoning A division of the land governed by a city. With certain designated uses being permitted for each area and other uses being declared improper and impermissible; government regulation of permissible land use for the general welfare of the community.

END