Corporate Governance and Financial Distress of Ghanaian Universal Banks

“A Critical Evaluation”

1.0 **Introduction and Background to the Study**

Corporate governance is well thought-out to have major implications for the growth prediction of banking system as well as the economy in general. Corporate governance represents the bridge and solution that govern the relationship between shareholders and the board of directors, and other stakeholders. There is always an uncertainty factor represented by the shareholders of how the board of directors are directing the corporation they are interested in, and whether they are managing it in their favour or not. Also, because the shareholders are not always aware of the management techniques that are used by those directors, there must be a solution that decreases the gap between the interested parties and the corporation represented by the board of directors. The Organization of Economic Corporation and Development (OECD, 2004;2010) defines corporate governance as involving “a set of relationships between a company’s management, its board, its shareholders, and other stakeholders. Corporate governance also provides the structure through which the objectives of the company are set, and the means of attaining those objectives and monitoring performance are determined. Good corporate governance should provide proper incentives for the board and management to pursue objectives that are in the interests of the company and shareholders and should facilitate effective monitoring, thereby encouraging firms to use resources more efficiently”.

Basel Committee on Banking Supervision (BCBS;2006; 2010; 2015) gives the definition of corporate governance in the banking industry perspective, which states that bank corporate governance involves the manner the business and affairs of banks are governed by the board of directors and senior management which, inter alia, affect how they: (i) set corporate objectives, (ii) operate the bank’s business on a day to day (iii) meet obligation of accountability to their shareholders and take into account the interests of other recognized stakeholders (including regulators and supervisors, depositors and government), (iv) aligning corporate activities and behavior with the expectation that banks will operate in a safe and sound manner and in compliance with applicable laws and regulations and (v) protect the interest of depositors (BCBS, 2006; 2010). Effective corporate governance practices are essential to achieving and maintaining public trust and confidence in the banking system, which are critical to the proper functioning of the banking sector and economy as a whole. Poor corporate governance can contribute to both bank distresses and failures, which can in turn pose significant public costs and consequences due to their potential impact on any applicable deposit insurance system and the possibility of broader macroeconomic implications, such as contagion risk and impact on payment system. The weaknesses in corporate governance within companies and banks were cited as the cause of a number of corporate bankruptcies and bank distresses in the 2007-2008 global financial crisis. The 2009 Report by the OCED stressed that the failures and weaknesses in corporate governance of certain financial institutions were largely regarded as the cause of the global financial crisis. These failures have led to conflicts of interest between shareholders and managers of banks and between shareholders and boards.

Banks are key players in any country’s financial sector, because they occupy a delicate position in the economic equation of any country such that their (good or bad) performance invariably affects the economy of the country. The existence of an effective banking sector is necessary for every economy because it creates the necessary environment and development through its role in intermediating funds from surplus sector to deficit sector of the economic units. Banking sectors are financial intermediaries whose activities are for of savings and lending, thus standing in between the ultimate lender and borrower and matching the investment requirement of the lender. Banks play important roles in the economic development of Ghana. In the recent years, there has been great concern on the management of banks' assets and liabilities because of the 2007-2009 global financial crises. The experience of many countries indicates that regulation and supervision are essential for stable and healthy financial system and that the need becomes greater as the number and variety of financial institutions increase. The banking sector has been singled out for the special protection because of the vital role banks' play in preventing bank distresses and failures, and ensuring that the banks carry out their activities in accordance with wider economic and social objectives of the country (Chude & Chude, 2014). Bank supervision entails not only enforcement of rules and regulations but also judgments concerning the soundness of the bank assets, its capital adequacy and management

(Volcker, 1992). Effective and efficient supervision leads to healthy banking industry. To maintain confidence and protect the banking system, regulators and supervisors worldwide ensure that banks play the game according to rules and regulations.

As an important component of the Ghanaian financial system, they channel scare resources from surplus economic units to deficit units. In Ghana, the formal banking took roots in the colonial Gold Coast towards the end of the 19th century with the establishment of the British Bank of West Africa in 1897 (known as Standard Chartered Bank) and Barclays (Dominion, Colonial and Overseas) in 1917 to the present day of expansion in the banking business. Distress in the history of the Ghanaian banking industry is not an entirely new phenomenon and this has had far reaching consequences on the economy. According to Brownbridge and Gockel (1995), the Ghanaian banking system suffered a severe shallowness together with widespread bank distress as the consequence of the pre-reform policies of financial repression, government control of banks and prolonged economic crisis. The consequences of distress include the loss of confidence by depositors in the industry with corresponding retardation in the tempo of capital formation for investment. Banking distress was not accident and did not occur in a day. It was rather organic as well as systemic. It could therefore be predicted ahead of time based on the identification of the early warning signals; thereby providing a sustainable framework for board of directors, senior management teams and regulatory authorities to take decisive actions to nip the problem in the bud. The early signals of the bank distress included increasing portfolio of non- performing assets, high operating expenses, consistent sourcing of funds from the interbank market, inability to meet statutory requirements and instability in corporate management (Donli, 2003; Kostyuk, 2011).Bank distress leads to loss of confidence of the banking public, which precipitates bank run and its negative effects on the economy.

Most of the business distresses in recent past are attributed to the failure in corporate governance practices. For instance, the distress of banks in Ghana in the early 1980s and onwards was as a result of inadequate corporate governance practices such as excessive concentration, insider-related credit abuses; corruption, politically related loans, poor risk appreciation and internal control system failure. Before the financial sector reform in 1988, Ghanaian banks were financially distressed to the tune of a total of C62 billion or US$ 170 million or 4.4% of GDP) of non-performing loans (Bawumia, 2010). The weaknesses manifested in ineffective boards, incompetent senior management, high operating costs, political interferences, prolonged economic crises, weak regulatory and supervisory framework, corruption, political interference and high state ownership of banks. A systemic failure of corporate governance means failure of the whole set of regulatory, market, stakeholder and internal governance mechanism which had contributed to the on- going Ghanaian banking distresses. A regulatory failure in governing banking institutions before the distress was manifested in substantial deregulation and lack of regulation in the banking industry.

Corporate governance refers to the organizational framework for decision making and action taking within a corporate entity. In this regard, it can also be defined as the structure of relationships within an entity for making decisions and implementation. Simply put, it refers to how an organization is run, that is, how the resources of an organization are employed in pursuance of the set of missions and goals of the organization. Hussey (1999) as cited in Ivior (2008) defines corporate governance more formally as “the manner in which organizations, particularly limited companies, are managed and the nature of accountability of the managers to the owners”. In other words, corporate governance is not just a set of rules but also a structure of relationships geared towards establishing good corporate practice and culture. The ultimate Business Dictionary (2003) as cited in

Sani (2010) defines corporate governance functionally as the managerial or directional control of an incorporated organization, which, when well-practiced can reduce the risk of fraud, improves company performance and leadership and demonstrates social responsibility. Essentially, corporate governance is focused on controlling the activities of those in whose custody the resources of an organization are entrusted with a view to protecting the interest of the resource owners.

Wise and MahboobAli (2009) opined that “corporate governance indicates the policies and procedures applied by firms to attain certain sets of objectives, corporate missions and visions with regard to stockholders, employees, customers, suppliers and different regulatory agencies and the community at large”. Effective corporate governance practices are essential to achieving and maintaining public trust and confidence in the banking system, which are critical to the functioning of the banking sector and economy as a whole. Poor corporate governance may contribute to bank failures, which can pose significant public costs and consequences due to inability of a bank to manage its assets and liabilities, including deposits, loss of confidence and in turn trigger a bank run or liquidity crisis. Roche (2005) as cited in Cadbury (1992) posits that corporate governance is the way and manner in which the affairs of companies are conducted by those charged with that duty. In Ghana, as in other jurisdictions, the governance of a limited liability company is the responsibility of its board of directors. By appointing the board of directors, shareholders have an instrument to control managers and ensure that the firm is run in their interest. The two most important roles of a board of directors are monitoring and advising. As a monitor the board supervises the managers so as to ensure that their behavior is in line with the interest of the shareholders, while as an advisor the board provides opinions and directions to managers for key strategic business decisions. Corporate governance is also characterized by transparency, accountability, probity and the protection of stakeholders' rights. Corporate governance refers to the manner in which the power of a corporation is exercised in the management of its total portfolio of economic and social sources with the aim of increasing shareholders' value and safeguarding the interest of other stakeholders in the context of its corporate mission.

The above definitions are summarized into one by the Report of the SEC Committee on Corporate Governance of Public Companies in Ghana (2003) as cited in BCBS (2010) which sees corporate governance as "the system by which companies in Ghana are directed, and managers are held accountable for the performance of the organization." This further emphasizes the fact that the concept of corporate governance is principally on the structure of relationship within an organization which is directed at best practice in the overall interest of the organization and its owners/stakeholders with the sole aim of curbing distress in the Ghanaian banking system.

In ordinary parlance, distress connotes being in danger or difficulty and in need of help. A bank is said to be distressed when it cannot meet its commitments as they fall due. Such a bank either experiences illiquidity or insolvency. A bank is illiquid when it can no longer meet its liabilities as when due; whereas a bank becomes insolvent when the value of its realizable assets is less than the total value of its liabilities. In such a case, owners' capital becomes negative as in the recent case of UT Bank and Capital Bank (Daily Graphic and Business Financial Times, 15/08/2017). An illiquid bank may not be insolvent immediately. However, both illiquidity and insolvency are sources of worry for owners and the regulators (Jimo, 1992)

The terms distress connotes "unhealthy situation" or a state of inability or weakness, which prevents the achievement of set goals and aspiration (Ologun, 1994). Benston et al, (1986) as cited in Sani (2010) defines distress as a situation of complete loss of shareholder funds. To evolve a working definition of distress, it is desirable to synthesize those factors that will be unhealthy as well as state some broad set obligation and aspiration of a typical financial institution. Banking literature describes distress as a situation in which a sizeable proportion of banking institutions have liabilities exceeding the market value of their assets which may lead to “runs and other portfolio shift” and eventual collapse of the banking system. Put differently, distress in the banking system occurs when a fairly reasonable proportion of the banking system are unable to meet their obligations to the customers, depositors, owners and the economy as a result of high non-performing loans as the consequences of ineffective board practices, mismanagement, excessive risk taking, poor risk management practices and ineffective and inefficient regulatory and supervisory framework.

Bank distress is a condition where a bank cannot meet nor has difficulty in paying off to its depositors and customers. It means that there is a tight cash situation and if prolonged may lead to failure and possibly to bankruptcy and even liquidation. Foster (1986) notes that filing for bankruptcy has been the most commonly used for corporate distress. A bank is distressed when it cannot meet its commitments as they fall due. According to Alashi (2002), a bank is said to be in severe distress, when a bank shows most or of all the followings: (i) gross undercapitalization in relation to the business orientation and strategy, (ii) consistent high level of non-performing loans to the total loans (iii) liquidity as reflected in a bank's ability to meet customers' cash withdrawals or persistent overdrawn position with central bank (iv) low earnings resulting in huge operational losses and (v) weak management as reflected by poor asset quality, insider abuse, inadequate internal controls, late submission of statutory returns and high level of staff turnover, among others. After reviewing several studies on worldwide episodes of banking distress and crisis, Dermirguc-Kunt and Detragiache (1997) concluded that for an episode of banking distress to be classified as fully-fledged crisis and of a systemic nature, at least one of the following four conditions had to hold: (i) the ratio of non-performing assets to the total assets in the banking system exceed 10%; (ii) the cost of rescue operation should at least be 2% of the GDP; (iii) banking sector problems resulted in large scale nationalization of banks ; and (iv) extensive bank run took place or emergency measures such as deposit freezes, prolonged bank holidays or generalized deposit guarantees or massive bail outs were implemented by the governments in response to the banking distress and crisis. However, the Ghanaian banking system has recorded a non-performing assets ratio of 16.2% in

2008; 17.6% in 2009; 14.1% in 2010; 13.2% in 2011; 14.7% in 2012; 15.7% in 2013; 14.6% in 2014; 16,6% in 2015; 17.1% in 2016; averaging 15.53% (IMF country assessment reports 2008-2016). This IMF country assessment reports confirmed Dermirguc-Kunt and Detragiache (1997) that the Ghanaian banking system is in fully fledged crisis.

According to Outecheva (2007) bank distress can be subdivided into four levels-: deterioration of performance, insolvency, default and failure. Whereas, deterioration and failure affect the profitability of the bank, insolvency and default are rooted in its liquidity. In general, bank distress is characterized by a sharp decline in the performance and the value of loan portfolio.A financial institution is described as unhealthy, if it is unable to meet its obligation to depositors, customers, owners and the economy occasioned by severe financial, operational and managerial weaknesses (Ologun, 1994). Elebuta (1999) cited that distress occurs when a fairly reasonable proportion of banks in the banking sector are unable to meet their obligation to customers, owners and the economy, as a result of weakness in the financial, operational and managerial capabilities which renders them either illiquid or insolvent. Brownbridge (1998) stated that banks can provide benefits to the domestic economies but they also present risk with many banks having suffered financial distress and bank failure as a result of high non-performing assets. The severity of bad debt problems was attributable to moral hazard on bank owners, and the adverse selection of bank owners, with many banks pursuing imprudent lending strategies in some case involving excessive risk taking.

The Ghanaian banking sector witnessed dramatic growth post –financial sector reform period. Banks grew both in size and numbers and even diversified across the shores of the country with branches and subsidiaries. The liberalization of the financial sector under FINSAP and FINSSIP resulted in an increase in the number of banks and non-banks in the financial sector with increased foreign and private domestic sectors participation. In 1988, the Ghanaian banking system comprised 10 banks with 405 branches (Bawumia, 2010). In 2016, there were 33 universal banks with more than 1000 branches. However, neither the industry nor the regulators were sufficiently prepared to sustain and monitor the sector's explosive growth. Prevailing sentiments and economic orthodoxy all encouraged this rapid growth, creating a blind spot to risks building up in the system. Prior to the crisis, the sentiment in the industry was that the banking sector was sound and growth should be encouraged. The International Monetary Fund (IMF, 2013;2014;2015) endorsed the strength of the banking system to support this growth but raised questions about distress among some banks. Among the many inter dependent factors that led to creation of an extremely fragile financial system is failure in corporate governance at banks. The rapid growth in the financial sector occurred during the time when corporate governance standards at banks were extremely weak. In fact, failure in corporate governance is indeed a principal factor contributing to the distresses over the past decade. Corporate governance malpractices within banks, unchecked at post financial sector reform period, became a way of life in large parts of the sector, enriching a few at the expense of many depositors and investors. Corporate governance in many banks failed particularly the state -owned banks and private domestic banks, because boards ignored these practices for reasons include being misled by executive management, participating themselves in obtaining unsecured loans, insider dealings, connected or related lending at the expense of the depositors and not having the qualifications to enforce good corporate governance on bank management. In addition, the audit processes at almost of these banks appeared not to have taken account the rapid deterioration of risk assets of banks until the IMF (2015) requested for full detailed assessment of asset quality review. As banks grew in numbers, size and complexity, bank boards' often did not fulfill their function and were lulled into sense of well -being by apparent year over year growth in assets and profits. In hindsight, boards and executive management in some of the banks were not equipped to run their institutions. Some board chairpersons/ CEOs often had an overbearing influence on the boards, and some boards lacked independence; some directors often failed to make meaningful contributions to safeguard of the growth and development of the banks and also had weak ethical standards and low moral values; and board committees were ineffective or dormant (Sanusi, 2010)

The entry of new banks had brought competition and diversification but failed to overcome the fundamental weaknesses in corporate governance in many of these banks. The problems in the Ghanaian banking industry in the post sector reform period have been that of risk management arising from accumulation of huge non-performing accounts. This is as a result of non-application of the five ‘C’ of lending – Character, Capacity, Capital, Condition and Collateral. The banking industry experienced misuse of shareholders’ funds, governance malpractices, unchecked at expansion. For instance, a large part of the sector enriched themselves at the expense of many depositors and investors. Corporate governance in many banks distressed because boards ignored governance practices to the extent that some non-executive directors and board chairpersons obtained for themselves un-secured loans at the expense of the depositors and they did not have the boldness to enforce good governance. This precipitated massive loan defaults across the banks.

In addition, the internal audit systems and risk management processes at all banks appeared not to have taken fully into account the rapid deterioration of the economy and hence the need for aggressive provisioning against risk and assets. As banks grew in size and complexity, bank boards' often did not fulfill their function and were lulled into a sense of well-being by the apparent year-over-year growth in assets and profits. In hindsight, boards and executive management in some major banks were not equipped to run their institutions. The bank chairman/CEO often had an overbearing influence on the board, and some boards lacked independence; assets and liabilities committees and risk management committees became rubber stamps; directors often fail to make meaningful contributions to safe guard the growth and development of the bank and had weak ethical standards: the board committees were also often ineffective or dormant, Chief executive officers (CEO's) tunneling money to themselves and other activities at variance with corporate governance (Bank of Ghana, 2006). A review of the prevailing situation in the Ghanaian banking industry shows that most banks are yet to embrace practices that will ensure good corporate governance in their institutions. Good governance practices result in higher firm’s market value, lower cost of funds and higher profitability (Black, Jang & Kim, 2006 & Claessens,2006). According to Chiejina (2009), “the executive of banks had abandoned the key elements of good corporate principles of honesty, trust, and integrity, openness, performance orientation, responsibility and accountability, mutual respect and commitment to the organization for selfish reasons”. The core banking practices have been traded off and the most beneficial are the CEOs and their loyalist. Corporate governance aims to create an atmosphere whereby Ghanaian banks will comply with laid down regulations and rules without compromise. This will in the end lead to transparency and disclosure in the banking institutions, proper risk management systems, adoption of professional practices in carrying out banking business, strong internal control system, restoration of public confidence, rapid economic growth and development, and in all prevent bank distress which might lead to failure. According to Asiamah (2016), the financial system is predominately bank based with assets to GDP ratio of about 40.32% as at December 2015. This gives an indication of the critical role of the Ghanaian banking system. He further opined that sound corporate governance practice is critical to improving economic efficiency and growth of the banking system as it serves as deterrent to mismanagement and also infuse discipline in the decision -making process at the board level.

1.1 REVIEW OF RELATED LITERATURE

The financial distress and corporate governance among Ghanaian banks

Theories of Bank Distress

There are two main theories that will be discussed in this article: Microeconomic and Macroeconomic theories.

Micro economic theory

At the microeconomic theory level, mismanagement plays a major role in bank distress or insolvency (Soyibo and Odusola, 2002). This approach sees mismanagement as an evil that destabilizes a bank or a whole banking system, especially where there is ineffective and inefficient banking regulation (Popel, 1998; De Juan, 1987). Mismanagement is classified into four categories: technical mismanagement, cosmetic mismanagement, desperate mismanagement and fraudulent activities. Other micro causes of banks' unsoundness relate to moral hazards in domestic finance and lack of transparency or market indiscipline in corporate governance. Weak regulation and supervision act as interface between macro and micro causes of bank distress and any financial system with characteristics is bound to experience deep crises, whenever there are shocks with the financial system (Soyibo & Odusola, 2002)

Macroeconomic theory

This perspective sees microeconomic causes as secondary and attributes bank distresses mainly to macroeconomic instability such as high inflation, high interest rates, currency depreciation and huge budget deficits. The macro economic developments under bank distresses can be categorized into four models. The first is the monetary model of financial crises, as pioneered by Friedman and Schwartz (1963) and further extended by Brunner & Meltzer (1988), which emphasizes the central role of the growth of money stock and its variability in making bank unsound. This framework posits that banking and debt crises are endogenous events, conditioned by economic policy and the banking structure, and not by independent or exogenous shocks (Soyobo & Odusola, 2002). The business cycle theory is the second approach and postulates that the financial environment responds endogenously to the state of the business cycle or to some displacement such as financial sector deregulation, which opens up opportunities for profit making. An example of this is the deregulation of the Ghanaian financial sector under FINSSAP in 1988 and FINSSIP in 2003 respectively, which increased the number of commercial banks from 10 in 1988 to 33 in 2016. The rural and community banks increased from 98 to 138 in 2016, and microfinance companies from 0 to 400 in 2016. In addition to these was the emergence of finance houses, savings and loan companies and other financial intermediaries in the post sector reform period. This approach argues that as a result of expanded activities in the Ghanaian financial sector, credit facilities have increased considerably which had also impacted negatively on the non -performing loans and distresses. These developments have also weakened the strength of the financial system as a result of inefficient and ineffective supervision and regulation and hence made the system more vulnerable to shocks (Udusola,2001). The intense competition also lowered the bar on effective loans evaluations and control in the attempt of banks' and non-banking financial institutions to expand their share of credit portfolios. Furthermore, there were also problems with the state- owned enterprises (SOEs) debts which capacitated the governments from fulfilling its loan repayment obligations to the banks (IMF, 2011, 11/131)

The third approach is based on the market failure theory and propagated by Stiglitz and Weiss (1981); Bernanke (1986) and Mishkin (1987) who used the framework of information asymmetry in the credit market to explain financial distresses and crises. They argued that conflicts between lenders and borrowers arising from moral hazards imply that lenders may divide that they would rather not make loans available to their customers, thereby creating sub-optimal investment levels and a sharp contraction in economic activities, which further raises the probability of default among borrowers,

Fourth, financial deregulation model is the last approach that has- received considerable literature. Brownbridge (1998) and Mayo et al (2013) explain this approach by stating that deregulation of the domestic financial market, before adequate regulatory and supervisory framework and appropriate prudential guidelines were put in place, created wide latitude for excessive risk taking and eventually led to the distress and collapse of financial institutions.IMF country assessment reports on Ghana (2009; 2011; 2015) showed that the non-performing assets ratio to total assets ratio has hovered around 16.2% in 2009 and15.7% in 2015, confirming Dermicgue-Kunt and Detragiache (1997) assertion that any country with the ratio of non-performing assets to total assets exceeding 10% in the banking system could be classified as banking distress and crisis. The asset quality had deteriorated in the manufacturing, energy and construction sectors, which have been particularly affected by volatility in the exchange rates, high inflation and interest rates. Moreover, widespread defaulting on bank loans and other credit facilities by VRA, Electricity Company Ghana, Gridco, TOR and the private corporate sector burdened the banks with huge non-performing assets. The non-performing asset ratios were relatively higher than those recorded in the Sub-Sahara Africa countries (Kenya, 5.7%; Tanzania, 8.5%; South Africa, 3.5%; Cote D' Ivoire, 9.9%; Nigeria, 8.7%,IMF Country reports 2009-2015)

First, most of the causes of financial distresses in Ghanaian banking sector over the last decade could be attributed to macro-economic instability, lending to high risk borrowers , weak corporate governance practices, poor management, excessive concentration in the energy sector (oil, gas and electricity), huge exposures in the road sector and insider lending or connected lending (Brownbridge, 1998; IMF, 2013;2014;2015)The problem of poor loan quality and non - performing assets in the banking sector were compounded by macro-economic instability. Ghana has faced macro-economic challenges during the 2008 to 2016 period which could be traced in part of government policies, huge public sector debt and declining commodities prices of cocoa, gold and oil. Government fiscal policies were expansionary from 2008 through 2016; inflation and interest rises and the currency depreciation, the rate inflation surged above 18% in 2008 and remained high until declining to 15.7% in December 2016.Demirguc-Kunt and Detragiache (1997) argue that bank distress and crisis tend to erupt when macroeconomic environment is weak, particularly when growth is low, inflation is high and currency depreciation is persistent.

According to IMF country assessment report (2016, 16/16), the banking system remained generally well capitalized, liquid and profitable, although there is substantial weaknesses across banks. However, currency depreciation, and high inflation rates, and the slowdown activity had fed through the deterioration in the asset quality, that had reflected in the increasing deterioration in the non-performing loans as well as distresses in some of the banks. The non-performing loans growth and distresses have risen sharply in the, construction, manufacturing and energy sectors which have been particularly affected by exchange rate volatility and energy crisis over the period under review. High inflation worked against long term investments. Since investors were worried about maintaining the real purchasing power of their capital. Consequently, the government's accumulation of non-payment arrears to the Bulk Oil Distribution Companies (BDCs), road contractors and other service providers had undermined their capacity to service bank loans and other credit facilities across the banking industry and created non-performing assets.

As at the of December 2016, Ghana's total public debt stock stood at GH 122 billion or 70% of GDP). This high level of borrowing had huge implications for the economy not only in terms of crowding out local investors with regards to the high domestic borrowings, but total Government's ability to pay for it securities bought by many universal banks and which are forcing an increasing proportion of the earning assets of the bank due to attractive returns on these government securities (PriceWaterHouseCoopers and Ghana Bankers Association report, 2016, IMF,2016). These easy ways improving their fee incomes made banks to forget their risk asset monitoring and credit administration procedures.

The traditional core banking activity of lending only became a second investment option to money banks after looking at what these government securities were paying as returns. Macroeconomic instability had two important consequences on the credit portfolios of banks that operated in Ghana under the period of review. As fiscal deficits widened, inflation accelerated, interest rates rose above 30%, investors became skittish and began to exit the debt markets, and the exchange rates depreciated and thereby created conditions for asset price deterioration (IMF,2011,11/131). High inflation rates over the period had two consequences on the assets quality. First, high inflation increased the volatility of business profile because of its unpredictability and because it normally entails a high degree of variability in the rates of increase of prices of the particular goods and services which make up the overall price index. The probability that firms will make losses rises, as does the probability that they will earn windfall profits (Harvey and Jerkins, 1994). This intensifies both adverse selection and adverse incentives for borrowers to take risks, and thus the probability of loan default.The second consequence of high inflation is that it makes loan appraisal more difficult for banks, because the viability of potential borrower depends upon unpredictable developments in its individual correspondent, exchange rates and interest rates. Moreover, asset prices are likely to be highly volatile under such conditions. Hence, the future real value of loan security is also very uncertain (Brownbridge, 1998).

The second major factor contributing to bank distress was lending, at high interest rates, to borrowers in high risk segment of the credit market. This involved element of moral hazards on the part of both the banks and their borrowers and the adverse selection of the borrowers. It was motive by the high part motivated by the cost of mobilizing funds because as depositors perceived as being less safe, banks have to offer higher deposit rates and in also granted loans at higher rates (Brownbridge, 1998). Banks in the same period had difficulty in attracting non-interest bearing current accounts because they could offer few advantages to current accounts holders which could not also be obtained from holding the higher government treasury bills or gilt- edged securities by the Bank of Ghana. The high cost of funds meant that Ghanaian banks had to generate high earnings from assets, for examples charging high lending rates with consequences for the quality of their loan portfolios. Some of the banks especially the private domestic banks inevitably suffered from adverse selection of their borrowers, many of whom had been rejected by the established foreign banks, because they did not meet the strict, creditworthiness criteria demanded by them (Brownbridge, 1998) because they had charged higher lending rates to compensate for the higher cost of funds, it was very difficult for newly established private domestic banks to compete with the old established banks. As a result, the credit markets had been segmented with many of the private domestic banks operating in the most risky segments. Moreover, asset prices are likely to be highly volatile under such conditions. Hence, the future real value of loan security is also very uncertain. The second major factor contributing to bank distress was lending, at high interest rates, borrowers in the high risky segment of the credit market. This involved element of moral hazards on part of both the banks and their borrowers and the adverse selection of the borrowers. (Brownbridge,1998). It was in part motivated by the high cost of mobilizing funds, because they perceived by depositors as being less safe, banks have to in the rates increase of prices of the particular goods and services which make up the overall price index. The probability that firms will make losses would rise, as does the probability that they will earn windfall profits (Harvey and Jerkins, 1994).This intensifies both adverse selection and adverse incentives for borrowers to take risk, and thus the probabilities of loan appraisal more difficult for bank, because the viability of potential depends on unpredictable developments in the overall rates of inflation on its individual components exchange rates and interest rates.

Third, ownership structures might influence the governance process on bank performance and stability. Many countries have banking sectors with a mixture of ownership structures such as private ownership, government ownership and foreign ownership and with Ghana not being an exception. Ownership structure has also played a major role in promoting financial distress in the Ghanaian banking industry. The ownership factor has relevance to the management set up of banks. Ownership structure serves as an important element in corporate governance because they affect managers' performance by influencing the type of incentives received from the firm. The forms of ownership are developed around different configurations of control rights and residual rights with variations on the characteristics of these rights (Shleifer, 1998). In private domestic banks, shareholders own both the cash flow rights and control rights of the banks, while in the government owned banks, politicians or bureaucrats have concentrated rights but no significant cash flow rights as all the profits generated by the banks are paid out as dividend to the Ministry of Finance and Economic Planning to finance the national budget. In the foreign banks, both the control right and cash flow rights are assigned to foreign institutional investors. The Ghanaian banking industry has concentrated ownership structure in the form of foreign institutional investors, government ownership and private domestic investors. The controlling (large) shareholders have incentives to maximize own benefits at the expense of non-controlling shareholders. The controlling (large) shareholders elect their representatives to boards who appoint senior management team that acts in their interest (Jensen & Meckling, 1976). However, Ghanaian banks with high concentrated ownership are found to be prone to financial distress and crisis. The existence of large shareholders with high authority to make decisions and control the senior management creates moral hazard behavior which long term affects banks' credit portfolio and performance. This is because the large shareholders tend to behave in a self- serving behavior by making decisions that might increase the banks' risk and jeopardize the quality of the risk assets and long- term performance. As equity –owners, controlling shareholders appoint the directors and key management staff in the state- owned banks and private owned banks on the basis of flimsy considerations other than merit, competence, proficiency and experience in banking, finance, accounting and risk management. Most research on government ownership focuses on developing nations and nearly always finds unfavorable effects (Barth et al, 2004; Micco et al, 2007; Cornett et al, 2010). State owned banks have relatively low efficiency and high non-performing loans, with evidence from the credit crisis of 2007 supporting the views of Hau & Thum (2009).

Third, board qualifications had been one of the major sources of challenges for the banking sector since the deregulation of the financial sector in 1988. Most of the boards do not possess, both as individual board members and collectively appropriate experience, competencies and personal qualities, including professionalism and personal integrity. Most board members do not conform to the Principle 3 of the Core Principles Methodology of the Basel Committee on Banking Supervision (2005) on the ownership structure, board members and senior managers for fitness and propriety test. Most of the appointment to the state- owned banks' boards and managerial positions were heavily determined by political sentiments, sympathy and affiliation with the ruling party in power. For the private domestic banks, most appointment to boards and senior management positions, were based on family members, friends, in laws and ex-politicians. These persons become rubber stamps and "yes men and women" for the controlling shareholders in the area of connected lending, insider lending and excessive risk taking. Thus, excessive risk taking by some the banks created significant negative externalities and systemic risk. As pointed by Laeven (2012), the owners of banks do not internalize the risks that the distress of their banks will pose on the rest of the financial system, even though such systemic risk can pose significant threats to the broader economy. The cumulative effects of such behaviors impacted negatively on loan loss provision and operating expenses which contributed to lower performance and distress in the banking sector. Through the combination of high risk growth strategies and unsound lending practices by the “rubber stamp boards and management” have pushed the banks into distresses over the period 2009-2016. The boards of some of the state-owned banks and private domestic banks did not provide entrepreneurial leadership of the banks within a framework of prudent and effective controls. As most of the board members did not set the values and standards by engaging in insider lending, connected or related lending which impacted negatively on the credit portfolios of the banks. Balancing of the executive directors and non-executive directors on the some of the banks’ boards have also been a challenge. As practice demands, the board should include a balance of executive and non-executive directors (an in particular independent non-executive director) such that no individual or small group of individuals can dominate the board’s decision making.

Fourth, banking literature often cites mismanagement as the most important cause of bank distresses and failures. Pantalone and Platt (1987) state that “it is the management of the bank that determines success or failure. Most often banks fail, because they have chosen paths that are excessively risky for the returns that they receive and because those paths make them particularly vulnerable to adverse economic conditions. Seballos and Thompson (1990) wrote that “the ultimate determinant of whether or not bank fails in the ability of its management to operate the institution effectively and to evaluate and manage risks. Additionally, in a study by the Office of the Comptroller of the Currency to under specific reasons for bank failures, Graham and Horner (1988) concluded that the difference between the failed banks and those that remained healthy banks or recovered from distresses depended on the caliber of management. The importance of management quality in a bank cannot be overemphasized. Management determines allocation of the bank’s resources, establishes the internal controls and procedures, organizes strategic plans and responds to changes in the external environment. It is therefore the prime responsibility of bank management to provide adequate shock absorbers that helps to face the challenges of unstable external environment. Mismanagement caused some Ghanaian banks to distress in the period under the review. Bank distresses mostly come from the absence of good managerial ideas in management decision making. Therefore, competence and focus play a major role in banking (Spiegel et al, 1996). Poor management continues as one of the major reason for financial distresses especially in the government and quasi government banks and private domestic banks in Ghana. Some of these banks were characterized by inept management and instability in tenure of office of key management staff. Negative culture of interpersonal wrangling among board of directors and senior management staff led to polarization of rank and file that had persisted since the deregulation of the banking sector. Board members and senior staff in most of these banks with the state interest and private domestic owned banks embarked on empire building and financial conglomerates, bickering, quarrelling over perks and privileges and perquisites of office rather than charting strategic plans for their banks. Poor bank risk management procedures had also caused distress among Ghanaian banks. Hampel and Simonson (1996) state the main activity of a bank management is not deposit mobilization and giving credit. Effective credit administration reduces the risk of customer default. The competitive advantages of a bank are dependent on its capacity to handle issues in a professional manner. In addition, the increases in the number of banks in the 2000s brought enormous pressure on the available level of skilled manpower in the Ghanaian banking sector. The situation had been made worse by establishment of more savings and loan companies, finance houses, hire purchase companies as well as over 400 microfinance companies without adequate provision for manpower requirement internally and also the dearth of adequate regulatory supervision. The result was that banks had to hire people without the relevant skills and competencies for banking function. These scenarios accounted for the distresses in the banking sector. In the 2000s, banking was foray of all kinds of banking “gurus and specialists”, while their intelligence quotient cannot be doubted, they did not have any relevant professional qualifications, affiliations or experiences to bear on the banking jobs. Some of the persons hired at the executive positions saw themselves as “persons” and merely to make money and hence their social status and possibly return to their original professions. Many of the “big men and women” parading through the corridors of power and the banking business in Ghana are “failed bank officials not professional bankers” (Duru, 1998). Most distresses in banks with government and quasi-government participation and private domestic banks between 2009 and 2016 had no clear succession plans. In the state and quasi state banks had being convenient for government in power to gratify loyalists at the expense of competence and experience. For the private domestic banks in Ghana relied heavily on family members, in-laws, and close associates. Again, these groups of people, not only did they lacked technical competence and experience but they only become rubber stamps for the promoters and owners. These might have contributed to the high non-performing assets as well as widespread distress in the banking sector.

Fifth, deregulation of the Ghanaian financial sector in the 1990 contributed to the wide spread distress. The number of banks had increased from 10 in 1988 to 33 in 2016. The growth of private domestic banks since the financial sector deregulation in the 1990s was due to low entry requirements and perception that banking provides opportunities for profits not available in the other sectors of the economy (Brownbridge, 1998). The Bank of Ghana's licensing regulation has been subverted by various political interferences. For example, a case of political interference subverted prudential criteria in the granting of banking licenses, where two retired governors and deputy governors became owners and directors of the banks respectively. Furthermore, some deputy governors and directors of the central banks retired and just under two years there were appointed as board chairpersons and board members of some the Ghanaian banks. These actions have highlighted the lax regulation and supervision and weaknesses in enforcement and regulatory forbearance.

Sixth, the rapid growth did not grow in tandem with sound credit risk management practices and robust regulatory and supervisory framework. Between the early 1990s and the mid of 2015, the licensing procedures were too lax, allowing politically exposed persons (PEPs) to obtain licenses and operate banks despites having no relevant qualifications as specified by BCBS principles (2006; 2010; 2016), competencies and experiences. The Bank of Ghana between 1990s and the 2010s has licensed 23 new banks and non-banking financial institutions made up of 28 finance houses, 22 savings and loan companies, and about 400 micro-finance companies. The rapid growth in numbers of various banks and non-banking financial institutions overwhelmed the supervisory capacities of the Bank of Ghana as most on -site inspections were infrequent and were confined mainly to the checking compliance with allocative requirements. This combined with political constraints allowed some banks to flout the banking laws and regulations, as most failed to meet the minimum capital requirements, capital adequacy ratio and primary reserve requirements. It is also clear that regulatory on limit on secured and unsecured lending as in the Banking Act 2004 Act 673 an amended Banking Amendment Act 2007 Act 738 were flouted. The de-facto of licensing policy before prudential regulations and supervisory capacities were not strengthened which allowed under-capitalized and poorly managed banks and NBFIs that were set up in large numbers in the industry contributed significantly to financial fragility which subsequently afflicted the banking distresses and failures. Although, the Bank of Ghana is also responsible for supervising and regulating banks and other non-banking financial institutions, it lacked operational independence from the Ministry of Finance and Economic Planning, especially with regard to the licensing of banks and the enforcement of sanctions when infractions of legislations and regulation. Political considerations and lack of technical expertise and competencies in the Ministry of Finance and the Bank of Ghana impede proper supervision and regulation, in particular how licensed savings and loans companies and finance houses have migrated from the non-bank financial institutions into universal banking institutions with a short period. The recent collapsed of UT bank which was a finance house in the early 2000s and Capital Bank which was a savings and loan company were all issued with the universal banking licenses. These two institutions used to operate in the higher risk end of the market with little or no regulation but suddenly became highly regulated institutions and that brought huge challenges in the areas of compliance and regulation. Bank of Ghana must be wary of the speed and alacrity in which savings and loans companies, finance houses and mortgage companies are relicensed with universal bank licenses over night without proper due diligence. By conducting a comprehensive due diligence on the savings and loan companies and finance houses, Bank of Ghana would have had a thorough understanding of business models, ascertain the quality of assets and liabilities, andalso identified any surprise business liabilities. The due diligence should also cover legal, financial, operational, and human resource management and synergistic effects of the migration from non-banking financial institutions into universal banking status.

What have been the synergic effects for these failed banks? Hooks (1994) stated that deregulation results in higher risking by banks and this could lead to bank distress and failure. Edogahe (1996) also opines that free banking encourages in speculative investments and over-expansion which creates bank failures. Hareken (1981) cited by Hooks (1994) noted that deregulations are unsafe for banks. He explains that when banks have freedom of investment and diversification, the situation leads to higher risk taking which could impact negatively on loans and other risk assets. The Ghanaian banking sector has seen rapid development in terms growth in the numbers and diversification of products as well as the universal banking licensing concept in 2003 which created room for diversification of the range of financial services provided by banks could have resulted in the wide spread of distresses over the past decade. For example, the universal banking licensing concept removed the monopoly that was given to commercial banks in the area of retail banking (Bawumia, 2010) and removed the restrictions on banking activity in Ghana. The introduction of universal banks was basically recognition that the financial system had to become integrated and old system of commercial banks, merchant banks and development became anachronistic (Bawumia, 2010). The universal banking licensing allowed banks to choose the type of banking services in line with capital, risk appetite and business orientation. However, this has created room for diversification for the range of financial services that bank could offer without assessing capabilities and competencies of banks. The rapid financial sector liberalization unsupported by measures to encourage prudent risk management in the banking sector (including a failure to build robust risk management capacity within banking institutions and effective structures to encourage sound risk management practices).

Sixth, regulatory forbearance has a major cause of bank distress in the Ghanaian banking industry. Regulatory forbearance can be defined as a discretionary delay in enforcing appropriate actions to reduce the cost of bank failure. Hempel and Simonson (1994) noted that some regulatory authorities exercised forbearance. This contributed to bank crisis by permitting distressed banks to continue their operation. Previous studies have used the term “forbearance” in various contexts, such as prompt corrective actions, the delay of liquidations (Schellhorn & Spellman, 2000), do not take any action on the distressed banks and bail out without enforcement rules (Osterberg and Thompson, 1992). One reason for regulatory forbearance is the breakdown in the incentives that cause the regulator to defend the regulated banks (Kane, 1986; 1990; Boot and Tharkor, 1993). In particular, Boot & Tharkor, (1993) opine that the notion that a bank regulator may pursue self –interest rather than social welfare. According this model, the regulator desire to acquire a reputation as a capable bank monitor can distort bank closure policy and increase the liability of deposit insurance. Schellhorn &Spellman (2000) suggest that regulators may delay the liquidation process of the bank because they believe that the shareholders may appeal to the court to reverse the liquidation or receivership and access monetary damages. Allen & Saunders (1993) argue that response of regulators has often been characterized by delay due to budgetary and political considerations Bank regulators’ forbearance have been criticized for causing market discipline to fail in more than a few countries. In Ghana, for example in 2010, the unprecedented losses from bank distresses have provided serious criticisms by IMF (2011) of regulatory forbearance, which Bank of Ghana allowed two insolvent banks to continue their operations. According to IMF country assessment report (2011, 11/131), the Bank of Ghana's regulatory forbearance enabled some Ghanaian banks to build loan concentration above regulatory limits without making adequate provision. Weaknesses in enforcing prudential regulations allowed some universal banks to build up substantial loan concentrations while deficiencies in the analysis of individual bank risk and systemic risks have led to under-appreciation of stability risk implications (IMF, 2011, 11/131). Universal banks in Ghana were highly exposed to credit risk since lending which accounts for the bulk of risk assets had grown in the environment of weak credit management and poor enforcement right of creditors.Poorly designed and implemented bank supervision and prudential regulation, including insufficient structures to ensure that Ghanaian banks maintain a prudent level of capital relative to their risks and have robust risk management systems, insufficient scrutiny of lending quality, and exposure concentration, and inadequate measures to constrain connected or related lending.

Seventh, weak corporate governance particularly ineffective board practices, excessive risk taking, connected or related lending, contravention of prudential guidelines, overbearing CEOs and board chairpersons, poor risk management, political interferences and ownership structure are some of the major causes of the bank distresses in Ghana. In addition, non-compliance with banking laws and regulations, weak internal controls and boards' incompetence and poor credit administration procedures also lead to banking distress in Ghana. World Bank ROSC (2005; 2010) conclude in his findings on "Nurturing corporate governance system: emerging trends in Ghana", concluded that major challenges which require urgent attention to enhance the effectiveness of the system were noted "making voluntary codes mandatory for the listed companies; developing more effective mechanisms for monitoring complianceand enforcement; developing strong internal control mechanisms to checkmate the boards ; crafting strategies to enhance shareholders activism and the extension of the codes to banks and state-owned enterprises with more cases of corporate abuses". Weak corporate governance (associated poor risk management practices) in the business and corporate sectors increased the risk profile of companies especially in the SOEs (VRA, Ghana Electricity Company Ltd, TOR, and Gridco) and exposed Ghanaian banks and other financial institutions to a greater risk of loss than would otherwise be the case. In a more direct sense, weaknesses in corporate governance arrangements in banks and other financial institutions reduced their capacity to identify, monitor and manage their business risks and which resulted in poor quality lending, excessive risk taking by banks. For example, inadequate corporate governance arrangement led to poor management of credit risks, insufficiently developed “credit culture”, excessive exposure concentration and inadequacies in the management of connected or related lending. In the recent cases of the collapsed of UT bank and Capital Bank, inadequacies of corporate governance, regulatory failure and poor risk management led to the two banks’ insolvency and financial instability.

The SEC code of best Practice for Public Companies in Ghana is voluntary and is designed to entrench good business practices and standards for all listed companies, including banks. The mandatory corporate governance provisions relating to banks are contained in the Companies Act 1963 Act 179; Bank and Other Deposit Taking Institution Act 2016 Act 930; Banking Act 2004 Act 674 as amended by Banking Amendment Act 2007Act 738; in 1993, the Investments and Securities Act 1993 (PNDC Law 333) as revised Securities and Exchange Commission Amendment Act (2000) Act 590; Securities Industry Act 2016 Act 929and Ghana Stock Exchange Listing Rules (L.I. 2006 1509). In addition to the numerous legislations, the Bank of Ghana as a matter of urgency should implement a mandatory code of corporate governance for the banks, savings and loan companies, and microfinance companies operating as done by the Central Bank of Nigeria (2006; 2014).

The impetus for the development of corporate governance system in Ghana also came through the activities of the Ghana Securities and Exchange Commission (SEC). In 2003, the SEC developed a Code of Best Practices for Public companies in Ghana was adopted (SEC, 2003) and was revised in 2010. The code is voluntary and is designed to entrench good business practices and standards for boards and directors, CEOs, auditors, etc., of listed companies, including banks. The SEC Code (2003; 2010) was divided into six sections namely as the responsibilities and accountability of the board of directors, board composition and qualification, board committees, relationship to shareholders and stakeholders and the rights of shareholders; financial affairs and auditing and ownership structure and control. Despite the growth of banks since the deregulation of the financial sector, the Bank of Ghana is yet to develop a code of corporate governance for the banking sector as has been done by the Central Bank of Nigeria (2006; 2014). A major development in the history of corporate governance in Nigeria is the recent intervention by the Central Bank of Nigeria (CBN).The incessant collapse experienced in the banking sector due to poor corporate governance and the recent bank consolidation exercise forced the CBN to issue new corporate governance guidelines to all banks operating in the country in (2006; 2014). Known as Central Bank of Nigeria Code for Corporate Governance for Banks in Nigeria Post Consolidation (CBN, 2006; 2014), the code seeks to address the issues of poor corporate governance and create a sound banking system in Nigeria. The code introduced more stringent requirements in the area of industry transparency, equity ownership, criteria for the appointment of directors, board structure and composition, accounting and auditing, risk management and financial reporting whereas the Bank of Ghana is yet to implement a mandatory code of corporate governance for the universal banks operating in Ghana. The question I want to ask is that "Does Bank of Ghana need IFC or the World Bank to prompt them of the importance and relevance of code of corporate governance for banking sector after nearly three decades of the financial sector reforms". In 2006, the Central Bank of Nigeria developed its first code of corporate governance for banks and discount houses. According to the Central Bank of Nigeria in 2014 developed new code according to CBN was developed to complement existing codes in the country, and compliance to it is mandatory for all banks and discount houses. To improve on governance and regulation of banks, CBN has since 2010 abolished its universal banking concept and replaced it with financial sector policy conducted through there-licensing of banks which sought to serve multiple objectives that are meant to develop specialized segments of banking and financial services notably commercial banking, merchant banking, development banking, construction banking and mortgage banking. The Bank of Ghana can also adopt the tiered recapitalization policy that will enable smaller size, medium size and big size banks to operate in the banking sector.

. In their review of corporate governance in Africa, Okeahalam and Akinboade (2003) conclude that “the adoption of corporate governance principles by African countries will be a giant step towards creating safeguards against corruption and mismanagement, promote transparency in economic life and attracting more domestic and foreign direct investment”. Biepke and Kyereboa- Coleman (2006) evaluated corporate governance issues in public quoted companies in Ghana. The findings of the study show that Ghanaian public companies have embraced the principles of good governance but at different stages of adoption of various issues that contribute to good governance. Owusu (2012) suggest that for Ghana to reap the benefits of effective corporate governance there is need to strengthen the enforcement mechanism of the regulatory institutions.

Eighth, the issue of corporate governance had also received a lot of attention from the World Bank ROSC reports (2005; 2010) and IMF country assessment reports (2011; 2012; 2013). These reports cited weaknesses in the corporate governance practices in the banks and non-banking financial institutions. The identified weaknesses manifested in lack of internal controls, poor risk management, ineffective board practices, and non-existent of code of corporate governance and weaknesses in regulation and supervision. Bank of Ghana in 2006 cited "the following challenges include technical incompetence of board management; Boardroom squabbles among directors; squabbles among staff and management; very few banks have a robust risk management system; malpractices and sharp practices; connected lending; rendering false returns and concealment of information from examiners; ineffectiveness of board/statutory committees and inadequate operational and financial controls".SEC (2003; 2010) opines that all existing companies including banks in the country are required by the code to adopt and enforce well- articulated codes of ethics and conduct for directors, management and staff and to render periodic report (Templars, 2006). The key highlights of the codes of corporate governance of SEC include: Separating the roles of the CEO and board Chairman; prescription of non-executive and executive directors on the board; improving the quality and performance of board membership; introducing merit as criteria to hold top management position; introducing transparency, due process and disclosure requirements; transparency on financial and non-financial reporting; protection of shareholder rights and privileges; and defining the composition, role and duties of the audit committee, etc (Wilson,2006). FINSSIP 11 (2012) posits that the appointment of directors to the financial institutions including banks should be considered as a matter of urgency, because the appointment to boards does not necessarily depend on due qualifications, competencies or appropriate skills. Boards of directors suffer from poor capacity and the passiveness of directors.

However, deliberate accounting fraud is serious problem of corporate governance in the country. Cases of “tunneling, inaccurate reporting and non-compliance with regulatory requirement” and “the prevailing incidences of false and misleading financial reporting” by some corporate organizations lead to corporate failures. Unlike Nigeria where such issues are considered as criminal charges and the culprits are prosecuted and jailed by the Nigerian Economic Crime Agency, in Ghana such criminals go unpunished (i.e.Culprits in BHC and Ghana Cooperative Bank debacle in the early 2000s).

Ninth, Etukudo (2000) argued that the shareholder associations serve the interest of the investing public as shareholders who had the opportunity to contribute to the formulation of broad corporate policies, thereby enhancing management accountability. However, for effective performance of this body, corporate governance institutions need to strengthen shareholders activism as a prerequisite for effective corporate governance and accountability in Ghana. In Ghana, there is the general weakness of public institutions, high level of corruption, poor managerial capacity and total absence of market discipline for transparency and accountability, which combine to create a seeming lack of demand for corporate governance in state-owned enterprises (World Bank ROSC,2005;2010).The corporate governance framework also depends on the legal, regulatory, and institutional environment. There are too many institutions, laws and regulations but enforcements had been the major challenge. In addition, two factors such as business ethics and corporate awareness of the environmental and societal interest of the communities in which a company operates will also have an impact on its reputation and its long- term success. Therefore, the primary causes of banking distresses were due to macroeconomic instability, weak corporate governance practices, inefficient and ineffective regulatory and supervisory framework, excessive risking taking and lending booms characterized by rapid increases in banks, credit portfolio and weak risk management practices in the Ghanaian banking sector.

1.2 Key elements of a sound corporate governance framework in a bank

BCBS (2006; 2010; 2015) expressly state the main elements of corporate governance in a bank to include the following:

- A well -articulated corporate strategy against which the overall success and the contributions of individuals can be measured;
- Setting and enforcing clear assignment of board responsibilities, decision making authority, and accountabilities appropriate for banks selected risk profile;
- Strong financial risk management function (independent of business lines), adequate internal control systems (including internal and external audit functions), and functional process design with the necessary checks and balances;
- Adequate corporate values, codes of conduct, and other standards of appropriate behavior and used to ensure compliance. This includes special monitoring of the bank's risk exposure where conflict of

interests is expected to appear (example relationship with affiliated parties).

- Financial and managerial incentives to act in an appropriate manner offered to the board, management, and employees, including compensation, promotion, and penalties (compensation should be consistent with the banks objectives, performance and ethical values).
- Transparency and appropriate information flow internally to the public.
- According to SEC (2003; 2010), “No one person should combine the post of Chairman/Chief Executive Officer of any company”. No two members of the same extended family should occupy the position of Chairman and that of Chief Executive Officer or Executive Director of a bank at the same time. The office of the Chief Executive should be held by a different person other than the chairman. This is because such step could lead to the problem of moral hazard and thereby threatening the financial sector stability. Effective corporate governance is all about board’s performance. The task of growing a corporate entity is the work of board of directors. For a board to function effectively, it should be composed of members who are

independent, skilled, knowledgeable, experienced and of diverse perspectives. In Ghana there has been a high-profile case of corporate failure which is traceable to weak and ineffective boards. In some cases, the board appear were dormant being satisfied with having business cards that identify them as board members. Critical reviews of the nation's banking system over the years have shown that one of the problems confronting the sector had been that of poor corporate governance. From the various IMF reports of banks distressed between 2011 and 2016, there were evidences that clearly established that poor corporate governance led to the distresses in the banking sector. A further revelation showed that some senior managers and directors abused or misused their privileged positions or breached their fiduciary duties by engaging in self- serving activities. The abuses included granting of unsecured credit facilities to owners, directors and related companies which in some cases were in excess of their banks statutory lending limits in violation of the provisions of the law.

BCBS (2010) contends that the primary responsibility of keeping individual bank sound lies with each bank's owner, managers, and the board of directors. Together, they must establish a framework of internal controls and practices to govern the operations of the bank and ensure that it functions in a safe and sound manner. Poor internal governance has been identified as a major factor in virtually all known instances of banking unsoundness. One basic requirement is that persons who control and manage the business of banking must been of integrity, above board, trustworthy and must possess appropriate skills and experience.

BCBS (2010), posits that disclosure and transparency are key pillars of a corporate governance frame work, because they provide all the stakeholders with the information necessary to judge whether or not their interest are being served. He sees transparency and disclosure as an important adjunct to the supervisory process as they facilitate banking sector market discipline. For transparency to be meaningful, information should be accessible, timely, relevant and qualitative. According to Anameje (2007) as cited in Babalola (2010), transparency and disclosure of information are key attributes of good corporate governance which banks must cultivate with new zeal so as to provide stakeholders with the necessary information to judge whether their interest are being taken care of. Sanusi (2003) opines that lack of transparency undermines the ethics of good corporate governance and the prospect for effective contingency plan for managing systemic distress. There are various laws put together to regulate the practice of a particular trade or profession in order to protect investors and ensure a stable business environment and to prevent distress, which in this case concerns the banking industry. They are Bank of Ghana Act (2002) Act 612, Banks and Specialized Deposit Taking Institution Act 2016 Act 930; Banking Act 2004 Act673 as amended Banking Amendment Act 2007 Act 738; Investment and Securities Act (PNDCL Law 333) 1993 as amended and other laws. However, the basic laws governing all companies operating in Ghana is the Companies Act 1963 Act 179. The Act makes it mandatory that all companies operating in Ghana must be registered either as a private company or as a public company limited by shares. The provisions of the Companies Act 1963 Act 179also require that the financial statements of each company should conform to the accounting standards. Specific standards for reporting consolidated accounts regarding all or any of the subsidiaries of the company must be specified. In Ghana, the connected lending, massive and prevalent frauds, mandatory retirement of CEOs of banks, due to corrupt practices and inefficient rubber-stamped board, have combined to signal the absence of or failure of existing corporate governance structure. The Companies Act 1963 Ac179 enacted to regulate and balance the relationship among the board, shareholders and the management including other stakeholders, failed woefully due to inadequate enforcement capacity.

1.3 Challenges and Failures of Corporate Governance in Ghanaian banking sector.

The challenges and failure of corporate governance in Ghana stems from the culture of corruption and lack of institutional capacity to develop, implement and enforcement of the codes of conduct governing corporate governance in the banking sector. Company executives enjoy an atmosphere of lack of check and balances in the system to engage in gross misconducts since investors are not included in the governing structure. The Bank of Ghana's policies and procedures required to ensure efficient internal controls are disregarded, and total lack of thorough selection process (of CEO and board members – round pegs in square holes) remain a challenge in Ghana. The Principle 3 of the Core Principles Methodology of Basel Committee on Banking Supervision to evaluate proposed board members and senior managers for fitness and propriety are most often not applied strictly. The fit and proper requirements for the board of directors and senior managers are to prevent known and unknown incompetent or corrupt persons from running a banking institution for their own benefit the expense of depositors.

The businesses cum shareholders' interests are secondary to the self - interest of board members and the management. Limited opportunities for institutional investors and near zero interest in corporate social investments to demonstrate companies' sense of belongingness as evidenced in high interest charges, unfair treatment of bank customers and unprofessionalism in banking, are clear indications of failure of corporate governance. Lack of managerial training and capacity development among Ghanaian executives to manage business risks has resulted in huge agency costs, and shareholders have had to shoulder several avoidable agency costs since the board of directors usually failed as a monitoring device to minimize agency problems.

BCBS (2010; 2015) posit that new board members and existing board members must be trained continuously to deepen their knowledge and skills to fulfill their responsibilities. The board should ensure that board members have access to programs of tailored initial (e.g. induction) and ongoing education on relevant areas such as oil and gas financing down and up- stream; global financial crisis impact, and cocoa loans syndications.

The failure in corporate governance in Ghana banks has also been traced to lack of effective yardsticks to evaluate board and management processes and performance, since the board sub-committees required to be fully independence, especially the audit, risk and remuneration committees, are compromised. The auditors/the audit committee of the board have been singled out as instrument of fraudulent practices given their readiness to cover-up corrupt practices for executives in a desperate bid for kick-back, and, to retain the audit engagement(s)

Of big clients (Habeeb, 2010). According to the Bank of Ghana (2006), the

Following are challenges that are faced by banks in respect to the adherence to the good corporate governance practices;

Technical incompetence of board and management:

in view of the greatly enhanced resources of the expanded entities, board members may lack the requisite skills and competences to effectively redefine, re-strategize, restructure, expand and or refocus the enlarged entities in the areas of change of corporate entities new business acquisitions, branch expansion and product development. BCBS (2010;

2015) posits that the banks' board of directors should collectively have adequate knowledge and experience relevant to each of the material financial activities the bank intends to pursue in order to enable effective governance and oversight. However, most Ghanaian banks financed the energy sector (oil, gas, electricity) without having the relevant expertise and competencies in that sector. Most board members did not have appropriate experience and expertise in finance, accounting, strategic planning, risk management, bank regulation, auditing and compliance as specified in BCBS (2006,2010l 2015)

Relationship among directors: boardroom squabbles could be an issue due to different business cultures and high ownership concentration especially in banks that were formerly "one-man" entities. The dominance of a "key man" could also emerge with the attendant problems. BCBS (2010; 2015) opine that the board should ensure a demonstrated corporate culture that supports and provides appropriate norms and incentives for professional and responsible behavior as an essential part of good corporate culture. In this regard, the board should take the lead in establishing "the tone at the top" especially in setting in setting professional standards, which includes optimal risk appetite, risk tolerance limits and corporate values that promote integrity for itself, senior management and other employees. Directors must also ensure that banks maintain an effective relationship with the regulatory authorities. Bank of Ghana must ensure that the boards of directors exercise their “duty of care” and “duty of loyalty” to the bank under the Companies Act 1960 Act 179 and Banking Act 2004 Act 673 as amended by Banking Amendment Act 2007 Act 738 and supervisory standards.

Increased level of risks: Currently, very few banks have a robust risk management system in place. With the huge amount of funds that will be available to them and the significantly increased legal lending limits, banks will be financing more long term mega projects in the real sectors of the economy as opposed to the existing working capital/trade financing. Given the expected significant increase in the level of operation, the banks will be facing various kinds of risks which, if not well managed, will result in significant losses. The management of risks in a transparent and ethical way will thus present some issues bordering on corporate governance. Most banks have the board committee for risk management, but few banks are aware of their current and future risk tolerance / appetite and strategy. Do board members ensure that internal risk measurements cover scenario analysis and stress -testing and availability of reliable data to aid strategic decision making?

Resurgence of high-level malpractices: to boost income as a result of intense competition and lack of enough viable projects, malpractices may resurface post financial sector period. Such sharp practices could include round tripping of energy sector, high interest rates charged by banks, falsification of records etc, and adoption of unethical methods to poach customers. The corporate failures which characterized 2000 to 2002 when institutions like Enron and WorldCom collapsed brought corporate governance issues to the front burner. Arunma (2010) stated thus that “corporate failures no doubt drew the world’s attention to the fact that good corporate governance was extremely important to corporate performance and survival; indeed there is a nexus between good corporate governance and the preservation of shareholders value, safeguarding investors’ assets and promoting financial stability particularly, when governance of financial institutions is concerned. Indeed good corporate governance has become an important index for institutional investors’ participation in business enterprises and financial markets”.

Lack of education for Shareholders and other stakeholders about their rights

Awareness of corporate governance is generally low in Ghana and shareholders do not know about their rights. There is not enough shareholder activism. For example, at the annual general meetings there is not enough probing of directors on the operations of the banks they have invested in. Shareholder associations should be formed so that members can be educated on their rights. Recent trends in corporate governance at large, publicly listed companies in USA include increased shareholder power to relative to the board. Shareholder activism can be defined to include any action (s) of any shareholder or shareholder group with the purpose of bringing about change within a public company without trying to gain control (Gillan &Starks, 2007). Proponents argue that companies with active and engaged shareholders are more likely to be successful in the long term than those that are left to do what they choose. Vigilant shareholders are said to play the role of fire alarms and their mere presence improves managerial inefficiency or ineffective board of directors. In particular, mechanism must be instituted to ensure that minority interests are upheld. When companies including banks perform poorly, shareholder activists are said to play the role of fire bridges that bring about change and more quickly. The goal of shareholder activism is usually to encourage one of four types of changes: (i) a change to board's governance policies and practices; (ii) a change to the company's oversight of certain functions (e.g. audit; risk management); (iii) a change to the company's behavior as a corporate citizen (political spending or lobbying; social and environmental risk practices) and (iv) a change to company's directors' and executive compensation plan. However, opponents argue that shareholder activism is a euphemism for disruptive, uninformed, populist ranting or "take the money and run". In its extreme, forms activism is said to be extortion scheme that weaken strong companies (ECGI, 2012)

1.4 Conclusion and recommendations

From the foregoing discussions, it is clear that poor corporate governance practices lead to bank distresses and failures. The problem of distress can affect a single bank as well as many banks within the banking industry. The weaknesses in corporate governance practices and distresses and failures are not only peculiar to Ghana, but it cuts across the entire world both developing and developed economies. Erkens et al (2013) provided evidence that weak corporate governance practices affected the performance of financial firms during the 2007-2008 global financial crises.

They posited that corporate governance had an important impact on banks' performance during the crisis through firms' risk taking and financing policies. The impact of poor corporate governance practices on the distress in the Ghanaian banking system, was manifested in loss of confidence by the banking public, liquidity squeeze on the part of distressed banks and non-performing risk assets which resulted in high loan loss provisions that impacted negatively on banks' capitalization policy. It is therefore imperative that Bank of Ghana and SEC should take steps to improve on corporate governance practices in the banking sector to prevent the wide spread of distresses and failures experienced in the late 1980s. In particular, we know that bank distress in Ghana and other economies have been caused in partly, by excessive exposure concentration, macroeconomic instability, weak corporate governance practices, lending to connected parties and poor risk management practices. The Ministry of Finance and Economic Planning which has the overall responsibility must take immediate steps to develop, implement, and supervise the corporate and financial governance super structure in Ghana. The continuous nature of distress in the banking sector, to a large extent,such as basic risk management failures reflect a break down in corporate governance practices in the banking sector. They reflect poor management of conflict of interest, inadequate understanding in the board room of key banking risks and poor oversight by boards of the mechanism for managing their banks, such as enterprise wide risk management system and internal control and internal audit arrangements. In some cases, a lack of truly independent directors on the boards of banks was also significant factor in weakening the effectiveness of boards. There must be a proper definition and qualification of board independence

Adherence to corporate governance is the foundation for effective risk management. It is evident that sound corporate governance is essential to the well-being of a bank and protection of interests of other stakeholders, particularly its shareholders and creditors. Practice of good corporate governance is not just a vital factor at the level of individual bank; it is also a critical ingredient in curbing distress in banks, promoting and maintaining a sound financial system and stability which in turn ensures a robust economy. To this end, the government through the regulatory authority (i.e. Securities and Exchange Commission) has taken keen interest in reviewing and emphasizing the adherence to the year 2010 revised code of corporate governance in order to curb future corporate distress in Ghana. The Bank of Ghana should urgently develop and implement its own code of corporate governance for all universal banks, savings and loan companies, micro-finance companies as well as other NBFIs.

1.5 Recommendation

Based on the theoretical and empirical findings in this study the following recommendations are made:

(1) Since corporate governance has a significant improvement on the prevention of bank distress; banks should be able to demonstrate that rigorous internal policies were in place and that procedures exist for identifying and managing conflicts of interest to avoid its adverse consequences on their customers and other stakeholders. Insider abuse, conflict of interest and widespread manipulations are at the heart of a nation's financial sector crisis. Such crisis connived at or orchestrated by management and board, should be captured by internal and external auditors and regulators so as not to reach serious proportions. The Bank of Ghana should ensure that board of directors do not abdicate their oversight responsibilities over senior management of Ghanaian banks including the review and approving the bank's strategic plans on a regular basis and also evaluate the risk management practices including the strict observance of the bank's risk appetite and tolerance levels, liquidity and capital planning

in a manner which are consistent with the banks' strategic plans. The Bank of Ghana should ensure also that ethical tone at the top by overseeing the development and implementation of code of conduct for all directors, senior management team and employees and that these addresses the treatment of breaches or lapses in ethical behaviors including inside abuses and dealings with the view of improving on the quality of assets to reducing loan loss provisions

(2) The study shows that corporate governance has the capacity to significantly improve the performance of the Ghanaian banking sector. Therefore, in addressing the role of corporate governance in curbing distress, the central bank should review the fit and proper person's regime in order to ensure that only credible persons of impeccable financial, personal and professional character are allowed as major shareholders, directors and managers of banks. The central bank should also strengthen its on-site and off- site supervision functions in recognition of the need for an effective supervision of the banking sector.

(3) The Bank of Ghana should implement a mandatory code of corporate governance for all banks and NBFIs. For example, to ensure that there is a clear division between the chief executive officer and the managing directors. The Bank of Ghana should ensure that the term for the CEOs or

MDs does not exceed 10 years. The tenure of non-executive directors should be set for initial 4 years with the upper limit of 8 years. The term independent directors should be properly defined to avoid any ambiguities. Persons occupying these positions should be properly approved by the apex body i.e. Bank of Ghana and such persons must be knowledgeable in business and financial matters with requisite experience in the banking field. The code of corporate governance must be made mandatory with the appropriate sanctions for the defaulting banks.

Of critical importance must be requirement that the Bank of Ghana should also ensure that Governors, Deputy Governors, Directors and Assistant Directors from the central bank do not accept board membership on the universal banks' boards after their retirement until a lapse of time limit of 10years as done in other jurisdictions.

(4) The Bank of Ghana must also ensure that banks should establish committees within their banks so as to oversee the management of risk, audit and credit. This is also to forestall any potential risk and prevent the bank from any imminent or future distress. The board should appoint members to these committees with the goal of achieving an optimal mix of skills, competencies and experience that, in combination, allow the committees to fully understand the factors and causes of distress and

objectively evaluate the strategies to address issues and bring fresh thinking into all the relevant issues concerning bank distresses. The Bank of Ghana must ensure that audit committees must be constituted of people with back ground in accounting, auditing, banking and finance while the risk committee must be comprised of finance, economics with econometric, mathematics, statistics, accounting and banking backgrounds. There is therefore the need to strengthen boards through initial and ongoing screening and training programs’ and to encourage continued improvement programs for all directors

(5) Bank of Ghana and other regulators in the Ghanaian financial sector need to adopt a zero tolerance posture against cases of unsound corporate governance practices. This will ensure that the banks are well run and administered. Identifying, preventing and managing conflict of interest should be at a very heart of corporate governance. The Ghanaian bank boards’ should ensure that policies to identify potential conflicts of interest are developed and implemented.

(6) The Bank of Ghana and relevant professional bodies such as Chartered Institute of Bankers of Ghana (CIB.Gh) and Institute of Chartered Accountant Ghana should ensure that bank workers do not hold vital position in the banks but rather bankers who have proven competence and

track records after the completion of the relevant professional courses should be given full backing to operate.

(7) In view of the low awareness of corporate governance practices in the banking business and most shareholders lack of knowledge rights including the minority, regulators like Bank of Ghana, SEC and Ghana Stock Exchange (GSE) should educate the shareholders on Shareholder Activism especially for institutional investors such as SSNIT which has significant shareholdings in nine universal banks operating in Ghana. For example, at the annual general meetings there is not enough probing of directors on the operations of banks they have invested in. Shareholder associations should be encouraged so that members can be educated on their rights and responsibilities (FINSSP, 11, 2012). Shareholder activism allows shareholders to impose control through involvement and engagement in company management; it also provides a secondary control system that can complement the existing governance structure of companies including banks with poor governance practices. This activism can play important role in reducing the agency costs by closely monitoring of company management through voting powers; the power to file a suit in court, and the selling of interests in the firm, thus aligning the interests of managers

and shareholders in order to ensure corporate sustainability and longevity (Thomas, 2008)

(8) In addition to good corporate governance practices in the banks, the government and Bank of Ghana must restore macroeconomic stability through an ambitious and sustained fiscal consolidation, prudent debt management strategy with improved fiscal transparency and effective monetary policy framework that go a long way to improve on high non-performing loan losses and distresses in the banking system. Lower inflation and interest rates, combined with a stable exchange rate environment would help to improve on loan losses provisions that banking system had been experiencing over the last decade.

(9) Pro-active approach to banking supervision should be advocated for banks and non-banking financial institutions. Bank of Ghana should identify banking system vulnerabilities through continual assessment on liquidity and solvency. This will allow the regulatory authority to classify whether the institution is suffering liquidity or solvency when a banking problem surfaces and the implications of the failure would be. Implementation of the Basel Committee on Banking Supervision and Surveillance (enterprise wide risk management framework) and corporate governance issues

(internal audit and internal control) should be practiced rather than to be continually on paper or the book shelf.