

CORPORATE GOVERNANCE IN THE FINANCIAL SERVICES SECTOR OF SMALL ISLAND ECONOMIES: A CASE STUDY OF MAURITIUS

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Abstract

This study investigates the practices of corporate governance in the financial services sector of small island economies with special reference to banks and insurance companies in Mauritius with a view to assess the level of compliance. The financial sector is today an important economic pillar on which the government is relying given the imminent recession in the sugar industry. In this respect financial institutions play a key role because they are the core set of the financial sector. It is therefore important for people to have confidence in both banks and insurance companies of their country. This is possible by ensuring compliance with good governance. In Mauritius, the Central Bank has issued its guidelines on good corporate governance for banks and this guide is made in line with the Corporate Governance Code issued by the National Committee on Corporate Governance. Banks are also required to comply with the codes as per the Banking Act 2004 and the Financial Reporting Act 2004. In a similar vein insurance companies should comply with the National Code on Corporate Governance and relevant laws related to good governance of insurance business, such as the Insurance Act 2005, the Financial Services Commission guidelines on Corporate Governance and the Financial Services Development Act 2002. In addition insurance companies should also comply with the Companies Act 2001 and the Financial Reporting Act 2004. This paper initially reports on the practice of corporate governance in the financial services sector of small island economies by drawing data from the Financial Sector Assessment Programme of the International Monetary Fund. A content analysis of the annual reports of companies in the sector is used to assess the level of compliance to corporate governance code in Mauritius and concludes that compliance rate is above 70% as regards board's composition, audit committee, disclosure of policies and practices. This study reports that there are few cases of non-compliance with the National Code but good governance is necessary in the financial services sector to inspire stakeholders confidence.

Keywords: Corporate Governance, Financial Services Sector, Small Island Economies', Compliance Score.

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1. Introduction

Banks and non-banking financial institutions (NBFI) play a key role in the financial services system of any country. They provide a platform to facilitate the intermediation process in the financial system of an economy. Any disruption in this process will undoubtedly have catastrophic effect on the economy. For this reason, stakeholders in the financial arena have strong interest in the good governance of the financial institutions. In this vein, the Parliament, the government and the private sector in many countries have worked together to build up a strong, reliable

and stable financial system. Nevertheless, the world has been allergic to several crises ranging from crises in the manufacturing sector to crises in the financial sector. The recent Asian financial crisis is a classic example, apart from individual crisis in different countries around the world. Of course these crises are accrued to many underlying factors, but in all these cases the main factor was poor governance; a sentiment which is mirrored by many researchers when we browsed through the history of corporate governance (see, Morck, 2004; Murphy, 2004; De Jong et al. 2004).

1.1 Motivation of the study

Previous researches find that banks are crucial for industrial expansion, corporate governance of firms and capital allocation (Levine, 1997, 2003). Proper functioning of banks entails prosperity of nations. For instance sound governance mechanisms would ensure efficient capital allocation and effective corporate governance over the firms they fund. Banking crises reflect the enormous consequences of poor governance of banks (Levine, 2003). Banking crises have seriously affected economies, destabilized governments and increased poverty. There are many studies on banking failures and corporate governance but all of them have addressed the cases of large countries (see Adams, & Mehran, 2003; Barth et al, 2003; Calomiris & Powell, 2000; Caprio et al 2003; La Porta et al., 2002; Prowse, 1997; Macey & O'Hara, 2003). As yet there has been no study on corporate governance in small island economies and in particular on the financial services sector.

This study aims to bring in the research arena the state of corporate governance in the financial and non-banking financial institutions of small island economies by drawing from data of Mauritius. The reason for choosing Mauritius is because of its specificity as well as its performance in the financial services industry in the globe. More details on Mauritius are given in section 3.

This paper gives an overview of the corporate governance in twenty-nine small island economies and then presents the financial services sector of Mauritius. The paper further uses data of six banks and six insurance companies to assess the level of compliance with the code of corporate governance. In this process a compliance index is developed to compute the level of compliance using the National Code on Corporate Governance (NCCG) as benchmark. A general compliance index is computed to calculate the general compliance score for both banks and insurance companies. This paper also reports the difference in the level of compliance between banks and insurance companies.

Through the use of a content analysis of the annual reports of both banks and insurance companies, Banking Act 2004 and Insurance Act 2005, this paper attempts to measure the level of compliance with the National Code of Corporate Governance in the financial services sector in Mauritius.

The objective of the study is to bring in the research arena the corporate governance practices in small island economies with special reference to corporate governance in the financial services sector of Mauritius.

The rest of this paper is organized as follows: Section 2 defines the term small island economies and their role in the global economy. It then presents data on the corporate governance approach and scores obtained by 29 Small Island Economies (SIE in the Financial Sector Assessment Report). Section 3 gives an overview of Mauritius and presents the structure of its Financial Services Sector including its regulatory framework. Section 4 is about Corporate Governance in Mauritius followed by section 5 which is a review of past literature. Section 6 describes the methodology adopted throughout the study. Section 7 presents the analysis of findings followed by a discussion. This paper ends with a concluding note on the implication of the findings and its contribution to knowledge.

2. Small Island Economies and Corporate Governance

Definitional Issue

Despite the availability of various definitions of the term 'Small Island Economies' (SIE), two common denominators that are found in all these definitions are the population size and the level of gross domestic product (FAO, 2002). For the purpose of this paper, these two lenses are utilized in the definition to identify SIEs. Any country with a population of less than 5 million and GDP of less \$US 700, million is therefore assumed to be an SIE.

Although exposed to various constraints to integrate into the global economy, some SIEs are making efforts to keep pace with global dynamism in order to attract foreign direct investments from developed economies. Some are wholly adopting international standards whereas others are not because they have other priorities or because of cultural or colonization influences. This paper does not address these issues because they are research topics that could be addressed separately.

Corporate Governance in SIEs

Some SIEs are inspired by the OECD principles of corporate governance whereas others are not pondering on it because their business environment does not warrant the setting up of a Code on Corporate Governance. A classic example would be the island of Niue where there population is less than 3,000. Another interesting example is Agalega but where this island is managed by a corporation owned by the Republic of Mauritius. Table 1 presents 29 SIEs and the corporate governance principle that they are inspired by or adopt.

Table 1. Small Island Economies and OECD Corporate Governance Principles

Adopting OECD Principles	Not Adopting OECD Principles
Domina	Antigua and Barbuda
Fiji	Bahamas
Kiribati	Barbados
Mauritius	Cape Verde
Papua New Guinea	Comoros
Samoa	Sao Tome and Principe
Solomon Island	Grenada
Tuvalu	Jamaica
Trinidad & Tobago	Seychelles
Tonga	Maldives
	Marshall Islands
	Micronesia
	St Kitts and Nevis
	Nauru
	Palau
	St Lucia
	St Vincent and the Grenadines
	Timo-Leste
	Vanuatu
<i>Total</i>	<i>19</i>

Source: UNCTAD's unofficial list of SIDS

Table 2. Financial Sector Assessment Programme- Scores and Comments on BCP & IAIS

List of SIEs	Year of Assessment	Scores	Comments in FSAP
Antigua and Barbuda	2004	Thin	Need to enhance prudential supervision and formal and effective information
Bahamas	2002	Robust	Made substantial progress
Barbados	2002	Robust	Compliance high with international standards
Cape Verde	n/a	n/a	
Comoros	n/a	n/a	
Dominica	2003	Thin	Need to strengthen legislative framework/set up formal information exchange
Fiji	n/a	n/a	
Grenada	2003	Thin	Legal/supervision needs strengthened/more formal information exchange
Jamaica	n/a	n/a	
Kiribati	n/a	n/a	
Maldives	n/a	n/a	
Marshall Islands	n/a	n/a	
Micronesia	n/a	n/a	
Mauritius	2002	Robust	Substantial progress on codes/standards etc
Nauru	n/a	n/a	
Palau	2002	Modest	Strengthen implementation capacities as regards money laundering/formal information
Papua New Guinea	n/a	n/a	
Samoa	n/a	Underscore	Absence of effective on-site supervision
Sao Tome and Principe	n/a	n/a	
Seychelles	2002	Modest	Moderate compliance with international standards/formal information needed
Solomon Islands	n/a	n/a	
St Kitts and Nevis	2003	Thin	Legal/supervision needs strengthened/more formal information exchange
St Lucia	2003	Thin	Legal/supervision needs strengthened/more formal information exchange
St Vincent and the Grenadines	2003	Thin	Legal/supervision needs strengthened/more formal information exchange
Timor-Leste	n/a	n/a	
Tonga	n/a	n/a	
Trinidad and Tobago	n/a	n/a	
Tuvalu	n/a	n/a	
Vanuatu	2002	Thin	Regulatory framework fall short of international standards

Source: International Monetary Fund: Assessment report, February 25, 2005, BCP= Basel Committee Principles, IAIS= International Association of Insurance Supervisors.

In order to be able to comment on the corporate governance status in the financial services sector of these countries, it is fundamental to glean at their scores in the Financial Sector Assessment Programme conducted by the International Monetary Fund in 2005. Table 2 presents a list of the SIEs, the year of the Assessment Programme and the score of each SIE along with a brief of the comments for each of these SIEs.

SIEs with a 'Thin' score imply that they do not fully comply with Basel Committee Principles. This also demonstrates lack of good governance or practice of poor governance. However, there has been no bank scandal of devastating nature reported by these countries. On the other hand, Mauritius with a good score by the FSAP yet had a substantial banking scandal in 2003.

Another point to note from the FSAP report is that in majority of cases, the common problem in the financial services sector is the formalisation of exchange on information and asymmetry of information. This finding mirrors the sentiment of a few researchers on bank opacity (see, Levine, 2003; Furfine, 2001; Benton, 1999). As in large and developed economies, information asymmetry is a common feature in the SIEs as well. Obviously, the lack of information would have unfavorable impact on the practice of good governance. The next section gives an overview of Mauritius and its financial services sector.

3. An Overview of Mauritius

Geographic, Economic, Social and Political

Mauritius is a small country both in terms of its physical size and population. It is 720 square miles in area with a population of 1.3 million. Almost every one knows each other in the country. This is a situation that makes it difficult to achieve independence (NCCG, 2004, p. 7)

Mauritius has realized rapid economic growth due to its diversification policies from agriculture to information technology and financial services. Today the financial services sector play a critical role in the economy both in the provision of employment and also in foreign currency inflow to the economy.

Mauritius has also a stable and democratic political system supported by strong legal and institutional infrastructures such as Anti-Money Laundering Act 2002, Financial Reporting Act 2004, Banking Act 2004, Insurance Act 2005, Securities Act 2005, the Independent Commission against Corruption (ICAC) and Financial Intelligence Unit

(FIU). Moreover, with its sound economic management system and long-term development strategy, the country is presently setting up new economic pillars such as seafood hub, medical hub and knowledge hub. Albeit the financial services sector remain important in the development of an economy. As such it is being continually upgraded in order to keep pace with the changes in the business network around the globe.

The legal system of the island is among the unique of the world. It is a hybrid of French and English law. The Civil law is based on the Napoleonic Code whereas the company law/tax law/Banking law is based on the British system. As in many other countries, the commercial banks operate under the supervision of Central bank which complies with the Basel Committee Principles. Insurance companies should comply with the provision of the Insurance Act 2005 and are subject to supervision by the Financial Services Commission (FSC). The next section presents the financial services sector of Mauritius.

3.1 The Financial Services Sector in Mauritius (FSSM)

The Financial Services Sector in Mauritius operates under two main wings, namely, the Bank of Mauritius and the Financial Services Commission. The Bank of Mauritius regulates the operation of banking services whereas the FSC regulates non-banking financial institutions (NBFI) including insurance services. Both banks and insurance companies should comply with the rules, regulations and guidelines prescribed by their regulator. In this respect, banks should comply with the Bank of Mauritius guidelines, Banking Act 2004 and insurance companies with the Insurance Act 2005, FSDA Act 2001 and guidelines. On the top of that, they should comply with NCCG (see NCCG report, 2004, p. 17). All of them should comply with the Securities Act 2005 if they are listed on the Stock Exchange. Figure 1 depicts the structure of the FSSM.

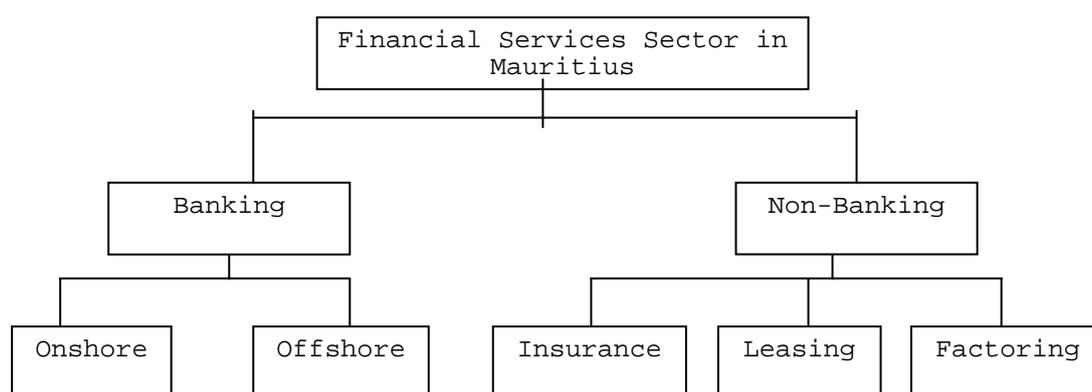


Figure 1. Financial Services Sector in Mauritius

The Banking Sector

Mauritius has a relatively well-developed domestic financial system and a growing offshore sector. There are 11 domestic commercial banks and 12 offshore banks in the country. Among the domestic banks, the two largest foreign banks are the Hongkong Shanghai Bank (HSBC) and Barclays International. These two banks control around 25 % of the market. As regards the local banks, they are dominated by the Mauritius Commercial Bank Ltd and the State Bank of Mauritius Ltd. They have more than two-thirds of the market. These two banks are also listed on the Stock Exchange. The Banking sector is regulated and supervised by the Central Bank.

The Insurance Sector

The Insurance sector plays a key role in the economy. There are 13 major insurance companies in the country and three of them are listed on the Stock Exchange. They have approximately more than 50% of the market. The regulator for insurance companies is the Financial Services Commission (FSC).

3.2 The Regulatory Framework

Banking Sector

The regulatory framework of the banking sector in Mauritius comprises the legal and technical framework. The legal framework is the law in place to regulate the operation and administration of the banks whereas the technical framework comprises guidelines, standards and code(s) to supplement the legal framework in areas which are purely technical that the law cannot afford to accommodate. The international financial reporting standards are an example because the law can only stipulate that accounts and audit should be made according to

international standards, but the law cannot recommend or prescribe standards. The Companies Act can stipulate that there should be effective control in the company, but cannot set up the standards of the control system. Table 3 below illustrates the regulatory framework of the Banking sector in Mauritius.

Insurance Sector

Like the banking sector, the regulatory framework of the Insurance sector operates under a similar model. The Insurance Act 2005 deals with the operations of insurance business whereas the FSC publish guidelines on the good governance of insurance companies. As companies, they should also comply with Companies Act 2001, Financial Reporting Act 2004 and the Securities Act 2005 if they are listed on the Stock Exchange.

4. Corporate Governance in Mauritius

“Corporate Governance is concerned with holding the balance between economic and social goals, and between individual and communal goals with the aim to align as nearly as possible the interests of individuals, corporations and society”

Sir Adrien Cadbury, 1993

Corporate Governance is no longer a matter of regulating the relationship between shareholders and their stewards, but recognizes the relationship between the corporations and stakeholders and the interests of each group. This orientation is called the inclusive approach which underpins corporate responsibility towards its stakeholders (NCCG, 2004, p. 5).

Table 3. Regulatory Framework of Banking Sector

	Legal	Technical
Banking Operations	Banking Act 2004 Anti-Money Laundering Act 2003	Bank of Mauritius Guidelines National Code on Corporate Governance
Corporate Administration	Companies Act 2001 Securities Act 2005 Financial Reporting Act 2004	International Financial Reporting Standards International Standards on Auditing Mauritius Bankers Association

Sources: Designed by author

Corporations have existed since the colonisation period. Under the French colony, Mauritius was administered by a corporation called ‘La Compagnie des Indes’. After independence in 1968, a large number of corporations were registered to trade in the country, especially corporations operating in the freezone sector. During this period, Mauritian companies were subject to the UK Companies Act 1948/1976. In 1984 Mauritius issued its own Companies Act which was revised in 2001. In 1989 the Stock Exchange of Mauritius was set up. In 2001 both the government and private sector have come up with new measures¹⁴ to bring wherever possible the practices of corporations in line with international best practice. This includes the setting up of a National Committee on Corporate Governance and asking the World Bank to complete a report on Standards and Codes (ROSC) on corporate governance in Mauritius. In July 2002 the NCCG decided to prepare the code on corporate governance and the services of Mervyn King was solicited. The Code is now operational in the country. Listed companies, large public and private companies with an annual turnover of Rs 250 million or more as well as banks and non-banking financial institutions shall comply with all the provisions of the Code.

4.1 The Mauritian Code on Corporate Governance

The Mauritian Code on Corporate Governance is written in nine sections. The objective(s) of issuing the Code is to improve governance at corporate level

¹⁴ These measures were: Issuing a new Companies Act, International Accounting Standards, Introducing new listing rules for companies listed on the Stock Exchange of Mauritius, Setting up of a National Committee on Corporate Governance, Asking the World Bank to complete the ROSC on corporate governance etc.

so as to increase further the confidence of stakeholders in the corporations. This exercise has obtained necessary political as well as professional support to become tangible. Without going into the hegemonic analysis of the development of the Code from the inception, it is worth noting that the Code has been inspired by the King’s report of South Africa, the OECD principles of good governance, Cadbury Report, Hampel Committee Report and other relevant studies on corporate governance. The interesting point to note is that the Code was developed taking into account the specific context of Mauritius. That is its size, population, ecosystem, multi-culture, closeness of the population, business organizations, capital markets and listing requirements and ultimately the cost implications in implementing the Code. Under the Financial Reporting Act 2004, all business entities falling under section 1 of the Code shall comply with National Code of Corporate Governance. The NCCG expects these business entities to start compliance as from July 2004, but earlier compliance is encouraged. Table 4 illustrates the contents of the National Code on Corporate Governance.

The Code requires corporations to explain where they have not complied with any part of the Code and also that all relevant entities should include a ‘Corporate Governance Report’ as a new section in their annual report.

To supplement the Code on Corporate Governance, the Bank of Mauritius has issued its guidelines on good governance for the banking sector whereas the Financial Services Commission issued guidelines for NBFIs. The latter was still unofficial at the time of writing. The more so is that the legal framework of the financial services sector was also strengthened by aligning where ever relevant to the Code in order to make it practical.

Table 4. Contents of the National Code on Corporate Governance

1. Compliance and Enforcement
2. Boards and Directors
3. Board Committees
4. Role and Function of Company Secretary
5. Risk Management, Internal Control and Internal Audit
6. Auditing and Accounting
7. Integrated Sustainability Reporting
8. Communication and Disclosure
9. relationship with shareholders.

Source: Report on National Code on Corporate Governance, 2004

For instance, the Code does not state the size of the board, but stipulate that every board should determine its optimal size and composition for effective execution of its responsibilities (section, 2.4, NCCG). Interestingly when the Banking Act was revised in 2004, it made it clear in section 18 (3) that the Board shall not compose of less than seven natural persons. In 2005 the new Insurance Act section 30 (2) has also made provision as regards the minimum size of the Board. Similar approach is adopted in the guidelines of the FSC. The Code is now in the camp of the corporations to comply with and in this study the author has used mainly the annual reports and other related documents to assess the level of compliance to the Code. The next section presents a review of previous literature on corporate governance.

5. Review of Literature

Good governance is not a new concept, but has existed since the early days of civilization. Both eastern and western civilization recognized and preached the principles of good governance. The philosophy of good governance can be related also to theological studies. Hinduism, Christianity, Islamism, Judaism, Buddhism and many other theological schools of thoughts give due importance to good governance. For example, in the epic of Ramayana, there is a good lot of teaching on governance. This is mirrored in the Holy Bible as well as the Holy Quoran. In the modern business world the concept of governance has been put in the context of business management, thus corporate management and control and to end up with today's buzz words 'Corporate Governance'.

The problem of corporate governance started quite a long time ago. It was nearly five centuries ago when the first corporate governance problem cropped up in the Netherlands in 1622 in the Dutch East Indies Company (Jong & Roel, 2004). In 1720 another corporate shock occurred as a result of the implosion of Mississippi Company. John Law, a Scottish

convicted murderer rescued France from the financial ruin wrought by the wars and court of Louis XIV. Law's company, then called Compagnie de l'Occident assumed all French government debt in return for a monopoly on trade with Louisiana. Law's company issued shares and hyped their value, increasing investment demand, which raised their value further, stimulating even more demand. This bubble imploded in 1720, ruining the finances not only of the French kingdom but of much of her aristocracy and merchant elite. Joint stock companies were banned, and wise businessmen shunned the financial markets and passed this wisdom to their children (Murphy, 2004). A similar case appeared in Britain in 1722 in the case of South Sea Company. The Bubble Act 1722 banned joint stock companies in Britain unless they obtained a parliamentary charter. That is to establish each new joint stock company required an Act of Parliament.

Nowadays, the debate on corporate governance would be thin without referring to Sir Adrian Cadbury (1999) who defines corporate governance as a system which is concerned with holding a balance between economic and social goals, and between individual and communal goals. This definition harmonises with that of Demb and Neubauer (1992). However, other writers do not welcome Demb and Nebauer (see Stenberg, 1996). Tricker (1994) adopts a different approach in his definition of corporate governance by focusing on the board room. Like this many authors come with a definition, but the pertinence in all these is the recognition of corporate interest. Corporate interest can be achieved unless corporate governance is made on a holistic approach (that is, taking into account the interests of all stakeholders) rather than on an apartheid approach as in the past where focus was only on shareholders and their stewards.

Linking definition with theory, it is sensible to argue that the standard definition of corporate governance stems from the agency theory. For agency theory and agency problem, see Coase, (1937); Jensen & Meckling, (1976). Shleifer & Vishny(1996) extend the definition to the ability of small investors to exert

corporate control and the further problem that they would encounter to monitor the activities of banks given the degree of opacity (see also Morgan, 2002).

Financial crises have occurred as a result of poor governance. This is the conclusion reached by Litan et al. after analyzing the financial crisis in Asia in 1977 and subsequent crises in other countries such as Russia and Turkey. It could be argued that though banking crises are due to some factors beyond the control of bank management, bank failures are attributed to poor risk management; a failure of internal governance. The collapse of the BCCI, the Barings case and the Allied Irish Bank, to mention a few, are examples of failures due to poor governance.

Another feature that affects the governance of banks is their opaqueness. Opacity increases information asymmetry and thus making agency problem more dangerous. Benton (1999) empirical study on opacity of banks would support the argument that the increased information asymmetries make it difficult for equity and debt holders to monitor the banks' stewards. Kaufmann (2003) states that poor governance of financial institutions increases the liabilities of the financial system. They have distorting effect on public institution, deter foreign direct investment and can lead to future financial crisis. Weaknesses in the corporate governance of financial institutions reduce their ability to properly evaluate and manage their risks which can entail in poor quality lending and increase risk taking. Therefore good corporate governance is an essence for the success of financial institutions.

All previous studies on corporate governance in the financial sector or even in other sectors were conducted on large economies such as the US, France, United Kingdom, Japan, India, just to mention a few. The SIEs have remained unaddressed on this topic. The author is arguing that corporate governance is a global issue and therefore important in the SIEs. Moreover, SIEs are making moves to join the globalization process and as such are trying to align their standards to international best practice, for example, accounting and auditing standards, banking practices and of course corporate governance. Many SIEs have inspired by the OECD corporate governance model and some have already produced their Code on Corporate Governance. Mauritius is one of them. The author is motivated to assess how far compliance is made to the NCCG in the country with particular reference to the financial services sector. Findings from this study shall provide data for comparative research in the future. The next section describes the methodology adopted in the conduct of this study.

6. Methodology

Data Collection

This study uses content analysis to assess compliance with Code on Corporate Governance in Mauritius. For this purpose secondary data is collected from the annual reports of both banks and insurance companies. Annual reports were collected in person from the companies or wherever possible they were downloaded from the company website. It was not possible to obtain the annual reports of 2005/6 because they are not yet published. For this reason, the annual reports of 2004/5 are used in this study. The Code on Corporate Governance of Mauritius, the Banking Act 2004 and the Insurance Act 2005 has also been used for reference purpose. Relevant section(s) of these Acts have been analysed and compared with the requirements of the Code to interpret the findings

Sampling

The financial services sector in Mauritius comprise of banks, insurance companies, pensions funds, leasing companies and factoring companies. This study is focusing only on banks and insurance businesses and therefore the sample excludes the other types of non-banking financial services companies. There are eleven commercial banks and twelve offshore banks on the island and thirteen major insurance companies. For the purpose of this study six commercial banks and six insurance companies are selected (see appendix A for a list of the companies). The banks include the two major banks which have more than two thirds of the market share and similar approach is adopted for the insurance companies. The insurance companies in the sample comprise of three listed companies which have more than 60% of the market share. The sample size is therefore representative of the population and the findings would therefore reflect corporate governance practices in the banking and insurance sector in Mauritius.

Content Analysis

Content analysis is used to assess the level of compliance with the Code on Corporate Governance in Mauritius. Content analysis is a way to categorise various items of a document into a number of categories. It is an appropriate method to use where a large amount of qualitative data has to be analysed. The use of content analysis has been supported by a number of authors for similar type of research (see Holsti, 1969; Boyatis, 1998; Weber, 1988; Krippendorff, 1980).

An essential issue in content analysis is reliability. Milne & Alder (1998) identified different types of reliability and this occurs in the process of coding. The main problem that arises in coding is when more than one coder is encoding the data. In this study there are only six issues of corporate governance and 12 companies that are involved. The six issues addressed in this study are as follows:

- (i) Board's composition
- (ii) Non-Executive Directors (NEDS)
- (iii) Audit Committee
- (iv) Disclosure of Policies and practices
- (v) Disclosure of Shareholders' Interests
- (vi) Shareholders' Rights

Not all of these issues are codable which therefore entices the author to conduct a sentence by sentence analysis to determine compliance (Shrives & Linsley, 2003). This is in the case of the disclosure of directors' interest and directors' right. The companies are coded by number (see appendix A).

Sections Analysis

The first step in this process is selecting the section(s) of the annual reports to be analysed and compared with the NCCG. Given that the annual reports of a few of these companies were not properly segmented, the information related to corporate governance is scattered in different parts of the report where as in others it was easy to identify the relevant page(s) or section(s). Table 5 is an example of how the contents of the annual reports of insurance companies on corporate governance analysed to assess compliance. Similar approach was used for banks.

Measuring Compliance

Compliance to the NCCG is measured using provisions in the Code as bases. Where the Code is silent on an issue, provision(s) of the law is then used as a basis. For example the Code stipulates that a company should have a balanced board but is silent as to the quantum of members. In that case the provision of Section 18 (3) of the Banking is used. As a result this facilitates the measuring process. This is followed in the case of each bank and insurance company under this study. A company is scored as full compliant if it meets the minimum requirement of the Code or the law. For example, the Banking Act 2004 stipulates that a bank shall have a board of not less than seven natural persons. In case the board of directors of a bank has more than seven members, it is scored 100%. However, if there is less than seven members, then the score is reduced on a prorata basis.

Comparing Compliance

Compliance is compared by comparing the average scores of the banking sector with the insurance sector. The same is applied to the insurance companies. The purpose of this statistic is to determine whether there is a significant difference in the compliance level to the NCCG between banks and insurance companies in Mauritius.

The methodology used in this study is simple and also very adaptable in other similar studies.

7. Findings and interpretations

This section presents the findings of this study followed by an interpretation and discussion. The findings of the banking sector is presented and analysed as the first part followed by the findings and analysis of the insurance sector. This section ends with a note on the difference in the findings of these two sectors in Mauritius.

Banking Sector

Table 6 presents the findings for the banking sector on compliance with board's composition, board's committee and disclosure of policies and practices.

Table 6 reveals that in the Banking Sector in Mauritius there is 100% compliance with the Banking Act 2004 as regards the Board's composition. As regards requirements for the number of Non-Executive Directors (NEDS) all the banks in the sample are also fully compliant both with the Act and NCCG. If we measure compliance with the Hampel committee requirement, again the score remains on the outstanding number. This result explains compliance with international best practice.

The only problem in the context of Mauritius is identifying an independent NED who is wholly independent as per its definition. This is due to size of the island and the fact that the community is so closed that each one knows the other. This presence of communal proximity could make it difficult to obtain an independent director. The alternative available is to acquire the services of independent NEDS from foreign countries but this option is constrained by the cost implication.

In the case of audit committee 5 out of the 6 banks satisfy Section 40 of the Banking Act, except one bank which as per its annual report 2004 did not have an audit committee. This would be classified as a serious weakness in the practice of good governance. However, this company has to put up with this requirement in the financial year ended 2005/2006. On overall the score is 83%.

Table 5. Description of Contents Analysis of Annual reports of Insurance Companies

Insurance company	Contents on Corporate Governance in Annual Reports	Page Number in Annual Reports
MU1	Corporate Information:	
	-Board of Directors	5
	-Chairman's review	6,7
	-Statutory Disclosures	10-12
SW2	Chairperson's Statement and Directors' Report:	
	-Corporate Governance	14-19
AIA3	Corporate Governance:	
	-Ultimate shareholding structure	9 para 1
	-Shareholding	9
	-Share price information	9
	-Board of Directors	9
	-Board and Committee meetings and attendance	
	-Board Committees	9-10 para 2
	-Corporate Governance Committees	11
	-Audit Committee	11 para 1
	-Risk Committee	11
		11
SI3	Corporate information:	
	-Board of Directors	2
	-Board Committees	2
	-Management	3
	- Directors of Subsidiaries	3
	-Director's profiles	6-10
ME5	Chairman's report:	
	-Corporate Governance	11 para 3
BA 6	Corporate Governance Statement:	
	Board of Directors	9
	Board Committees	9

Sources: Designed by author

Table 6. Compliance Level with NCCG in Banking Sector

Corporate Governance issues	Bases	Number of banks						Average	Standard Deviations
		1	2	3	4	5	6		
Board Composition	S 18 of Banking Act 2004 and Bank guidelines	15	11	17	22	12	11	14	9.79
Non-executive Directors	Bank guidelines	13	10	8	13	5	6	9	7.28
Compliance Score %		100	100	100	100	100	100	100	0
Audit Committee	Section 40 Banking Act 2004	4	5	6	8	6	0	5	6.63
Compliance Score %		100	100	100	100	100	0	83	91.29
Disclosure of policies and practices Expected	Appendix B	12	12	12	12	12	12	12	n/a
Compliance Score %		95	95	95	95	92	75	91	17.92

Sources: Annual report 2004/5

Notes: S 18 of Banking Act stipulates that the minimum number of members in the BOD should be seven of which 40% should be NEDS

Table 7. Compliance Level with NCCG in Insurance Sector

Corporate Governance issues	Bases	Number of banks						Average	Standard Deviations
		1	2	3	4	5	6		
Board Composition	S 30 of Insurance Act 2005 and FSC guidelines	8	14	8	8	10	5	9	6.6
Non-executive Directors		8	10	3	3	8	3	6	7.2
Compliance Score % Full Board		100	100	100	100	100	71	95	24.51
Audit Committee	Section 46 Insurance Act 2005	3	Exist(no mention on size)	2	4	Exist(no mention on size)	Exist(no mention on size)	n/a	
Compliance Score %		100	n/a	100	100	n/a	n/a		
Disclosure of policies and practices	Appendix B	12	12	12	12	12	12	12	0
Compliance Score%		67	83	67	67	75	75	72	14.62

Sources: Annual report 2004/5

Notes: S 30 of Insurance Act stipulates that the minimum number of members in the BOD should be seven of which 30% should be NEDS

Disclosure of policies and practices has been determined from a list of 12 items as shown in appendix B. For this purpose it is expected that a company should score 12 points to achieve 100%. It can be generalized that there is no 100% compliance with the disclosure of policies and practices in this sector. Not all banks disclose their business goals and strategies. It would be more informative if the annual report includes also an assessment of business climate and risk. Disclosure of interest and shareholders' rights are also two important issues in corporate governance. This is provided in section 48 of the Banking Act 2004. Directors and even management team disclose in writing the extent of any transaction with their banks and the nature of their interest. This view is supported in the Corporate Governance report, 2003. As far as the shareholders rights are concerned, all banks comply with the provision of the Companies Act 2001.

Insurance Sector

Table 7 reports the result obtained from the content analysis of the annual report of the insurance companies. On average the insurance sector scores 95% compliance rate as regards Board's composition and NEDS. In the case of insurance company number 6, it does not have the minimum of seven members on its board, although its NEDS comply with the 30% rule of the section 30 of the Insurance Act 2005.

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However, 5 out of the six companies score 100%.

All these companies state in the annual report 2004/2005 that they have an audit committee, but only 3 out of 6 stated the size and composition of the committee. Disclosure of policies and practices are less than 75% compliant on average. Many of these companies do not disclose the business goals and strategy. Very few report on the management's assessment of business climate and risk and as regards risk management systems this area could be more elaborative.

These companies comply with the disclosure of interests and shareholders' rights. There is no mention on the strategic committee in these companies, but emphasis is made on the investment committee.

Comparative Assessment on Compliance: Banking and Insurance

Table 8 reveals that the banking sector is more compliant to NCCG than the insurance sector. This is based on the 2004/2005 annual reports. It also reports that there is a significant difference between the level of compliant in the banking sector and the insurance as regards disclosure of policies and procedures. Overall compliance to the NCCG in the financial services sector is beyond 75%.

Table 8. Comparing Average Compliance Score

Corporate Governance Issues	A Banking Sector	B Insurance Sector	A-B Difference	Significance
Board's Composition	100	95	+5	No
Audit Committee	83	n/a	n/a	n/a
Disclosure of Policies and Practices	91	72	+19	Significant

Source: Prepared by author

8. Conclusions

This paper has addressed the issue of corporate governance principles and practices in the financial services sector in small island economies. Corporate governance is fundamental for corporate success but the development of and compliance with a proper code for corporate governance is the prerequisite. Corporate governance is not only an issue of large countries or developed economies. On the contrary it is a major issue for the success of small island economies. However, very few researches were conducted in that perspective. Therefore this paper brings to the body of literature the status of corporate governance in SIEs.

This paper concludes that in many SIEs corporate governance principles is inspired from the OECD five principles and also copied from Cadbury and Hampel. It reveals that 10 out of 29 SIEs use the OECD principles as a benchmark to develop corporate governance. Using the FSAP report, this paper has also reported the strength of corporate governance in some the SIEs by re-organising and simplifying the data. This becomes available to support future research on corporate governance in SIEs.

Moreover this paper has presented the Corporate Governance Code of Mauritius and the related rules to it. It has revealed the role of the law in fleshing the Code where necessary and also presents how the Code aligns with Cadbury, Hampel and OECD rules.

This study also provides empirical evidence as to the compliance with Corporate Governance Code in the financial services sector of Mauritius. It reports compliance by corporate governance issues in both the banking and insurance sector. It measures the level of compliance in both insurance companies and banks and also reports on comparative compliance. The author has used a very simplistic statistical method to measure compliance. These findings add to the body of literature by reporting which of these two sub-sectors in the financial services sector is more compliant with the NCCG in Mauritius. This result can be used later to compare with other similar research on SIEs.

The limitation of this study is that the results and findings cannot be generalized but is specific in nature. It could be confirmed, if not amended after replicating a similar study on other SIEs.

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Appendix B: List of Disclosure of policies and practices

1. Risk management systems
2. Business goal and strategies
3. Cross-shareholdings and cross debt guarantees
4. Management assessment of business climate and risks
5. Names of directors
6. Directors compensation rates
7. Principal external jobs held by the directors
8. Corporate governance practices of the company
9. Material claims and court cases
10. Related party transactions
11. Existing and potential conflicts of interests
12. Shareholdings of directors or their family members in the company or its related companies.

Appendix A: List of Companies

Insurance Companies:

Mauritius Union Assurance (MU1)
Swan Insurance (SW2)
Albatross Insurance (ALA3)
SICOM (SI4)
Mauritius Eagle (ME5)
British American Investment (BA6)

Banks:

Mauritius Commercial Ltd (MC1)
State Bank Mauritius Ltd (SB2)
Barclays Bank Ltd (BB3)
HSBC (HS4)
Post -Office Co-operative Bank (PC5)