

**PROFIT BEFORE PEOPLE: CORPORATE GOVERNANCE AND THE
STATUTORY PROTECTION OF THE PUBLIC INTEREST IN THE
PRIVATISATION OF STATE CORPORATIONS - THE CASES OF DAVID
WHITEHEAD AND SONS LTD AND THE MALAWI SAVINGS BANK**

MASTER OF LAWS IN COMMERCIAL LAW (LL.M) THESIS

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Submitted to the Faculty of Law in partial fulfillment of the requirements
for the degree of Master of Laws (Commercial Law)

**UNIVERSITY OF MALAWI
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MAY, 2017

DECLARATION

I, the undersigned, hereby declare that this thesis is my own original work which has not been submitted to any other institution for similar purposes. All the sources that I have used or quoted have been indicated and acknowledged by means of complete references.

Name

Signature

Date

CERTIFICATE OF APPROVAL

I, the undersigned, certify that this thesis represents the student's own work and effort and has been submitted with our approval.

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DEDICATION

To Hendrina my dearest Wife who gave me all the support and the spaces that I needed and my sweetest daughters Vanessa and Watipaso who believed I could do this even after the age 50. They gave me tremendous encouragement when I really needed it.

*Our selfish hearts make true, our faith failing renew
Our life belongs to you, our Lord and King.....*

*Take all that daily toil, plants in our heart's poor soil,
Take all we start, and spoil, each hopeful dream.
The chances we have missed, the graces we resist
Lord, in thy Eucharist, take and redeem*

Msgr Kevin Nichols- Roman Catholic Hymns

ACKNOWLEDGEMENTS

I would like to express my deepest and most profound gratitude to my supervisor Professor Edge Kanyongolo who gave me direction, tremendous guidance, support and encouragement even when I thought I was lost in my thesis and could not go on. Many thanks go to my friend and Classmate Masauko Msungama who made numerous phone calls to check on me and to encourage me. A big thank you to late George Bakuwa for giving me a book that I found very helpful. Many thanks go to Matthias Chiwaya my Secondary School classmate and Librarian for helping with the articles that I could not download off-campus. Sincere appreciation to Mrs. Emily Makuta my Corporate Governance Lecturer who made comments that made me think and thus indirectly was responsible for the choice of my thesis topic. Mr. Sunduzwayo Madise my initial Course Coordinator who in his lectures made presentations almost effortlessly and made it all look so easy. Mr. Henry Ngutwa my Taxation Law Lecturer who unbundled taxation in such an elaborate fashion, I was able to see clearly tax issues I had considered complex. My classmates in the 1st LLM Cohort, they were a diverse and an interesting lot. Most of all my very special thanks go to Dr. Ngeyi Kanyogolo who made an impassioned presentation on my behalf without which this Thesis would never have been presented.

ABSTRACT

In the year 1996 the Government of Malawi (GoM) passed the Public Enterprises (Privatization) Act (PEPA) which it subsequently applied in the privatization of a majority of its State Owned Enterprises (SOEs) including David Whitehead and Sons (DWS) Ltd. In 2011, PEPA was repealed and replaced with the Public-Private Partnership Act (PPPA) which was intended to improve the legal mechanisms for facilitating privatization of state corporations. Using the PPPA, the government proceeded to privatize a number of enterprises, including the Malawi Savings Bank. The privatization of DWS and MSB generated significant public debate around the question whether the processes had taken sufficient account of the public interest as required by corporate governance principles governing public enterprises. Despite the said high public interest in the matter, there has never been any systematic academic study of the issue to provide an evidence-based response to the question. This dissertation seeks to fill that gap by presenting and discussing the findings which emerged from research which compared the effects PEPA and PPPA on the safeguarding of the public interest in the privatization of public enterprises. The research uses a comparative study of the privatization DWS and the privatization of MSB. The main finding that emerged from the doctrinal study of the question was that the PPPA did not significantly improve on the PEPA with respect to the provision of statutory protection of the public interest in the privatization of state-owned enterprises to meet the standards set by corporate governance. The paper thus suggests a revision of the conceptual, institutional and legal framework in PPPA to align it with corporate governance principles that safeguard the public interest so as to inform future privatizations.

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Competition and Fair Trading Act (Act No. 43 of 1998)

Companies Act (Act No. 19 of 1984)

LIST OF ABBREVIATIONS AND ACRONYMS

ACB	Anti-Corruption Bureau
AGOA	African Growth and Opportunity Act
ADMARC	Agricultural Development and Marketing Corporation
CG	Corporate Governance
DWS	David Whitehead and Sons
ECSAFA	Eastern, Central and Southern African Federation of Accountants
FDH	First Discount House
GoM	Government of Malawi
IFIs	International Financial Institutions
MGDS	Malawi Growth and Development Strategy
MRFC	Malawi Rural Finance Company
PEPA	Public Enterprises (Privatization) Act
PC	Privatization Commission
PPPA	Public-Private Partnership Act
PPPC	Public-Private Partnership Commission
SAL(S)	Structural Adjustment Loan (s)
SAP (S)	Structural Adjustment Program (s)
SOE	State Owned Enterprise

CHAPTER 1

INTRODUCTION

Background

1.0 What is privatization?

As with many other African states, Malawi became an independent country without having in place adequate institutional structures to support socio-economic development. Among the many arguments for independence was one that the colonial governments did not act in the best interests of the indigenous Africans.¹ In the period following the attainment of independence therefore many corporations were created under state ownership out of a desire on the part of governments to have enterprises that served the broader public interest. These State Owned Enterprises (SOEs) were often expected to serve the national interest by channeling investment into sectors that were deemed to be national priorities by the state, or to assist in the “incubation” of industries intended to bolster international competitiveness (Heath & Norman, 2004)². Beginning in the 1970s, state ownership and control of SOEs was becoming unfashionable and the trend globally was towards privatization.

Privatization is not one clear and absolute economic proposition. Rather it covers a wide range of different activities, all of which imply a transfer of the provision of goods and services from the public to the private sector. For example, privatization covers the sale

1. “The fight against colonialism and imperialism in Africa” accessed at <http://www.sahistory.org.za/article/fight-against-colonialism-and-imperialism-africa>

² Heath and Norman, 2004:256

of public assets to private owners, the simple cessation of government programs, the contracting out of services formerly provided by state organizations to private producers, and the entry by private producers into markets that were formerly public monopolies (Goodman & Loveman 1991; Ogwezzzy & Bello 2013; Obinger, Schmitt & Zohlnhöfe 2014). Under the Public Enterprises (Privatization) Act, privatization was defined as the transferring to the private sector of part or the whole of the equity or other interest held by the Government, directly or indirectly, in a public enterprise.³

In many developing countries, apart from the general fact that several of the SOEs were generally inefficient, poorly managed and operated at substantial deficits the period between 1970 to 1990 was dominated by the growing dominance of neo-liberalism as a model for economic development (Jauch, 2002). The neo-liberal ideology is driven by the belief in the "free market" as the best regulator and engine of economic growth while the state's developmental role in the economy is to be reduced (Chirwa 2002; Ogwezzzy & Bello, 2013).

Further the period between 1980 and 1990 saw most developing countries in Africa adopting privatization as part of the structural adjustment programs (SAPs) introduced by international Financial Institutions (IFIs). The SAPs were meant to "assist" countries that were going through some economic hardship. The World Bank and International Monetary Fund (IMF) offered loans to these countries, and in return for these loans, African countries were required to implement neo-liberal economic policies, which included privatization of public enterprises (Magalasi, 2008; Wolff, 2014).

³ Section 2 PEPA

Malawi in the said period between 1980 and 1990 was in the process of implementing the SAPs. (Cammack, 2004) Thus as the conditionalities⁴ for the Structural Adjustment Loans (SALs) were being implemented and the winds of democracy were blowing change was inevitable. According to Mawindo,⁵ following the change of Government in 1994, Malawi under the first democratic government led by the United Democratic Front Government (UDF) proceeded to adopt a neo-liberal political ideology under which government was only too ready to implement (if not to experiment with) privatization.

The process of privatization has been espoused as an effective way of bringing about fundamental structural change by formalizing and establishing property rights, which directly create strong individual incentives (Filipovic, 2005). It has been stated by (Filipovic, 2005) that a free market economy largely depends on well-defined property rights in which people make individual decisions in their own interests. In Malawi the privatization programme was intended to achieve four broad objectives, namely, to foster increased efficiency in the economy; to increase competition and reduce monopoly in the economy; to promote participation by the Malawian public in enterprises and finally to raise revenue for the Government.⁶

Even though privatization has received positive theoretical economic assessments, it has also attracted a lot of critics who have expressed strong reservations about its fairness and efficiency (Chirwa, 2002). The critics have also at times questioned the impact of privatization. (Chirwa, 2002; Magalasi, 2008). Some of the specific

⁴ The requirements placed on the usage or distribution of money lent

⁵ Forbes Global Magazine, October 30th 2000 Issue. Accessed at <http://www.winne.com/malawi/to16interv.html#top> on 7 November 2013 at 19:40 hrs

⁶ Section 3(1) PEPA

arguments are that in the first place privatization causes social dislocation. Secondly, privatization leads to layoffs and a worsening in labour conditions, in the short term in the divested firms and in the long run in the economy at large (Magalasi, 2008). Thirdly, it has been argued that the bulk of the benefits accrue to a privileged few – shareholders, managers, foreign or domestic investors, and those connected to the political elite in spite of the costs being borne by many, particularly tax payers, consumers, and workers (Magalasi, 2008). Thus the overall citizen welfare benefits achieved by privatization are not very clear.

1.1 Problem Statement

In Malawi the legal framework for privatization is contained in the Public Private Partnership Act (PPPA) which repealed the Public Enterprises (Privatization) Act (PEPA)⁷ in 2013. The organisation responsible for privatization is the Public-Private Partnership Commission, the successor to the Privatization Commission which had had that responsibility under the PEPA. As had been the case under PEPA, the legal framework in PPPA is predicated on the premise of privatization or divestiture being a technical legal process that is driven exclusively for economic and financial welfare of the nation. However, inherent in the legal framework governing privatization is the structure of the corporation with the Government as the owners (shareholder/ primary stakeholders) and the citizens as the secondary stakeholders. In the set-up, the Public Private Partnership Commission- as was the case with its predecessor, the Privatization Commission (PC)- is the agent/manager. Under the PPPA the Public-Private Partnership Commission is answerable primarily to the

⁷S. 77 of PPPA

Minister of Finance and ultimately to the Cabinet. This had also been the case under the PEPA.

According to the 2006 German Government Country Report on Malawi the privatization program was interrupted in 2001, due to its negative effect on rent seeking and patronage opportunities. The program was restarted, but progress has been slow.⁸ The research investigates whether the structure of the corporation in PPPA has improved on the PEPA with respect to provision for the principles of corporate governance that should ideally govern the relationship between owners and managers as well as other important stakeholders such as employees and the general public. The particular focus of the investigation will be on whether the PPPA has improved on the PEPA in relation to the provision for corporate governance principles that protect the public interest in the privatization of SOEs.

1.2 Research Question(s)

The main research question guiding the study is whether the PPPA has improved on its predecessor, the PEPA, with respect to the protection of the public interest in the privatization or divestiture of state-owned corporations in Malawi.

The main question will be answered incrementally through the following specific questions:

- What legal regime regulated privatization of SOEs in Malawi prior to the enactment of the PPPA? What legal regime currently regulates the privatization of SOEs?

⁸ Shaping Change: Strategies of Transformation and Development accessed at <http://bti2006.bertelsmann-transformation-index.de/72.0.html?L=1>

- What corporate governance principles for safeguarding the public interest in the privatization of SOEs were provided for by the PEPA?
- What corporate governance principles for safeguarding the public interest in the privatization of SOEs are provided for by the PPPA?
- Do the corporate governance principles provided for in the PPPA provide for better protection of the public interest in the privatization of SOEs than was done by those provided for under PEPA?

The research questions will be answered by examining the privatization of David Whitehead and Sons Limited under PEPA and the Malawi Savings Bank under the PPPA. This will entail contextualizing the specific research questions and investigating whether the public interest was better protected in the privatization of MSB under the PPPA than in the privatization of David Whitehead and Sons under the PEPA.

1.3 Justification and Significance of the Study

The overarching development policy framework for Malawi identifies the private sector as the key to economic growth⁹. It follows therefore that understanding of the factors that affect privatization in Malawi is very important. One of these factors is the legal framework which must necessarily include the corporate governance structure of the PPPC or its predecessor the PC. There have however been few studies of the legal framework that governs privatization in Malawi. The current research intends to interrogate that legal framework and will as such contribute to the general

⁹ MGDS - Malawi Growth and development Strategy MGDS II 2011-2016 accessed at <http://www.eisourcebook.org/cms/February%202016/Malawi-Growth-and-Development-Strategy-MGDS-II%202011-2016.pdf>

understanding of corporate governance as a branch of commercial law. The study compares the legal frameworks embodied in the PEPA and its successor, the PPPA with respect to their upholding of corporate governance principles which protect the public interest in privatization. The research will investigate whether the decisions to privatize and, in some instances, the selection of SPEs for privatization, while conforming with the legal framework generally, are made on sound economic considerations, taking into account the public interest, including the interests and welfare of the employees. The research will add to a general understanding of the law, the positioning of public interest in the legal framework and the jurisprudence of corporate governance.

1.4 Hypothesis

The hypothesis of this dissertation is that the legal regime for privatization in Malawi as contained in the PPPA has not improved on the PEPA in terms of inclusion or facilitation of the application of corporate governance for safeguarding the public interest in the privatization of SOEs.

1.5 Methodology

The research employs both exploratory and descriptive approaches to uncover if non adherence to corporate governance principles undermines public interest in privatization. The analysis of the David Whitehead privatization and the MSB privatization case studies findings provides the basis for answering the sub question on the relevance of corporate governance in safeguarding public interest during the privatization process.

The research will utilise a qualitative methodology of research. Library research and field research were utilised as methods of research. The Library research involved review of secondary data compiled by the Privatization Commission, review of the Annual Returns of DWS at Registrar of Companies, review of the Gondwe Commission of Enquiry Report, a review of the Financial Statements of the DWS in the period immediately preceding privatization being undertaken. An analysis of newspaper articles and various press interviews at the material time were also reviewed.

Field Research involved personal interviews using a detailed schedule of open and closed questions with the Executive Director of the Privatization Commission. The interview was intended not to establish the veracity of the content of the interviews in a quantitative fashion but rather as a key performance indicator to provide context of and in depth understanding of the context of privatization. It was hoped that the interview would thus provide both background and context of how privatization is conducted generally and more specifically how the privatizations of DWS and MSB were conducted

The use of these case studies were viewed as essential in bringing out a clearer understanding of the various considerations underpinning privatization. As (O’Leary, 2004) and (Yin 2013) have stated, a case study offers an in-depth understanding of phenomenon and could often ‘bring new understandings to the fore.’¹⁰

¹⁰ (Yin, 2013, P. 7)

The purpose of the comparative analysis of the two case studies in this research was intended to compare how the legal frameworks obtaining in PEPA and PPPA respectively was/is applied in reality. The case studies have enabled the research to probe deeply into how in the privatization process the Privatization Commission worked and how differently does the PPPC and Management work. The research examined the role of the Minister responsible for privatization, namely the Minister of Finance and the role, if any, of the Cabinet. The research compares the results of the literature review with the results of the case study.

The researcher is only too aware of criticisms that have been levelled against the case study method of research. The main criticism has been the result of making generalisations based on the result of a case study (Alderman et al, 1977; Bell, 2005; Denzin and Lincoln, 2011). It could be argued that selecting the privatization of DWS and MSB only and drawing lessons from them is not representative of what happens in privatization generally as most privatizations in Malawi have gone ahead without the spectacle that accompanied the privatization of DWS and MSB. That argument has merits. However, other than draw generalisations from the case studies, this research is intended to find out if corporate governance gaps existed in PEPA. It is intended to find out in the event that corporate governance gaps existed if these gaps may have been used, consciously or unconsciously to the detriment of the public interest in the case of DWS. The case study of MSB interrogates whether by repealing PEPA and enacting the PPPA the corporate gaps, if any, that existed in PEPA were eliminated. The research makes a meaningful comparison between the legal framework in PEPA and its practical application in the case of DWS and the legal framework in PPPA and its practical application in the case of MSB. The

research thus adds more knowledge to the discipline of corporate governance and the general body of commercial law.

1.6 Conclusion

The foregoing discussion has shown that the research intends to investigate the legal framework as was contained in PEPA and the legal framework now obtaining in PPPA using qualitative research methodology. The research is intended to investigate if there were corporate governance gaps in PEPA. In the event that gaps are found to have existed in PEPA the research will inquire whether the repeal of PEPA and the enactment of PPPA addressed such corporate governance gaps? If it is established that corporate governance gaps exist even in PPPA the research inquires whether such gaps are significant so as to lead to the public interest being ignored in the implementation of privatization. The qualitative research methodology has been adopted and library and field research was used as methods. In respect of the field research an interview with a key informant was utilized. The case studies of DWS under PEPA and MSB under PPPA was conducted for in-depth investigation of the implementation of the legal framework in reality.

CHAPTER 2

CONCEPTUAL AND THEORETICAL FRAMEWORK

This chapter outlines the conceptual and theoretical framework of the study. It starts with the definition of corporate governance. It traces the development of the concept of corporate governance from the definition emanating from the theory of the firm to the modern day concepts of such as Stakeholder theory. The discussion then proceeds to define the concepts surrounding privatization and public- private partnerships. The discussion then defines the concept of public interest as contained in the Constitution and other authorities. Proceeding onwards it makes the connection between privatization, public- private partnership and corporate governance. The chapter concludes by drawing linkages between the two concepts and arguing that the concepts are interlinked and excluding corporate governance from the legal framework dealing with either privatization or public- private in essence excludes essential oversight necessary to safeguard public interest in privatization and private –public partnerships.

2.1 Corporate Governance

Ever since the publication of the *Modern Corporation and Private Property* (Berle and Means, 1932), the agency problem has been identified to be at the centre of corporate governance. The agency problem concerns itself with the separation of ownership from control. The root of the agency problem is that even though it is the

principal (Owner) who has resources and who imposes structures on the agents (Managers) it is the agents who have effective authority of the corporation.

From this emanate many issues relating to efficient control of the assets of corporations in the interest of all company's stakeholders. The agency problem of corporate governance is stated by (La Porta *et. al.*, 2000: as the relationship between "controlling shareholders and outside investors,"¹¹ instead of the conventional (Berle and Means, 1932) conflict involving "outside investors and managers". On the other hand (Branston, Cowling and Sugden, 2006) state that the overall conclusions that are reached are broadly the same: *de facto* control of the corporation rests between a set of (large) shareholders and the company's senior managers/board.

Earlier (Jensen and Meckling, 1976) had stated that although the separation of ownership and control may provide the opportunities for managerial divergent behaviours from maximising shareholders' value, the markets – particularly the capital market, the managerial labour market and the market for corporate control – provide the most effective restraints on managerial discretion¹²

Corporate governance has therefore been defined in some instances simply as the prevention of theft (Nganga *et al.*, 2003). That definition is too simplistic as the issues at the centre of corporate governance are not merely related to prevention of theft. An expanded definition was given by . (Shleifer and Vishny, 1994) stating that corporate governance deals with the ways suppliers of finance to corporations assure

¹¹ (La Porta *et. al.*, 2000:15)

¹² See LetzaSun and Kirkbride, 'Shareholding Versus Stake holding: A critical review of corporate governance' [2004] Corporate Governance

themselves of getting a return on their investment, how they make sure that managers do not steal capital or invest in bad projects. They state in other words that, corporate governance is “the mechanism through which outside investors are protected against expropriation by insiders” (Shleifer and Vishny, 1994). Insiders, according to this definition, include managers, major shareholders (individuals, other firms, family interests or governments) as well as large creditors such as banks. Outsiders include equity investors, providers of debt and minority shareholders.

Expanding the definition even more, (Oman,2001) defines corporate governance of private and public institutions as including laws, regulations and accepted business practice, which in a market economy govern the relationship between corporate managers and entrepreneurs (corporate insiders) on the one hand, and those who invest resources in corporations, on the other hand.¹³

The Eastern, Central and Southern African Federation of Accountants (ECSAFA) defines corporate governance as the means by which an organisation is directed and controlled. It states that in broad terms corporate governance is to be understood as the processes by which organisations are directed, controlled and held accountable.¹⁴

Despite the diversity of the definitions, the issue at the centre of corporate governance is the relationship between insiders meaning those that have a management role in the firm (at either management or board levels) and outsiders meaning those that have an interest in the firm but do not have any management roles.

¹³"An Overview of Corporate Governance and Accountability in Southern Africa ECSAFA'

¹⁴Guidelines on the Good Governance of Parastatal Organisations: An ECSAFA Perspective

In this research the ECSAFA definition is the preferred definition of corporate governance as it encompasses the authority, accountability, stewardship, leadership, direction and control exercised in corporations. In short corporate governance should be understood as dealing with who governs the corporation and in whose interest.

2.2 Corporate Governance in SOEs

In the previous section corporate governance was examined generally. However, parastatal organisations or SOEs are in a special category in that they are established with financial resources from tax-payers. This means that the main stakeholders in state-owned enterprises are members of the public, whose taxes have been invested in these corporations. It was observed earlier on that many SOEs are and were created under state ownership out of a desire on the part of governments to have enterprises that served the broader public interest.¹⁵ It follows therefore that one of the major problems of governance in public enterprises is that of plurality of objectives. Unlike private enterprises who work only for profit, objectives for the public enterprises may be diverse ranging from commercial to social welfare, and from efficiency and economy to equity. (Khan and Imran, 2012). The issue to grapple with therefore becomes how and to what extent are the members of the public able to exercise control over Managers of the SOEs.

It has been stated by (Khan 2006) that a public official is an individual who would optimise his benefits, and his benefits are maximised in terms of pay, power and prestige when his organization grows and he maximises his “budget” Following the same logic, (Khan, 2006) argues that all public organizations compete for more

¹⁵ Paragraph 1.4 above

“funding, staffing, policy ‘territory’ or other resources” and unless an official has to pay the cost of adding more personnel, he will be motivated to increase the size of his organization indefinitely. Khan states further that "Niskanen (1973) finds public officials as inherent maximisers yearning to be at the top of the “virility index” – more resources they grab, better their performance on the index. He equates this behaviour as logical, and analogous to that of the owners and managers of private firms."¹⁶ (Heath and Norman, 2004) have stated that the idea that agency problems in the public sector are more acute than in the private is widely accepted. They state "in some cases this is due to the peculiar character of the state as an owner. They give as an example the fact that the public sector cannot give its managers an ownership stake in the operation that they run. They also state that the top end of the pay scale is also significantly lower than in the private sector, for a variety of reasons, and this may make it difficult for SOEs to attract or retain top managers. They again note the well-known problem of the “soft-budget constraint” meaning that if the managers of a privately-owned firm cannot keep it in the black, shareholders will eventually withdraw their investment, regardless of the social consequences and because of this, private owners are able to issue much more credible threats to their managers. Politicians, on the other hand, would never allow a major public corporation to go bankrupt, and the managers know it. Thus public-sector managers have much less fear of losing money. It has been stated by (Heath and Norman 2004) that "it is known that public sector managers sometimes intentionally run deficits in order to secure budget increases"¹⁷. They state that the "most widely accepted explanation for losses generally experienced in SOEs is that the structure of public enterprise makes it

¹⁶ accessed at https://mpra.ub.uni-muenchen.de/13443/2/MPRA_paper_13443.pdf

¹⁷ Joseph Heath & Wayne Norman “Stakeholder Theory, Corporate Governance and Public Management: What can the History of State-Run Enterprises Teach us in the Post-Enron era?”, (2004) *Journal of Business Ethics* 53: 247–265 p. 257)

extremely difficult for the state to exercise effective discipline over its managers"¹⁸. It will thus be noted that unless constrained by corporate governance principles managers of SOEs will appear to act in the best interest of the public when in reality they are thinking of pleasing the people that appointed them and rewarding themselves. It will again be noted as has been stated by (Heath & Norman, 2004)¹⁹ that although some of the agency problems are intrinsic features of public ownership others were produced by the specific character of the “social responsibility” mandate given to SOEs in the period from independence up to the late 1980s. It was the latter that Malawi in line with neo liberalism principles intended privatization to correct.

2.3 The Stakeholder Theory of Corporate Governance

Whilst in the Berle and Means definition of owners and managers, the managers are to manage the firm in the interest of the owners, the stakeholder theory is to the effect that a corporation should not be managed only in the interest of the shareholders or the stockholders but other interests of other interest groups such as employees, suppliers and the general public should be taken into account. According to (Keay, 2012) Stakeholders are inherently valuable to the corporation and should be treated as such in the management of the affairs of the corporation. The normative explanation of the Stakeholder theory is on a moral basis which holds that not only shareholders but groups that are classified as stakeholders should be seen and be ktreated as “ends” and not “means (Keay, 2012).”

A distinction has been made above between private corporations and SOE. It was noted that as SOEs are funded by taxes of the general public SOEs are in a special

¹⁹ Ditto

¹⁹ Supra

category. As such members of the general public are not secondary stakeholders but primary stakeholders. The Government and or Board of a SOE are therefore in a fiduciary relationship with respect to the citizens and as such ought to act in the best interest of the Citizens in the management of the affairs of the SOE and in making the decision to privatise any SOE.

2.4 Privatization

Privatization of state-owned enterprises (SOEs) has been defined generally as the transfer of ownership from the public to the private sector²⁰. Under the PPPA divestiture is defined as the disposing of the whole or part of the assets and shares of a state-owned enterprise.²¹ Thus in this research privatization or divestiture are used together or interchangeably.

Privatization has been a major policy instrument in private enterprise development in developed and developing countries in the past two decades.

We noted above that apart from the neo-liberal policies aimed at making the private sector an engine for growth the imperative for privatization stems from inefficiency, poor management and low productivity generally associated with SOEs. The result of these inefficiencies are, consequently, reflected in poor quality of goods and services and mounting losses and rising debts. This is because as we noted state ownership creates the wrong incentives. SOEs are controlled by managers who have no rights to the cash flow generated by the business. Too often, those managers are motivated not

²⁰Section 2 PEPA

²¹Section 2 PPPA

by noble causes but may have socially harmful objectives, such as political favoritism and corruption.

Privatization according to neo liberal theories can lead to better alignment of corporate decision-making and allocation of cash flows, through managerial and technological innovations. On the other hand privatization has been frowned upon because of its social consequences. It is associated with rising unemployment and social dislocation, which the creation of SOEs in the first place was intended to address. Privatization of SOEs without the appropriate regulatory restrictions may create unfair profit opportunities and overall welfare losses²².

Many developing countries and African countries have followed the path of privatization of the state-owned enterprises (Adam et al., 1992; Cook and Kirkpatrick, 1995; White and Bhatia, 1998). The pull and push factors leading to privatization differ across countries (see White and Bhatia, 1998). Nonetheless, in most African countries, privatization of state-owned enterprises has been associated with World Bank and International Monetary Fund (IMF) sponsored structural adjustment programs (Adam, 1994; White and Bhatia, 1998).

It has been stated by (Magalasi: 2008) that "the government of Malawi, from the mid-1960's to the early 1980s, followed a policy of seeking comprehensive ownership of the means of production and also centralized management of the economy. In a way, this aimed to give the economy a state driven boost that was anticipated to

²²See Mitchell, Arthur "Privatization and Reform of the Financial Sector in the People's Republic of China" [2005] ADBLP Res 24 (5 December 2005)

trickle down to the poor masses, hitherto marginalized during colonial rule” (Magalasi, 2008).

According to (Magalasi, 2008) the Agricultural Development Marketing Corporation (ADMARC,) a replacement of Farmers Marketing Board (FMB), was established essentially for agricultural activities to safeguard and level the playing field for peasant farmers. However apart from agricultural marketing activities, ADMARC invested in activities that were not its core business such as heavy investments in n equities and loans in various enterprises and was also directly involved in estate agriculture. According to (Magalasi, 2008) by the mid-1980s, ADMARC had equity investments in 34 commercial enterprises and owned numerous estates. Until 2002 ADMARC also used to run various subsidiaries (e.g. David Whitehead and Sons a cotton ginning company, Stage Coach a bus company and Cold Storage many of which were loss making. In 2002, the Ministry of Finance assumed control over its four largest loss-making subsidiaries, in preparation for public sale, and three of the companies have since been privatized (Magalasi, 2008).

The program of privatization in Malawi started in the late 1980s mainly as a result of SAPS and thus was not a new phenomenon. In the MCP Government under Dr Banda there had been a fair amount of divestiture that was aimed at ridding MDC (Malawi Development Corporation) and ADMARC (Agricultural Development Marketing Corporation) of some of the investments which they had acquired over the years. In the late 1980s, with the support of the World Bank and USAID, a program was put together to divest some investments owned by ADMARC. (Magalasi 2008) The major change coming with the enactment of PEPA was the development of a

fully-fledged privatization program with this responsibility is being implemented by the Privatization Commission.

The Privatization Act and Privatization Policy came into being in 1996, and paved the way for the establishment of the Privatization Commission. This second phase of the restructuring program had the major objective of increasing the size and diversity of the private sector while reducing public budgetary and administrative burden. According to the provisions of PEPA and PPPA, the major objectives of the Malawi privatization program are stipulated as: to foster increased efficiency in the economy; to increase competition and reduce monopoly; to promote participation by the Malawi public in enterprises; and to raise revenue for the government.²³

Accordingly, by realizing these objectives, the Government was expected to create an economic environment conducive to private sector development and also free public resources for investment in infrastructure and social programmes.

It has been stated by (Magalasi,2008) that "the first three objectives, have direct welfare implications for the society, in terms of availability of goods and services and their quality, their competitive pricing, and equity in the distribution of income generating assets. The last objective probably not only covers the proceeds of privatization but also expenditure savings from reduced subventions as well as revenue generated from profitable and tax paying enterprises" ²⁴

²³Section 3 PEPA and/or S. 3(2) of PPPA

²⁴ (Magalasi, 2008).

The institutional arrangement places the Public-Private Partnership Commission formerly the Privatization Commission (PC) with the sole authority in Malawi to implement the privatization of the direct or indirect government ownership of any public enterprise. The Commission's functions include, but are not limited to, the planning, management implementation, and control of the divestiture of public enterprises in Malawi.²⁵ It is also the duty of the Commission to report to the Cabinet the details of the sale of each public enterprise.²⁶

Membership of the Commission under PEPA included ex-officio representatives of Government, representatives nominated by each political party represented in the National Assembly, a representative nominated by the Malawi Congress of Trade Unions, and members representing professional and commercial business interest. Under the PPPA the Commission consists of a Chairman and-(a) four other members appointed by the President by notice published in the *Gazette*, and (b) the following members *ex officio*-(i) the Secretary to the Treasury;(ii) the Solicitor General and Secretary for Justice;(iii) the Principal Secretary responsible for planning and development; and (iv) the Principal Secretary responsible for industry and trade.²⁷

A Secretariat of the Commission no different from that obtaining under PEPA is established comprising a Chief Executive Officer (formerly Executive Director) and subordinate employees. The Chief Executive Officer of the Public-Private Partnership Commission is responsible for the effective administration and implementation of the provisions of the privatization programme.²⁸

²⁵ PEPA section 8(2)/PPPA section 8(4)

²⁶ PPPA section 8(4)(d)

²⁷ PPPA section 5(1)

²⁸ S.16(2) PPPA

(Goodman and Loveman, 1991) have stated that "contrary to the skeptics' assertion that governments won't sell the winners and can't sell the losers, governments sold off many prized assets in the 1980s". Thus in an apparent role reversal according to Magalasi (2008), "the government, not the Commission, devised a Divestiture Sequence Plan. This was essentially a list of 100 SOEs earmarked for privatization". According to Magalasi "The government determines who; the Commission only determines when and how" (Magalasi, 2008)

Pursuant to Section 39 of PEPA, the proceeds of privatization were held in the Privatization Revenue Account for use in "funding the direct costs of the Commission and the Privatization Programme, funding the restructuring public enterprises to be privatized including payment of retrenchment benefits, ..." Under Section 54 of the PPPA proceeds of every sale of state-owned enterprises as the Minister shall determine with the advice of the Commission shall be paid into a fund to be known as the Divestiture Proceeds Account to be established by the Minister responsible for Finance and to be held at the Reserve Bank of Malawi or at such other bank or place as that Minister, on the advice of the Commission, may direct

It will be noted that one of the criticisms that has been raised with regard to privatization is that residual revenues from this one-off exercise, after privatization related expenditures, could also be used in one-off development projects, rather than government recurrent expenditures (B Kaluwa, 2000; Magalasi: 2008). It is interesting to note that the PPPA has not improved on the structure and scheme obtaining under PEPA.

2.5 Public – Private Partnerships

Section 2 of the PPPA defines "public-private partnership" as a contract in which a Contracting Authority partners with a Partner to build, expand, improve, or develop infrastructure or service in which the Contracting Authority and private sector partner contribute one or more of know-how, financial support, facilities, logistical support, operational management, investment or other input required for the successful deployment of a product or service, and for which the private sector partner is compensated in accordance with a pre-agreed plan, typically in relation to the risk assumed and the value of the result to be achieved;

From the definition it will be appreciated that the PPPs occur mainly on occasions when the State retains ownership or control of the services under the PPP. Thus PPPs are loosely joint ventures between the Public and Private sector. As the aim of this study is really concerned with privatization or divestitures of SOE where the whole or part of SOE is disposed of, this research shall not dwell much on PPPs save to the extent that the same relates to privatization or divestiture.

Although the research did not deal with PPPs in *stricto sensu* the research was able to establish that the effect of the PPPA was to expand the role of the Privatization Commission in PEPA. As was observed earlier on that all public organizations compete for more "funding, staffing, policy 'territory' or other resources (Downs, 1967),²⁹ This appears to have been the effect of the enactment of the PPPA. Thus although the objectives of the PPC are stated to be aimed at facilitating the development and implementation of public-private partnership arrangements for

²⁹ (Downs, 1967: 53)

purposes of efficient delivery of infrastructure and services in order to achieve sustainable economic growth and social development,³⁰ it will be noted that the effect of the PPP Act in totality is to increase the “territory” of the commission.

2.6 Public interest

It is not very easy to define public interest. It can best be understood by saying that public interest is that which is not private interest. Despite the vagueness of the term, on occasions public interest has been claimed generally by governments in matters of state secrecy and confidentiality.³¹ According to (Starr: 1988) the public sphere may be conceived of as the open and visible -the sphere of public life, public theater, the public marketplace, public sociability. The public sphere also may be conceived of as that which applies to the whole people or, as we say, the general public or the public at large, in which case the public may consist of an aggregate or a mass who have no direct contact or social relation--the very opposite of a sphere of sociability. Or the public sphere may be conceived specifically as the domain circumscribed by the state, although exactly where to draw the state's boundaries may be difficult indeed.³²

The Economic and Social Research Council of the United Kingdom conducted a research project specifically to look at Public interest as used in legislation and by the courts and has stated the following:

Public interest is a term with a long history in traditional political philosophy.

The idea of transforming the interests of many people into some notion of a common good is of course for many people the central task of the whole political process. Thomas Aquinas maintained the “common good” (*bonum*

³⁰Section 3(1) PPPA

³¹ See <http://www.businessdirectory.com/definition/public-interest.html>

³² Starr op.cit 2

commune) to be the end of government and law, while Aristotle took the idea of the “common interest” (*to koinei sympheron*) as the foundation for his distinction between “right” constitutions, in the common interest, and “wrong” constitutions that were merely in the interests of the rulers. The purpose of government is therefore, within many traditional accounts, to give expression to the public interest. As John Locke puts it, “the peace, safety, and the public good of the people” are the ends of political society, and “the well being of the people shall be the supreme law”. Jean-Jacques Rousseau took the idea of the “common good” (*le bien commun*) to be the object of the general will and purpose of government.³³

In Australia the Law Institute of Victoria submitted that:

This is a phrase commonly used in legislation and one with which courts are familiar. ‘Public interest’ is a broad concept that is flexible enough to respond to the facts and circumstances of any particular case. Given that privacy is fact and context specific, it is appropriate to keep concepts such as ‘public interest’ broad and flexible³⁴

In the Australian case of *Hogan v Hinch*, French CJ stated that when ‘used in a statute, the term [public interest] derives its content from “the subject matter and the scope and purpose” of the enactment in which it appears’³⁵

In this research therefore we use public interest in the sense that we use the term "public" when we speak of public opinion, public health, or the public interest,

³³ Public Interest in UK Courts, *Public Interest, Political Philosophy and the Study of Public Administration*, Accessed at <http://publicinterest.info/> on 8 October 2016 at 20:35

³⁴ Australian Law Reform Commission accessed at <https://www.alrc.gov.au/publications/8-balancing-privacy-other-interests/meaning-public-interest>

³⁵ *Hogan v Hinch* (2011) 243 CLR 506

meaning the opinion, health, or interest of the a significant part of the population be it a class or an individual. Public in this sense means "common," not necessarily governmental.³⁶

(Branston, Cowling and Sugden, 2006:195) state that for an act is private when its consequences are essentially confined to the persons directly engaged in it, but if the consequences extend beyond those directly engaged then 'the act acquires a public capacity'³⁷ He sees the public as those who are 'indirectly and seriously affected for good or for evil' by an act. Drawing on this, Long views the public interest as an evolving consensus among a set of people—a public—regarding the actions of private parties; it is the standard agreed upon by that public and against which those actions can be reasonably assessed. According to him, 'by arriving at some consensus, a moving one, we agree on what is important both for policy and research and the latter becomes a more purposive, disciplined, cooperative endeavour as opposed to a matter of fad, fashion and funding. For public administration and political science, the appropriate standard of evaluation would appear to be the public interest' (Branston, Cowling and Sugden 2006:195)

It has been stated that "it is neither for those unaffected by the activity to determine those objectives, nor for those affected to be excluded from the decision-making. Otherwise exclusive interests would make the decision following their own preferences and despite the wishes of others"³⁸ Furthermore, we cannot predict

³⁶ Starr op.cit 1

³⁷ (Branston, Cowling and Sugden 2006:195, p. 244)

³⁸ K. Gugler & B.B. Yurtoglu, *The Economics of Corporate Governance and Mergers* (Elgar Publishing, 2008), at page 61.

exactly what the democratic outcome would be without the democratic process actually taking place (Branston, Cowling and Sugden, 2006:197)

The researcher therefore agrees with Tsumba that "to understand public interest there is need to create an environment where stakeholders, be they shareholders, citizens or other interested parties are assured that "the goings-on" are not detrimental to their own political and financial interests."³⁹

2.7 Conclusion

(Magalasi, 2008) states that in Malawi, the benefits of privatization mostly exist at company levels. The linkages to the poor and marginalized are weak or absent in some cases. The poor, who are supposed to benefit are getting worst outcomes of privatization, consequently affecting overall development negatively. However, despite all this, privatization is still pushed at the policy level. It seems clear therefore that public interest does not appear to be at the center of the privatization. What appears to be of importance is the desire to make the private sector to be the driver of economic growth. How best that should be done requires further discussion and research.

³⁹ L. Tsumba "Corporate Governance Country Case Experience - Perspectives and Practices: Zimbabwe" Reserve Bank of Zimbabwe. Accessed at <https://pdfs.semanticscholar.org/3142/9f0bc816f49a47933bb9c4f8cd9c67f95604.pdf>

CHAPTER 3

THE LEGAL FRAMEWORK OF PRIVATIZATION IN MALAWI

3.1 Constitutional principles of public interest and privatization

The Malawi Constitution adopted in 1994 establishes a legal regime predicated on principles aimed at transforming the society and promoting the welfare of all sections of the population, particularly those hitherto marginalized. The Constitution is founded upon principles which state, *inter alia*, that all legal and political authority of the State derives from the people of Malawi and shall be exercised in accordance with the Constitution solely “to serve and protect their interests;”⁴⁰ and that all institutions and persons shall observe and uphold the Constitution and the rule of law and no institution or person shall stand above the law.⁴¹ The Constitution also lays down the principles of national policy intended to promote “the welfare and development of the people of Malawi”⁴² that should guide state priorities. One of the principles is stated as intended to achieve a sensible balance between the creation and distribution of wealth through the nurturing of a market economy and long-term investment in health, education, economic and social development programmes.⁴³ To introduce measures which will guarantee accountability, transparency, personal integrity and

⁴⁰ Malawi Constitution S.12 [Emphasis added]

⁴¹ Ibid.

⁴² Malawi Constitution S. 13

⁴³ Malawi Constitution S.13(n)

financial probity and which by virtue of their effectiveness and transparency will strengthen confidence in public institutions.⁴⁴

It is clear therefore that at the centre of the Constitution are the interests of the people, the welfare of the people and the development of the people. All State institutions ought to be run and policies ought to be implemented ideally in the interests of the people or in other words the public interest.

3.2 Comparison of, and analysis of, relevant provisions of PEPA and PPPA

Up to 2010 the law governing privatization in Malawi was contained in PEPA which created the Privatization Commission as the sole authority in Malawi to implement the privatization of the direct or indirect Government ownership of, or interest in, any public enterprise and no other person or other authority had the power to perform such function.⁴⁵ Under the PPPA the PPPC while taking extensive roles vis-a-vis PPPs has retained the role as the sole authority to implement divestiture of direct or indirect in state owned enterprises.⁴⁶ The functions of the Commission under PEPA were to plan, manage, implement and control the privatization of public enterprises in Malawi to ensure that the privatization of each public enterprise carried out was usually transparent to the public at large and that the process was fair and efficient.⁴⁷ Under PPPA the PPPC has the obligation to ensure that the divestiture of each state-owned enterprise is carried out according to the following principles, that is to say, that- (i) each transaction is fully transparent to the public at large; (ii) participation is competitive by making it open to all investors;

⁴⁴ Malawi Constitution S.13(o)

⁴⁵ PEPA S. 8 (1)

⁴⁶ PPPA s. 8(1)

⁴⁷ Ibid

(iii) the process is fair and efficient; (iv) the transaction is such as to reduce concentration of ownership and marketing.⁴⁸

Members of the Commission under PEPA were appointed by the President subject to confirmation by the Public Appointments Committee of Parliament.⁴⁹ Under the PPPA members of the Commission are appointed by the President and there is no requirement for confirmation by the PAC.⁵⁰ Like the scheme under PEPA members of the Commission under PPPA hold office for a period of three years and are eligible for reappointment but may cease to hold office if the member resigns by giving one month notice, in writing to the President; (b) upon the member's death; (c) if the member is absent, without the consent in writing of the Chairman, or without valid excuse, from three consecutive meetings of the Commission of which the member has had notice; (d) if the member is convicted of a criminal offence without the option of a fine; (e) if the member becomes an undischarged bankrupt; or (f) if the member participates, directly or indirectly, in a public-private partnership arrangement or acquires shares or other interests in a state-owned enterprise in contravention of PPPA.⁵¹ Under PEPA a member could cease to hold office if the President so directed.⁵² Under PPPA that ground has been removed and replaced with one where the member is convicted of a criminal offence without the option of a fine.⁵³ Although the PPPC just as the Privatization Commission under PEPA is stated to be the sole authority in Malawi to implement divestiture of SOEs it is required to prepare the long term divestiture sequence plan and submit such plan to the Cabinet

⁴⁸PPPA s. 8(4)(d)

⁴⁹PEPA s. 5(1)

⁵⁰PPP s. 5 (1)

⁵¹PPPA s. 9

⁵²PEPA s 6(1)(d)

⁵³PPPA s. 9(d)

for approval⁵⁴ to report the sale of each public enterprise to the Cabinet, specifying the method of sale used and the reasons why such method was considered appropriate, the proceeds realised and other particulars;⁵⁵ Any recommendation or report by the Commission to the Cabinet is submitted through the Minister.⁵⁶

Whilst the Commission has discretion at any time and for any period to invite any person, the Minister may in like manner nominate any officer in the public service to attend any meeting of the Commission or of any of its committees and take part in the deliberations of the meeting.⁵⁷ Under PEPA the Secretariat of the Commission was headed by an Executive Director who was appointed on terms approved by the Minister but such person or officer was not entitled to vote at the meeting.⁵⁸ Under the PPPA the Secretariat of the Commission is headed by a Chief Executive Officer appointed on terms approved by the Minister who similarly is not entitled to vote at the meeting of the Commission.⁵⁹

In any agreement for the sale of a public enterprise, the parties may agree that the Minister responsible for finance may retain or at any time after the date of the agreement acquire, a share in the privatized enterprise, which share shall confer special rights to enable the Government in the national interest to intervene in the operations of the enterprise where such intervention is necessitated by the specific actions or undertaking of the enterprise.⁶⁰ The final sales agreement to transfer shares is signed by the minister Responsible for finance, where the shares sold were directly

⁵⁴PPPA s. 8(4) and PEPA s. 8(2)

⁵⁵PPPA s. 8(4)(d) and PEPA s. 8(1)(f)

⁵⁶PEPA s. 8(2) PPPA s. 8(8)

⁵⁷PEPA s 13 and PPPA s.14

⁵⁸PEPAs. 15

⁵⁹PPPA s. 16

⁶⁰PEPA s. 21 and PPPA s.33

owned by the Government⁶¹. Under PEPA the proceeds of every sale of public enterprises as the Minister shall determine with the advice of the Commission were to be paid into a fund to be known as the Privatization Revenue Account. The funds held on the Privatization Revenue Account with the prior approval of the Minister responsible for Finance, may be used for funding the Commission; funding the cost of privatization under this Act; funding the restructuring of public enterprise to be privatized; supporting payments for retrenchment, redundancy or other form of lay off resulting from privatization processes and funding of any project within the Government development plans.⁶²

Under the PPPA there is a similar provision which except for reference to the funding of cost of PPP development and replacing the Privatization Revenue Account with the Divestiture Proceeds Account provides that: “Such amount of the proceeds of every sale of state-owned enterprises as the Minister shall determine with the advice of the Commission shall be paid into a fund to be known as the Divestiture Proceeds Account to be established by the Minister responsible for Finance and to be held at the Reserve Bank of Malawi or at such other bank or place as that Minister, on the advice of the Commission, may direct”

"(2) With the prior approval of the Minister responsible for Finance, the funds held on the Divestiture Proceeds Account may be-used for-(a) funding the Commission; (b) funding the cost of divestiture under this Act;(c) funding the cost of public-private partnership development;(d) funding the restructuring of a public enterprise to be divested or commercialized;(e) supporting payments for retrenchment, redundancy or other form of lay-off resulting from divestiture processes under this Act;

⁶¹ PPPA s. 47 and PEPA s.36

⁶² Section 39

(f) funding of any project within the Government development plans."

With regard to reporting as soon as practicable, but not later than six months after the expiry of each financial year, the Commission shall submit to the Minister a report concerning its activities during that financial year.⁶³ The report shall be in such form as the Minister shall approve and shall include information on the financial affairs of the Commission and there shall be appended to the report an audited balance sheet; an audited statement of income and expenditure; and such other information as the Commission may consider appropriate or as the Minister may direct.⁶⁴ The Minister is required to lay the report before the National Assembly during the meeting of the National Assembly next following receipt by him of the report⁶⁵

The Commission was given power to inquire into the sale of any public enterprise effected at any time before the commencement of PEPA to determine whether or not the sale was done in the best public interest. It followed that where the Commission was of the opinion that such sale was not done in the best public interest it was given power to renegotiate the purchase of the public enterprise in question with the new owner thereof, following, as far as possible the principles and procedures outlined PEPA.⁶⁶

⁶³ PPPA s. 62(1) PEPA s.43(1)

⁶⁴ PPPA s. 62(2) PEPA s.43 (2)

⁶⁵ PPPA s. 62(3) PEPA s.43 (3)

⁶⁶ Section 50 (2) and (3) PEPA

3.3 Judicial discourse on public interest

In Malawi there are no cases addressing the power relations that exist in the appointment of members of various boards or commissioners of statutory corporations including the PPPC or before it the Privatization Commission. There are also no judgments concerning the definition, interpretation, or application of the principle of public interest. However, in the case of *Mwapasa and another v. Standard Bank and Another* Misc. Civil Cause Number 110 of 2003 Justice Mwaungulu stated that it did not matter that under the Privatization Act (PEPA) all government interests vest in the Privatization Commission. He observed that nothing in the Privatization Act suggested different treatment from the Companies Act for Government as a shareholder in a company under the Companies Act. In that case he stated that Government acted through ADMARC Investment Holdings Ltd.

In the judgment of the Supreme court in the case of *Civil Liberties Committee v Ministry of Justice and Another* MSC Civil Appeal No. 12 of 1999 Tambala JA stated that " Courts exist to conduct serious business. They deal with real live issues affecting parties to an action." He then proceeded to say the following:

In the field of public law the right to commence an action may similarly depend upon unlawful conduct or abuse of power on the part of a public authority which adversely affects the plaintiff's right, interest or legitimate expectation. Thus a plaintiff may allege that his house was pulled down or his farm was taken away to give way for the construction of a road. However, a breach of public duty or a failure to properly exercise statutory powers may adversely affect the general public. In that situation "a plaintiff would have locus standing if he can show that he has suffered damage of a special kind or greater degree than that suffered by the rest of the members of the public".

In that case the court held that Malawian law does not provide for public interest litigation. What is unclear is how the courts would treat a case where what was being said was that the conduct of a particular entity caused suffering to or affected all the members of the public

In *Kamuzu Banda and the Foundation for the Integrity of Creation, Justice and Peace*,⁶⁷ the court said that if the former president had been “voiceless, defenseless and weak” the foundation could, in the public interest, have undertaken the case on his behalf. However, the court did not agree that Banda was voiceless and defenseless and found that to permit public interest litigation under the circumstances would encourage the creation of “a class of person popularly referred to as ‘a private Attorney General.’”⁶⁸

Generally, therefore the courts in Malawi appear to take an interpretation of the constitution that seeks to give effect to the intention of the legislature rather than constitutional norms. It was said by a judge in the case of *Human Rights Commission v. Attorney General*: that “if the language used by the law giver is ignored in favor of a general resort to ‘values’ the result is not interpretation but divination.”⁶⁹

3.4 Public interest in the legal framework of privatization

What comes out clearly from a review of the Constitution and PEPA is that the public interest should be at the centre of privatization. Apart from the constitutional provisions contained in Sections 12 and 13 of the Constitution if any doubts were entertained Section 50(2) and (3) of PEPA make that clear in reverse analogy. The section provides as follows:

⁶⁷Misc Appl. 89 of 1994

⁶⁸See For further discussion Gloppen and Kanyongolo(2007) Courts and the Poor in Malawi

⁶⁹Ditto

The Commission shall have power to inquire into the sale of any public enterprise effected at any time before the commencement of this Act to determine whether or not the sale was done “in the best public interest”.

(3) Where the Commission is of the opinion that the sale referred to in subsection (2) was not done “in the best of public interest”, the commission shall have the power to renegotiate the purchase of the public enterprise in question with the new owner thereof, following, as far as possible, the principles and procedures outlined in this Act⁷⁰.

It follows therefore that if the Privatization Commission was given powers to inquire into the sale of any public enterprise effected at any time before the commencement of PEPA to determine whether or not the sale was done in the best of public interest it must follow that PEPA was intended to ensure that privatization in compliance with it would be conducted in the public interest.

Our review of the legal framework obtaining in PEPA and PPPA however shows that the law favours the government and the Cabinet. It is therefore clear that weak as that framework is, corporate governance standards can be flouted with the cooperation or at the behest of politicians. The legal framework also demonstrates the weakness of the Privatization Commission or the PPPC in the management and supervision of the privatization of SOEs. This is because the Commission is appointed by the President and answers to the Cabinet in almost all respects. Thus it is not difficult to see that PPPC will in most if not all instances tow the Cabinet and government line and not that of the public interest. Indeed in the case of *Evelyn Mwapasa and another v. Stanbic Mwaungulu J* observed that:

⁷⁰ Emphasis added

The Privatization Commission clearly acts as agent of Government as shareholder in a company. The rights of the Privatization Commission on behalf of the shareholder are not any better than the shareholder'

There is no doubt that in the view of the court the PC was the agent of the Government. It did not appear necessary or important it appears, for the court to have gone a step further to look at the interests of the employees let alone the general public.

3.5 Conclusion

It will be noted that in the case of the legal framework obtaining in PPPA as in PEPA before it and the case authorities the situation in Malawi is far from optimal. The law appears to give to the PPP Commission on one hand the sole authority in Malawi to implement privatization and on the other hand to make the PPP Commission answerable to Cabinet for approval of divestiture or privatization policy guidelines and to implement the privatization programme in accordance with the policy guidelines approved by the Cabinet.

CHAPTER 4

THE PRIVATIZATION OF DAVID WHITEHEAD AND MSB

4.1 Background to the privatization of DWS and MSB

This Chapter examines the privatization of David Whitehead and Sons Limited under PEPA and the Malawi Savings Bank under the PPPA. It examines the background to the Privatization of the two SOEs. It explores the arguments and justification made at the material time for and against the privatization of each of the two entities. It further examines the general public perceptions and reactions of the management, employees and members of the public to the privatizations. The chapter contextualizes the research questions and investigates whether the public interest was better protected in the privatization of MSB under the PPPA than in the privatization of David Whitehead and Sons under the PEPA.

4.1.1 DWS Privatization

DWS was a private limited company incorporated in Malawi under the Malawi Companies Act 1984. DWS commenced operations in 1967 as a 51% subsidiary of Lonrho (Mw) limited from large, commission- built, factory premises in Blantyre's heavy industrial site. It was involved in the manufacturing and selling of cloth and cloth products. For many years DWS prospered and contributed significantly to Malawi's GDP. Production peaked in the early nineties as approximately 33 million meters of dyed and printed fabric plus moderate quantities of yarn and twine for the domestic market. Within a few years, radical market changes began to occur. DWS

failed to respond fully to these radical changes, thus productions fell off rapidly and profits and cash flow shrank.⁷¹ The government of Malawi, which initially had a minority shareholding then proceeded to acquire through ADMARC Investment Holding Limited, holds 100% of the issued share capital.⁷²

In an interview the Executive Director of PC as he then was, stated that Government issued instructions to sell David Whiteheads in 2002 when it was very apparent that failing a sale, the only other viable option was factory closure. He stated that the objectives of DWS Privatization were many but some of the principal ones included, to alleviate government from the burden of financially supporting DWSM; the selection of an investor with sufficient technical and financial expertise to invest in the much needed spares and machinery; backward linkages to smallholder cotton growing; forward linkages to the production of quality with material in light of AGOA.

The Executive Director of PC further stated that in August 2002 the privatization commission recruited Economic Resources limited, in Association Belmont Consultants of the UK, to identify a strategic equity partner for DWS. Following that international tender, a bid from Mapeto wholesalers, of Malawi, in association with Jimtex Group of companies of India was adjudged the most responsive and declared preferred bidder. Following conclusion of negotiations the commission signed an investment agreement with the preferred bidder's consortium.

⁷¹ Interview Meya Chinula/Jimmy Lipunga on 12 June 2013

⁷² Ditto

The Executive Director of PC stated further that the consortium established a joint venture company called Mapeto (DWSM) Ltd owned 60% by Mapeto Wholesalers and 40% by Jimtex. The joint venture acquired the core assets of DWS (Properties, Machinery) and equipment stocks and intellectual property rights) at a purchase price of US\$ 786,289. Mapeto (DWSM) limited acquired the assets free of accumulated corporate commercial liability, as well as free of accumulated Government and shareholders indebtedness. The Jimtex Groups was to provide technical and management expertise to Mapeto (DWSM) limited at no fee.

The Executive Director of PC stated further the business plan submitted to the commission indicated that Mapeto (DWSM) Limited intended to invest US\$ 11.25 million in rehabilitation and expansion expenditure. The Bidder intended to gin and spin at the Salima factory, ultimately fixed employment was expected to rise to 3,000 to 4,000 over five years.

To understand what was meant by free of accumulated corporate commercial liability, as well as free of accumulated Government and shareholders indebtedness in the interview with the Executive Director, the 1996 Statements of accounts for DWS have the following note:

Subsequent to the year end, the Government of Malawi, being the sole shareholder, has resolved to restructure and reorganize the company with the objective that it reverts to profitability. The restructuring will include the capitalization of Government loans of MK78 million and the Government has also agreed to waive arrears of surtax amounting to MK15 million. As part of the restructuring and, the commitment in principle to provide continued financial support, Government has

provided additional working capital of K42 million. The accounts have therefore been prepared on a going concern basis.

What comes out from the 1996 accounts is that the company was capitalised to the tune of K135 million in the period prior to privatization. It was sold for K73 million.⁷³

The Chief Executive of DWS and workers dissatisfied by the decision to sell DWS at a loss having been capitalized for a whopping K135 million took the Privatization Commission to court and obtained an injunction seeking to stop the sale, which injunction was later vacated⁷⁴. An attempt was made to resolve the impasse and to address the public concerns relating to the sale by the establishment of a Presidential Commission of Inquiry chaired by Presidential Advisor Goodall Gondwe. The Presidential Commission of Inquiry found that appropriate considerations had been taken prior to the sale and recommended that the sale proceed. Writing in the social media one journalist gave an overview the situation prevalent at the time:

“Many analysts also took for a joke DWS' sale price of K73 million, saying it was too low. But the PC argued that the company could not have fetched more, given its precarious financial position due to huge debts and below- capacity production owing to obsolete machinery. The Privatization and subsequent sale of DWS was thus marred by controversy as former employees put up violent resistance claiming the PC had suppressed the company's true market value which they estimated at over K300 million.”⁷⁵

⁷³ See Statement by PC dated

⁷⁴ *Mwapasa and another v Stanbic Bank Ltd* Misc Civil Cause No. 110 of 2003

⁷⁵ Mapeto puts K400m in DWS - Report BY FRANK PHIRI at <https://groups.yahoo.com/neo/groups/MALAWIANA/conversations/topics/1622>. Accessed on 11 November 2013

It is not the concern of this research to look at whether the sale of DWS was a good deal or not but rather this research looks at whether in PEPA there existed a legal framework that ensured that the interests of the employees and the public interest were sufficiently taken into account at the time of privatization. The research explores whether the need to appoint a Presidential Commission of enquiry was an attempt to fill a gap existing in the legal framework contained in PEPA.

4.1.2 The Divestiture of MSB

The divestiture of MSB was undertaken after the coming into operation of the PPPA. The divestiture was undertaken in circumstances that were reminiscent of the privatization of DWS.

MSB started its operations as a bank when it took over the financial service activities of the Malawi Post Office Savings Bank (POSB). MSB and the Malawi Post Corporation (MPC) signed an agency agreement permitting MPC staff to process transactions for MSB depositors.

MSB was incorporated on June 16, 1994 as a private company limited by shares under the Companies Act. All assets and liabilities of the defunct POSB were transferred to it. MSB was granted a banking license in March 1995. While it was subject to all Banking Act regulations, the RBM provided it exemptions from the liquidity reserve requirements. MSB had a six-person Board of Directors and its Chairman represented the Ministry of Finance. The GoM held essentially 100% of issued and fully paid up shares in MSB. (Buritt, 2006:153)⁷⁶

⁷⁶As per (Kampanje, 2013)

According to (Kampanje, 2015) the Government of Malawi's bids offering seventy-five per cent equity stake in Malawi Savings Bank were made in March 2015 when the bank had not published its year-end financial statements as at 31st December 2014. Therefore, the bases for negotiations were derived on half-yearly results for period ending 30th June 2014 which depicted the net assets of the bank (total assets less current liabilities) as MK5.65 billion (about US\$12.44 million) and therefore total net assets attributable to acquirer would be US\$9.33 million against offered price of US\$10.00 million. (Gondwe, 2013) noted that the valuation of Malawi Savings Bank could have been grossly overstated in view of toxic assets which the bank had accumulated due to political interference. (Gondwe, 2013) noted by as follows:-

... The IMF is said to have observed that politically-connected persons, like Mulli Brothers, got huge loans from MSB but are failing to service them.

The Bretton Woods institutions are also said to have recommended that debts amounting to over K3 billion which MSB advanced to Mulli Brothers should be written off and should not appear as assets of the bank.

The initial offer of US\$10.0 million might have taken into account the toxic assets that were haunting the bank. According to (Gondwe, 2013) the final consideration of US\$21.1 million appears to be a fair price based on the financial condition of the bank.

It has however been stated by (Kampanje, 2015) that the general public through Civil Society Organizations (CSOs) applied for high court injunction to block the sale of equity in Malawi Savings Bank. This was however quashed by the Court on the basis

of lack of sufficient interest by the applicants in the matter⁷⁷. The second legal application was made by members of staff of Malawi Savings Bank who were seeking court's interpretation of whether the proposed sale of Malawi Savings Bank was in full compliance with Public Private Partnership Act. The case also failed as the court did not find that the employees who commenced the action had substantial interest in Malawi Savings Bank to commence action employees in the matter⁷⁸.

The sale of MSB was also vigorously debated in the National Assembly with considerable emotions from both government and opposition sides.

In the heat of the debate over the privatization President Mutharika through a press statement suspended the sale.⁷⁹ The suspension was however short lived as without any announcement to the general public the Minister of Finance proceeded to finalize the sale and divestiture of the bank. President Peter Mutharika issued a statement after the sale stating that government has sold the bank after listening to public debate and based on powers conferred on him by the Constitution.⁸⁰

"The general public is, therefore, assured that the sale of the government shares in MSB shall not, in any way, result in closures on any branches currently operating throughout the country," said a statement issued by President Mutharika's press secretary Gerald Viola.⁸¹

⁷⁷ The researcher's effort to get the court judgment or record were futile and the research relied on the reports published in the press

⁷⁸ ditto

⁷⁹ <http://www.times.mw/peter-mutharika-defers-malawi-savings-bank-sale/> Posted By: Gregory Gondweon: June 04, 2015In

⁸⁰ <http://allafrica.com/stories/201507021178.html> per Zawadi Chilunga

⁸¹ ditto

4.2 The Privatization policy and practices in the privatization of DWS and MSB

The privatization of DWS and the divestiture of MSB were similar to the extent that they were characterized by the PC or PPPC with Government on its side insisting that the privatization was the right thing to do and a chorus of voices of dissent claiming that Malawians were being shortchanged by the privatization.

4.2.1 The case of DWS

The former Executive Director of the Privatization Commission Dye Mawindo stated, in relation to privatization, the following:

This new policy came about in 1994, following the change of government. As part of its manifesto, the UDF (United Democratic Front) had the wish to divest government ownership of public enterprises. The rationale was to rid the government of the onerous responsibility of managing public enterprises, understanding and accepting that the government did not have a competitive advantage in managing these various public enterprises. It is the private sector which has a competitive advantage, so the decision to divest various interests had four major objectives: the first was to increase efficiency, the second was to generate competition in the economy, the third was to enable Malawians to participate in the companies that were to be privatized, and the final goal was to raise revenues⁸²

Thus the rationale of the privatization of DWS having been premised on the honourable intention to rid the government of the onerous responsibility of managing public enterprises, the privatization of DWS cannot be singled out as improper. However, according to (Magalasi 2008) the divestiture plan for sale of DWS was

⁸²Forbes Global Magazine. October 30th 2000 Issue. Accessed at <http://www.winne.com/malawi/to16interv.html#top> on 7 November 2013 at 19:40 hrs

approved by Cabinet in 1996. The final sales agreement to transfer shares was, as is required by the law, signed by the minister Responsible for finance, where the shares sold were directly owned by the Government.

In an interview with Meya Chinula it will be recalled that the Executive Director stated that it was very apparent that failing a sale of DWS, the only other viable option was factory closure⁸³.

It will be observed that the PC stated that it was a good deal. The Minister for Privatization and the Minister of Finance said that it was a good deal and the Commission of enquiry found that there was nothing untoward in the sale.

Thus the research was able to establish that in terms of compliance with the black letter of the law there was nothing wrong with the privatization of DWS.

4.2.2 The Case of MSB

The decision to privatise MSB although implemented in the year 2015 had been mooted much earlier. In the year 2001 an international tender was floated by the Malawi Government with funding from International Development Corporation under Phase 1 to evaluate both MSB and MRFC for any possible restructuring to put the two entities on strictly commercial basis; the merger of two institutions; and options for privatization of the two institutions.⁸⁴

⁸³Paragraph 4.2 above

⁸⁴DgMarket

It has been stated that at the time that the decision to privatise both MSB and MRFC was made, the two SOEs were still receiving support from World Bank Privatization and Utility Reform Project (PURP) to restructure their operations to prepare for eventual private sector participation in their ownership (Burrit, 2006:7).

In 2015 the Public Private Partnerships Commission (PPPC) requested strategic investors to buy a controlling stake in state-owned Malawi Savings Bank (MSB) and Indebank Malawi Ltd., in which the government owned nearly 70 percent of its shares.

PPPC did not disclose the sizes of the stakes that were up for sale or how much it was selling them for.⁸⁵

"The decision to recapitalise the two institutions has been motivated by the desire to strengthen their financial and operational capabilities in a competitive environment,"⁸⁶ the agency said in a statement.

Kampanje (2015) states that Sabola (2015) however observed that Government of Malawi had issued promissory notes in excess of MK6 billion (US\$13.3 million) to clean up toxic assets in readiness of takeover by FDH Financial Holdings Limited: Sabola (2015) quoted the following:

"I write to inform you that government has resolved to hive off MSB toxic assets amounting to K6,074,773,871.70 and to replace them with a promissory note. In this regard, I have already requested the Reserve Bank of Malawi to issue that promissory note for this purpose," reads the letter in part.

⁸⁵ <http://www.reuters.com/article/malawi-privatisation-idUSL6N0UY28R20150119>

⁸⁶ Ditto

(Kampanje, 2015) states that this is a probable indication that Malawi Savings Bank's assets were overstated and cleaning up the toxic assets was only meant to reinstate the balance sheet of the bank to its real monetary terms with no possible benefit to FDH Financial Holdings Limited. Some of the debts had to be cleaned since government had guaranteed them.

4.3 Public interest issues in privatization of DWS and MSB

Around the time of the privatization of DWS D.D. Phiri wrote an article in the Nation Newspaper which stated as follows:

“The dispute about the sale of David Whitehead and Sons is not just a matter for the firm's employers and those who want to buy it. David Whitehead and Sons is one of the flagships of the Malawi economy. Whatever happens to it is a matter of concern to third parties; members of the public.

The findings of the President's Commission of Inquiry into the wrangles are eagerly awaited. They will form part of our experience in handling privatization of government enterprises. What I am going to say here is not intended to prejudge what the commission will bring to light. Rather my aim, as a member of the public, is to remind ourselves that what is going on is as much our business as it is the business of those who are directly concerned.

The reasons for government disposing of its commercial assets are well-known. In spite of the good intentions, profit making is not part of good governance. In the majority of cases state owned enterprises have not been successful. To remain in business they have had to receive constant infusions of government subvention or government backed loans. It is the hope of those who advocate the sale of a state enterprise that the

private owners will run it so efficiently that it will not just survive but expand as well.

The article aptly demonstrates what the research found that the privatization of DWS was marred in controversy involving both employees and members of the public. The controversy was such that it involved the appointment of a Presidential Commission of enquiry. Public interest appears to have been ignored in the whole process of the privatization of DWS.

The case of public interest in the privatization of MSB is no better. There were protests and complaints from various quarters of the Malawi society. As an epitome of the dissatisfaction the the Budget and Finance Committee of Parliament recommended that government should stop the sale of Malawi Savings Bank (MSB).

According to a report published by the Times on line Newspaper the committee stated the stop had to be pending injection of K4.5 billion that was required to make it stand on its feet so that it meets Basel II requirements.⁸⁷ Committee Chairperson, Rhino Chipphiko said this in Parliament when he presented his committee's findings on the sale of the bank.

“In the interim, management should be challenged to run the bank proficiently while, in the process, government should help the bank to collect its non-performing loans from politically exposed persons to strengthen its financial muscle,” Chipphiko said.⁸⁸

⁸⁷ Parliament resolves against MSB sale” reported by Macdonald Thom accessed at <http://www.times.mw/parliament-resolves-against-msb-sale/>

⁸⁸ “Parliament resolves against MSB sale” reported by Macdonald Thom accessed at <http://www.times.mw/parliament-resolves-against-msb-sale/>

The research therefore established that in both the privatization of DWS and MSB the question as to whether there was sufficient consultation or whether the privatizations took into account the public interest prior to the privatization was answered in the negative. It was established that the privatization went ahead in spite of concerns raised.

4.4 (In)Effectiveness of application legal principles of Corporate Governance

It has been stated by (Vagliasindi, 2008) that to ensure corporate governance in an organization there is need to have a sufficient number of independent directors. (Vagliasindi, 2008) however notes that empowering them to exercise effective monitoring of management, however, may prove to be a formidable challenge for of state owned enterprises. More attention to board procedures, particularly related to the Board selection and evaluation process, is essential, to produce the necessary insulation of Boards from government interference. Ensuring sufficient continuity of services to directors is particularly crucial to improve corporate governance. In addition, other factors that may reduce directors' ability to monitor corporate activities, such as the age profile and the number of Boards on which they sit, need to be handled more carefully.⁸⁹

When the research looked at the legal framework governing privatization in the previous chapters above it was noted the appointment of Commissioners and who could be appointed as commissioner leaned heavily in favour of the government. Similar issues were also noted in terms of the appointment of the Chief Executive

⁸⁹Maria Vagliasindi "The Effectiveness Of Boards Of Directors Of State Owned Enterprises In Developing Countries" World Bank Policy Research Working Papers. March 2008 accessed at <http://elibrary.worldbank.org/doi/abs/10.1596/1813-9450-4579> on 14 October 2015

Officer and the Secretariat. The research thus established that the legal framework obtaining in PPPA just as that obtaining in PEPA was such that it was the cabinet essentially that decided on the privatization of MSB just as it did in the privatization of DWS. Although the employees and the general public complained or went to court there was no mechanism for their grievances to be sufficiently addressed. Corporate governance principles were thus either lacking or were not adhered to.

4.5 Conclusion

While in this Chapter the research has looked at the privatization of entity that was DWS and the divestiture of MSB, focus of the research in reality was the application of PEPA and the PPPA in relation to those privatizations. The two case studies examined the governance structure of privatization obtaining in PEPA and that obtaining in PPPA. Having examined that governance structure in the PEPA the research established that there were inherent deficiencies in the framework and posited that these deficiencies were to some extent responsible for the dissatisfaction that went with the privatization of DWS. The research then looked at the divestiture of MSB and the legal framework obtaining in PPPA. The research noted that the legal framework in respect of divestiture of SOEs under the PPPA did not improve on the structure obtaining in PEPA. It was established that the structure obtaining in PEPA was transferred *mutatis mutandis* into PPPA.

The research thus found that the legal scheme obtaining in PPPA just like that in PEPA has in reality no corporate governance structure separating ownership and control in the framework governing privatization or divestiture. The PPPC like its predecessor the Privatization Commission is not independent of the government. The

PPPC board is appointed by the President. The PPPC reports to the Cabinet through the Minister. The Commission is full of representatives and appointees of Government. The Minister's decision is approved by the Cabinet. The public only comes close to receiving a report when an annual report is presented in Parliament at the earliest and if at all close to two years after the event.

Thus in the divestiture of MSB, as happened with the privatization of DWS, although there was a public outcry and although the employees of MSB as their counterparts in DWS took the Commission to court, this did not help. The court did not see the need to look at the conduct of the agent of the Government. The Government in the case of DWS in a self-fulfilling prophecy appointed a commission headed by an insider. The findings of the Commission did nothing to allay the concerns that led to the appointment of the commission of enquiry in the first place.

In the case of MSB there was an outcry by employees, the Legal Affairs committee of Parliament and the public at large. The President acknowledging that all was not well in the privatization of MSB suspended the sale. However, there being nothing in the legal framework to prevent the finalizing of the sale of MSB to FDH Bank the Minister of Finance with apparent acquiescence of the President proceeded to complete the divestiture of MSB in disregard (if not with contempt) to the public outcry on the sale.

CHAPTER 5

CONCLUSION AND RECOMMENDATIONS

The aim of this research was to find out if there existed corporate governance gaps in the legal framework governing privatization under PEPA and whether the repeal of PEPA and the enactment of PPPA improved on and addressed the corporate governance issues relating to privatization. The research sought to establish whether if gaps existed in both PEPA and PPPA the gaps contribute to lack of transparency in privatization vis-a-vis safeguarding the public interest. The research has established that there were indeed corporate governance gaps in PEPA and the approach to divestiture under PPPA was not an improvement on the structure obtaining in PEPA. The Commission is appointed by the President. In a serious regress the requirement for Commissioners to be approved by the Public Appointments Committee of Parliament was removed. The Commission works hand in hand with the Minister of Finance. The Commission reports to Cabinet which is chaired by the President and includes the Minister of Finance. The research has established that while PPPA as PEPA gives the PPP commission the responsibility to determine and implement privatization by making it answerable to the Cabinet there is in fact no corporate governance oversight as both the Commission and the Cabinet are insiders. Under PPPA just as PEPA the proceeds of privatization are utilized in the most part for purposes that are not for public benefit. This legal framework renders itself open to abuse by the PPP Commission and the Cabinet. It is very important to keep in mind the importance of interests that inform the privatization process.

Good governance is demanded of our government in respect of its public duties and governance institutions such as the ACB, the ODPP and the CFTC are set up for that purpose. The question that we ask is why we do not have a governance structure set up to ensure corporate governance in respect of privatization. The current research has demonstrated in the case study of DWS that although the finding of the Goodall Gondwe Presidential Commission of Enquiry was (as could be expected) that there was nothing wrong with the sale or privatization of David whitehead, the mere setting up of the Presidential commission to look at that privatization demonstrates the yawning corporate governance gap that existed in the legal framework governing privatization in Malawi. Similarly, if the legal framework under the PPPA had sufficient corporate governance safeguards there would be no need to set up commissions of enquiry or as was the case in the sale of MSB for parliament to have a debate and an ad hoc resolution to stop the sale of MSB or indeed for the President to temporarily stop the sale.

To comply with principles of Corporate governance and to protect the public interest with regard to privatization, it is recommended that PPPA ought to be amended. There is a need to have a commission characterised by independence away from the Cabinet. Thus it is recommended that the board should be selected by a competitive transparent process. The Commission ought to be made available and willing to answer questions not from fellow insiders such as the Minister of Finance or Cabinet but from Parliament. The Commission should have a diversity of membership and it is recommended that there is need for independent people in the PPP Commission. The entire Commission and the CEO should be hired and fired by Parliament. They should be reporting not by annual reports but timeously and at any time when called upon do

so by a relevant Committee of Parliament. These recommendations if implemented would ensure transparency in decision-making and accountability to the members of the public.

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