

THE DIVIDEND POLICIES AS A MECHANISM OF CORPORATE GOVERNANCE IN UZBEKISTAN

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Abstract

Distribution of profits is one of the important issues for most investors, especially for minority shareholders and individuals. For private investors it is particularly important to be aware of dividend policies of joint-stock companies. This study deals with the regulation of the process and payment of dividends in joint-stock companies in Uzbekistan and, analyzes recent trends in the payment of dividends in companies representing various sectors of the economy. It should be noted that the legislation of Uzbekistan, sets a number of requirements for public companies to ensure timely provision of information to all shareholders with respect to distribution of profits and payment of dividends. However, as analyzed the quality and scope of information provided by joint-stock companies in practice does not meet the regulatory requirements. The analysis shows that dividends are paid by most companies, although amount of dividends differs. As expected, private joint-stock banks tend to deliver higher dividend yield ratio. In my opinion, the level of dividends in the Uzbekistan's banking sector is largely affected by a number of factors, including the shareholders structure, profitability of banking operations, level of state intervention as well as track record of dividend payments. This is also in line with some other authors, who find that banks with higher profitability or performance pay more dividends in Korea (S.Lee, 2009) as well as large and more profitable companies have a higher dividend payout ratio in Poland (O.Kowalewski et al, 2007). The paper suggests that stock exchange, investment advisors and credit rating agencies should play an increasingly important role in monitoring market trends, ensuring compliance with regulatory requirements and to identify best practices in the activities of joint-stock companies, especially in the areas of investor relations, disclosure of information to shareholders and implementing clear dividend policies.

Keywords: joint-stock companies, minority shareholders, shareholders' meeting, income distribution, dividend policies, dividend payments, stock exchange

INTRODUCTION

Joint-stock companies represent the bases of modern industry in Uzbekistan, which has increased significantly its share in GDP from 14% in 1991 to 24% in 2014. At present more than 1,100 joint-stock companies operate in Uzbekistan, most of them being created as a result of privatization process in the 1990's and still some of the important enterprises maintaining the government share in the capital. They represent large enterprises operating in manufacturing, oil and gas, mining, chemicals, construction materials, financial services and other sectors of the economy. Total share capital of joint stock companies exceeds 11.7 trillion soums (equivalent of 4,775 Billion US Dollars at current exchange rate) as at the end of 2014 and this amount has grown 5.3 times for the last ten years.

Corporate governance in large enterprises still remains weak, existing rules and regulations requires revision. Many enterprises are dominated by directors, while interests of other shareholders and society may not be properly protected. This is especially true in case of JSC with state ownership, where minority shareholders in practice have to voice in corporate governance and decision-making process. Recently it is being recognized by the government that corporate governance principles and practices should be revised based on the experience of industrially developed countries, especially with regards of distribution of income, the role of state in corporate governance and further privatization of state-owned enterprises.

REGULATORY REQUIREMENTS IN RESPECT OF DIVIDENDS

The question of distribution of profit and dividend payments is one of the key issues for investors. Legislation in the field of securities market and joint stock companies sets out a number of requirements for decision-making and distribution of net profit enterprises. In particular, Article 55 of the Law of Uzbekistan "On joint-stock companies and protection of shareholders' rights" stipulates that the payment of dividends and its amount belongs to the competence of the general shareholders' meeting based on the recommendation of the Supervisory Board.

In the corporate legislation of Uzbekistan is no definition of "dividend". Among the provisions of the Civil Code of Uzbekistan, Article 43 states that the memorandum of association specifies the conditions and procedure for distribution of legal entity's profit and losses among the participants. In Article 59 of the Civil Code among the rights of participants of the legal entity stated the right to participate in distribution of profits, while the Article 65 of the Law "On joint-stock companies and protection of shareholders' rights" defines the distribution of profit and losses as the exclusive competence of the general meeting of shareholders.

Table 1. Main requirements for dividends according to Law of the Republic of Uzbekistan
 "On joint-stock companies and protection of shareholder rights"

Decision of payment of dividends	Frequency of dividend payments	Sources of dividend payments	Dates of dividend payments	Dividend payments sequence	Taxation of Dividends
The General Meeting of shareholders on the basis of recommendations of the Supervisory Board	Possibility of paying dividends for the quarter or the year	Dividends are paid from the net profit of the reporting year and (or) retained earnings of previous years	Dividend payment period may not be later than 60 days from the date of such decision	First of all, dividends are paid on preferential shares, then dividends on ordinary shares	Income tax rate for dividends and interest paid to residents of the Republic of Uzbekistan is set at 10 percent

Source: Compiled by the author based on the legislation norms.

However, the Company Law uses the notion of dividend (articles 53, 54, 55, 56). In our opinion, the concept of "profit distribution" in the Civil Code of Uzbekistan and the term "dividend payment" in the Company Law are used interchangeably. This opinion is also in line with the civil law as a means of understanding the distribution of profits among the shareholders of the joint-stock companies. There is every reason to believe that the legislation considers that the dividend is part of the income of society, which is to be divided among the shareholders.

The law states that the amount of dividends may not exceed the amount recommended by the Supervisory Board. In this regard, in preparation for the convening of the general meeting of shareholders, which agenda includes the issue of dividends, the Supervisory Board prepares recommendations on the amount of dividends. Recommendations of the Supervisory Board with respect to the payment of dividends shall be based on the results of financial and economic activities of the company, which needs to be confirmed by the opinion of the independent auditors and the audit committee. As a rule, many joint stock companies hold annual general meetings during May-June, where the issues related to auditors reports and distribution of profits shall be considered.

To receive dividends are entitled the shareholders recorded in the register of shareholders formed for the general shareholders' meeting. According to legal requirements, the company closes the register of shareholders 3 calendar days before the official announcement date of the General Meeting of Shareholders, which will consider the distribution of profits of the company. As the analysis of trading at stock exchange shows, during the general meeting of shareholders many owners held back from selling their shares as interested in receiving dividends.

All shareholders included in the register of shareholders of the Company, have the opportunity to attend and vote at the general meeting of shareholders, including on the issue of distribution of profits of the company. Therefore, it is important for small shareholders to participate, vote and, if necessary, to clarify certain issues. Voting at the General Meeting of Shareholders based on the principle "one voting share of the company - one vote". The decision of the General Meeting of Shareholders shall be adopted by simple majority. It should be noted that the general meeting of shareholders is competent if more than 60% shareholders of representing common shares of the Company have been registered.

The Company Law establishes a number of restrictions on the conditions under which and how much corporation shall be entitled to payment of dividends. In accordance with Article 60 of the Company Law, the Joint-stock company may not decide to pay dividends in the following cases:

- Until full payment of the share capital of the company. Until full payment of the charter capital, dividends may not be declared or paid.
- If at the time of payment of dividends, the Joint-stock company has the elements of bankruptcy or the payment of dividends may cause such consequences. This restriction on the payment of dividends is a standard safeguard in the interests of creditors.
- If on the day of the decision to pay dividends, the value of company's net assets is less than the sum of its charter capital and reserve fund. This is a common provision in the Law designed to protect the interests of creditors and shareholders.

In order to protect the rights of shareholders and creating equal access to material information about the Company's activity, in accordance with the legislation establishes disclosure requirements for issuers on the general shareholders meeting, issues on the agenda, etc. Thus information about the general meeting of shareholders shall be communicated to the shareholders by publishing relevant information in the press and sending them a written notice on the basis of the register of shareholders. Additionally, information about material facts, including the accrual of income on securities, start and end dates of payment of dividends must be submitted to the Centre for Coordination and Control of the Securities Market no later than two working days from the occurrence of a material fact as well as during the same period published in the media.

THE PRACTICE OF PAYING DIVIDENDS

Our analysis shows that many Joint-stock companies have taken the decision to pay dividends to shareholders. As practice shows dividends are paid by most companies, although amount of dividends differs. For example, in large commercial banks dividend yield ratio, i.e. the ratio of

amount of dividend to nominal value of shares ranges from 2.5% to 15%. As expected, private joint-stock banks tend to deliver higher dividend yield ratio. In my opinion, the level of dividends in the Uzbekistan's banking sector is large affected by a number of factors, including the shareholders structure, profitability of banking operations, level of state intervention as well as track record of dividend payments. This is also in line with some other authors, who find that banks with higher profitability or performance pay more dividends in Korea (S.Lee, 2009) as well as large and more profitable companies have a higher dividend payout ratio in Poland (O.Kowalewski et al, 2007).

In many large enterprises a significant portion of net profit goes to the implementation of various projects, including the purchase of new equipment, construction of new facilities, etc. It should be noted that such a policy is stimulated by the presence of a number of tax benefits. For instance, dividends received by legal entities as a return on funds allocated for capitalization and investments are exempt from taxation. Also in accordance with the Tax Code of the Republic of Uzbekistan dividends re-invested into share capital of the legal entity, from which they have been derived, are not taxable.

The amount of funds allocated for payment of dividends, also varies by issuers. In particular, one of the largest banks "Uzpromstroybank" paid dividends worth 3776 mln. soums in 2013, which is 37% of the total net profit for the year. At the same time, it should be noted that the new banks in the first years of activities usually tend to invest net profits into expansion of activities. Thus, shareholders of JSC «Asia Alliance Bank» decided to re-invest full amount of net income in 2009 for expansion of bank's operations, of which 30% for the reserve fund, 25% for the fund of concessional lending and the remaining 45% as retained profits. Such a decision of the new bank is logical since it has plans to increase its capital base to the level of other established private banks in the country.

Table 2. Dividend payments in selected joint-stock companies in Uzbekistan

Issuer company	Date of decision on dividend payments	Amount of dividends per share	Dividend yield ratio
Banks			
Uzpromstroybank JSC	4.06.2010	472 soums	2,5%
Ipotekabank JSC	21.05.2010	150 soums	15%
Aloqabank JSC	25.05.2010	8 soums	8%
Trustbank JSC	25.06.2010	690 soums	69%
Industrial enterprises			
Uzmetkombinat JSC	5.06.2010	42,76 soums	3,75%
AGMK JSC	21.05.2010	51,46 cym soums	5,15%
Kyzilkumsement JSC	7.05.2010	7 002,00 soums	7%

Ahangarancement JSC	28.06.2010	-	-
Ferghanaazot JSC	28.06.2010	39,86 soums	0,4%
Koson yoq-ekstraksiya JSC	2.06.2010	-	-
Trade and services			
Chilonzor Buyum Bozori JSC	15.04.2010	250 soums	25%
Uztelecom JSC	25.06.2010	43,45 soums	4,3%
Matbuot Tarqatuvchi JSC	28.05.2010	305,64 soums	30,56%

Table 2...

Source: www.gazetabirja.uz, www.orientcap.uz

In accordance with the law, the payment of dividends in the first place paid dividends on preferential shares, then dividends on ordinary shares. The payment of dividends on preferential shares, in case when net profit is not adequate, is possible from the reserve fund established for this purpose. The minimum amount of dividends on preferential shares of Joint-stock companies shall be defined in the statute of the company. In practice, many companies tend to pay higher dividends on preferential shares compared to ordinary shares. For example, the JSC "Uzpromstroybank" decided to pay dividends on preferential shares for 2009 in the amount of 20% of their nominal value, which is much higher than the level of dividends to ordinary voting shares. "Uzbektelecom" paid on ordinary shares 2.5% dividends, while on preferential shares - 25%. But not all enterprises and financial institutions do so. "Uzmetkombinat" decided to pay dividends on common and preferred shares the same size - 4% of the nominal value of the shares.

CONCLUSIONS AND SUGGESTIONS

Our analysis demonstrates that corporate governance is an important determinant in explaining the dividend policy of public companies in Uzbekistan. In my opinion, the level of dividends in the Uzbekistan's banking sector is largely affected by the shareholders structure, profitability of banking operations, level of state intervention as well as track record of dividend payments. Banks with more private shareholders tend to pay higher dividends compared to state owned banks. These results also suggest that when shareholders have greater participation and involvement in corporate governance, they can use their power to influence dividend policy.

The paper also shows that regulatory framework and fiscal incentives play an important role in corporate decisions on dividend payments. In many large enterprises a significant portion of net profit goes to the implementation of various projects, including the purchase of new equipment, construction of new facilities, etc. These decisions have been stimulated by the presence of a number of tax benefits. For instance, in accordance with the Tax Code of Uzbekistan dividends re-invested into share capital of the legal entity are exempt from taxes.

The results of the analysis demonstrate that the quality and scope of information regarding the corporate policies on income distribution and dividend payments should be enhanced. It suggests that the combined effort of the securities market regulator and professional associations should be aimed at introducing the mandatory disclosure of dividend policy adopted by shareholders. In addition, it is recommended that separate units should be created to deal with investor relations (disclosure of information, preparation of shareholders meetings, preparation of dividend policies etc) and ensure compliance with the regulatory requirements.

Stock exchange, investment advisors and credit rating agencies should play an increasingly important role in monitoring market trends, ensuring compliance with regulatory requirements and to identify best practices in the activities of joint-stock companies, especially in the areas of investor relations, disclosure of information to shareholders and implementing clear dividend policies.

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