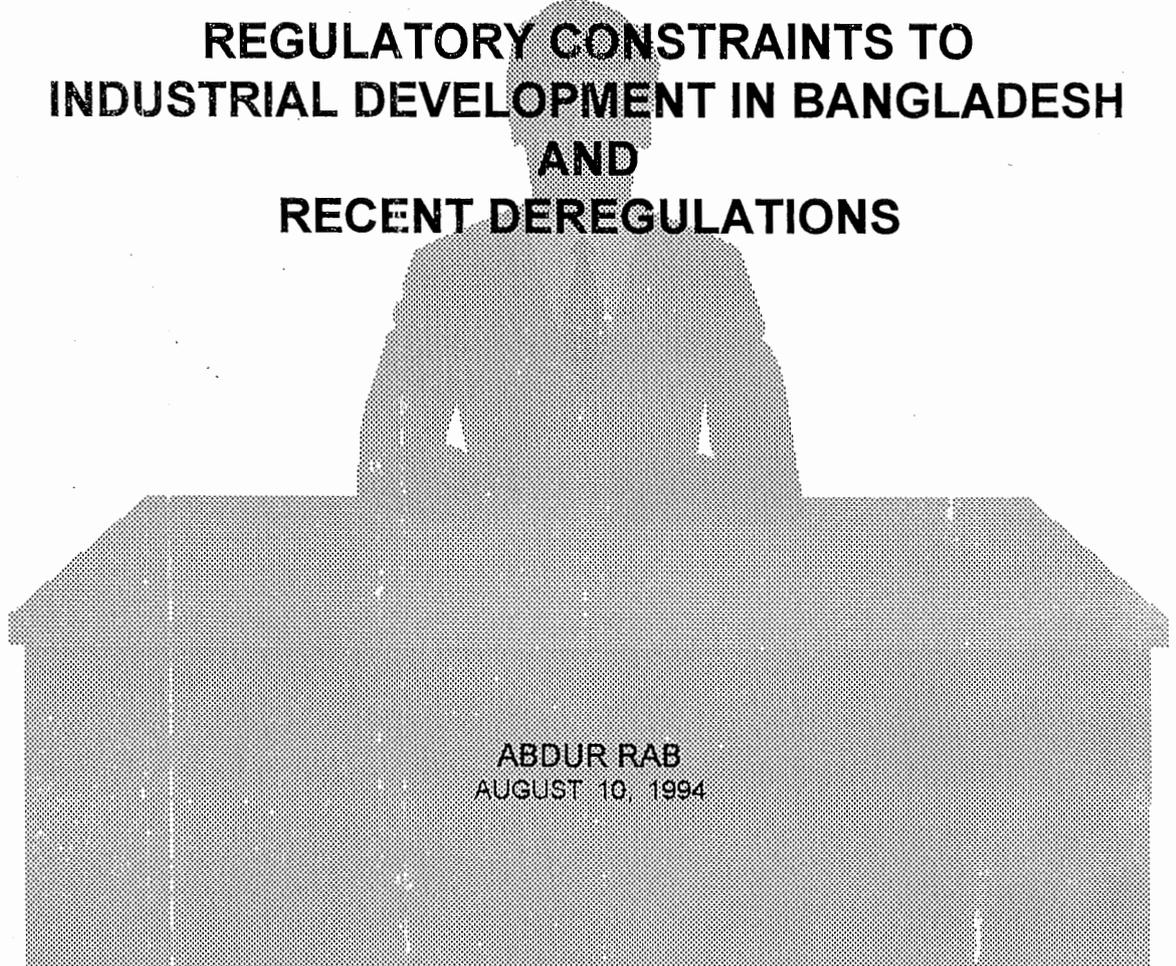


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FINAL REPORT

# REGULATORY CONSTRAINTS TO INDUSTRIAL DEVELOPMENT IN BANGLADESH AND RECENT DEREGULATIONS



ABDUR RAB  
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A PROJECT OF THE

MINISTRY OF INDUSTRIES, GOVERNMENT OF BANGLADESH  
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MANAGED BY

INTERNATIONAL MANAGEMENT AND COMMUNICATIONS CORPORATION (IMCC), WASHINGTON



## FOREWORD

The Policy Implementation and Analysis Group (PIAG), a project of the Ministry of Industries implemented with financial assistance of USAID, is designed to enhance the policy formulation and policy implementation capabilities of this Ministry. The purpose of the project is to carry out studies and analyses to identify problems and constraints with industrial policies and their implementation, to assess the effects of incentives and support services to the industrialization process, to determine areas where policies and procedures of the Government need to be modified, and to assist the Ministry in formulating and evaluating new policy recommendations. This report, *Regulatory Constraints to Industrial Development in Bangladesh and Recent Deregulations*, is the sixth in a series of PIAG reports aimed at providing the Government and the private sector such information.

The present report has been through several drafts. The first draft was important for the country's development process since it was a significant step towards meeting part of the conditionalities for the World Bank's Second Industrial Sector Adjustment Credit Programme (ISAC-2). The draft was sent to a wide spectrum of relevant organizations including Government ministries and agencies, business chambers and associations and members of the donor community. The final draft was prepared taking into account the feedback received from various quarters.

Some recommendations have already been accepted and implemented as a result of this process. The final draft was published in January 1994 and was circulated to relevant ministries, agencies and organizations. A day-long seminar was held in April to deliberate on the report. In addition to many good suggestions and inputs that were received at the seminar, a summary of the seminar proceedings was prepared and sent to all participants for a final opportunity for comments on the report. Based on all of these, the final report is now being published.

The Ministry of Industries and its Policy Implementation and Analysis Group now invite the concerned Ministries, Agencies and Organizations to study the report and consider its recommendations. The Ministry along with PIAG will be holding targeted discussions on specific areas covered in the report over the next several months.

We look forward to a continued and fruitful dialogue on deregulation as well as continued progress towards creation of an enabling environment conducive to rapid industrial growth and economic development.

Syed Yusuf Hossain

Additional Secretary, Ministry of Industries and  
Project Director, PIAG



## ACKNOWLEDGEMENTS

This study represents one of the major tasks of the PIAG's initial work program and at the same time meets one of the requirements of the World Bank's Second Industrial Sector Adjustment Credit (ISAC-2) program for the Bangladesh Government. The study is the product of a joint-sponsorship of the Ministry of Industries of the Bangladesh Government and the USAID mission in Bangladesh.

A major research effort involved in this study has been documentation of considerable information about a wide array of industrial regulatory policies regarding both the current situation and recent changes and on the empirical aspect of private entrepreneurs' perceptions of the problems they face from regulatory policies. This documentation work could not have been possible without the generous and active co-operation the author has received from many government, semi-government and other organization officials and private industry entrepreneurs and managers. These persons have been listed in Attachment 2 of this report. The author gratefully acknowledges their help.

Two earlier versions of this report received thorough in-house scrutiny in the hands of PIAG's Chief of Party Dr. Ronald Black. The initial draft (then without the concluding chapter on recommendations and executive summary) has been discussed by the PIAG team and also in a meeting with several USAID officials. The second chapter of the report on investment controls was discussed with some officials of the Board of Investment (BOI) and its advisor Dr. Charles Byron. Some BOI officials provided written comments on some observations in the paper. Written comments have been received also from IMCC's Dr. Trent Bertrand and Mr. Paul Pieper. Some editorial and other comments for improvement were also received from Dr. Ross Bigelow of USAID. The final draft of the report dated January 23, 1994 was discussed in a day-long seminar on 16 April, 1994 organized by PIAG and the Ministry of Industries. This final version takes into account many valuable comments made by the designated discussants, Dr. Zaid Bakht, Mr. Chaudhury A.K.M. Aminul Haque, Dr. A.K.A. Mubin, Mr. Anis ud Dowla and Mr. Syed Nizamuddin, and other participants. Some post-seminar suggestions for further improvements of the paper were also received from Dr. Stuart Callison and Dr. Nazmul Hossain of USAID. The author wishes to gratefully acknowledge his debt to all of them whose comments have helped improve the content and presentation of the paper. The author, however, remains solely responsible for any remaining errors of omission and commission and for any views expressed in the paper.

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# EXECUTIVE SUMMARY

01. In recent years, the Bangladesh Government has made commendable progress in economic policy reforms. The policy documents profess a considerably liberal environment for private sector operation. However, the policy improvements have not yet been able to create a significant private sector response. Growth and investment have remained at low levels in recent years. Overall private investment rose to only 7% of GDP last year. The flow of foreign direct investment remains very meager. The sluggishness of investment and growth continues despite an impressive improvement effected in macro-economic management.

02. The continued lack-lustre growth and investment can be attributable to a whole host of factors: poor infrastructure; limited access to credit; an inefficient labor force and labor market; a controlled trade policy and foreign exchange regime; a deficient legal framework; administrative and bureaucratic bottlenecks; a high tax regime; poor public enterprise performance; slow privatization initiatives; and last, but not least, the dramatically increasing world-wide competition for new industrial investment. The present study focuses on the industrial regulatory framework in Bangladesh, which encompasses some of these factors. Particular areas reviewed are:

- Investment controls.
- Exchange controls.
- Quantitative import restrictions.
- Export controls.
- Banking regulations.
- Labor regulations.
- Legal reform issues.
- Industry-specific regulations.

## Investment Controls

03. Officially all controls on private domestic and foreign investment have been eliminated except for regulated sectors and a few sectors reserved for exclusive public sector involvement. In practice, however, significant traces of investment control still remain. These controls arise mainly due to (1) lack of transparent and well-designed guidelines about which industries qualify as regulated ones and about the procedures used for industrial regulation; (2) some ambiguity remaining in the revised 1991 Industrial Policy about how to deal with credit for investment in industries which appear to have reached market saturation; (3) some regulatory functions that can be exercised by the industrial promotion agencies; and (4) some special de jure and/or de facto controls on foreign investment.

04. Existing uncertainty and lack of transparency about which industries need clearance on environmental grounds and about the approval criteria and procedures of such regulation leave some scope to the investment registering authorities, the investment financing institutions and the Environment Department to apply discretionary powers in designating industries as requiring environmental clearance, thus creating scope for unnecessary delay or other forms of control on investment including rent seeking opportunities for the organizations involved in the clearance process. Environmental clearance entails a lengthy process starting with a site clearance requirement from local authorities.

05. The 1991 Industrial Policy discourages the production of jute substitute synthetic fibers, especially polypropylene bags by imposing high tariffs on related imports and by ensuring compulsory use of jute bags for packing of food grains, sugar, cement, fertilizer, etc. Guided by this Industrial Policy directive, a tacit ban has been in place on new capacity creation for the production of polypropylene bags. And recently (late October, 1993), the Government has come out with explicit directives that, except in Export Processing Zones (EPZs), no new capacity will be permitted to produce polythene shopping bags and also that existing production of such bags must cease from January, 1994 (giving effect to the latter decision has been deferred). Such investment and production controls, which appear to be primarily motivated on considerations of protection to jute goods, are undesirable. While there may be some grounds for concern from an environmental perspective, the direct prohibition will only encourage smuggling of such goods at the expense of domestic production.

06. There is a ban in place on investment in fishing trawlers exceeding a specified number, specifically, seventy three. This ban imposed a long time ago, on an environmental consideration about over-fishing, is worth reviewing to determine if it is still an appropriate form of control.

07. The pharmaceutical industry is subject to a plethora of controls in addition to a ban on the production of many of its products. These controls are impeding further investment and growth of this industry.

08. The Board of Investment (BOI) has informed financing institutions of an over-capacity in the production capability of the edible oil refining industry. This was because of the Industrial Policy guideline that industrial sponsoring and development financing institutions ensure that market over-saturation does not occur in any sector due to new private investment. The Industrial Policy further mentions that the agencies concerned will provide correct statistics and survey reports on existing and future market demands and developments and on existing and future production capacities. The BOI is currently considering other industries such as electric fans, corrugated iron sheets, mild steel rods, and single-phase electric meters for inclusion in the over-saturated category. While most potential investors would welcome information about the degree of market saturation as an input into their investment decision, the use of this information as a control on investment credit is a disguised form of reinstatement of the old Discouraged List which was scrapped to

remove controls on investment. Investment credit risks are best left to the investor and his bank. The ambiguity left by the Industrial Policy should be cleared.

09. As an authority which registers investments in medium and large-scale industries and all foreign investments outside the EPZs, the BOI exercises in practice significant regulatory powers in the discharge of several functions imposed on it by higher authority. The BOI provides recommendations on imported input requirements of industries to the import control authority; it issues a passbook incorporating its approved technology transfer-related remittances of industries and remittances on account of consultancy fees and overseas training costs; it considers requests for foreign borrowing by industries outside the range of terms used for automatic approval of such borrowing; and it provides an employment contract to expatriate employees incorporating the company-approved remunerations and the allowable remittances of their savings in foreign exchange. Complaints are heard from some private investors, both local and foreign, about the delays and/or side costs involved in these processes. Under a technical assistance project, the BOI's functions are being recast and it is being reorganized to enable it to perform as a promotional rather than a regulatory agency. Most of the regulatory functions it now performs should be taken away to transform it into an effective promotional agency. Until recently, the BOI's function of registering new industrial projects was also regulatory: the registration required proof that investment was in progress. This registration function has, since March 1, 1994, been made automatic and simplified, a reform which was recommended in the earlier version of this report and which has resulted in a dramatic increase in the registration of new industrial investment with the BOI.

10. Even though the Foreign Investment Act does not allow discrimination between domestic and foreign investors, foreign investments in some industries are subject to special de jure or de facto controls. For example, they are barred from investing in certain pharmaceutical product ranges. Their investments in readymade garments are also subject to certain restrictions. They are not freely allowed to import any items commercially even though such items are commercially freely importable by Bangladesh nationals.

11. Foreign investors report that they are affected by other factors such as lack of or weak enforcement of patents and trade marks and the relative difficulty they face in winding up business and repatriating their invested capital. In the latter case, the permission required for repatriation from the Bangladesh Bank is a remaining unnecessary irritant to the foreign investors. There was a permission requirement also from the Securities and Exchange Commission for transfer of shares, but this requirement has been recently withdrawn by this Commission following a recommendation to this effect which was made in the earlier version of this report.

12. A general control on investment remains because of a restriction that import of second hand or reconditioned machinery above the value of Tk 200,000 requires a surveyor's certification that the machinery has a minimum economic life of 10 years. Other controls on private investment are in the forms of obstacles to investing in sectors newly opened for the private sector and in

dealing with an inefficient and difficult customs administration. Currently gas prices are differentiated according to whether the gas is used in public power generation or in industry. Higher prices charged for private power generation, which is treated as an industry, discriminates against private investment in power generation. Although, no official permission is required for industrial investments, private investment in financial institutions and insurance companies requires official sanction and is subject to rigorous Government control as it should be.

## Exchange Controls

13. During the last two fiscal years and the few months of the current fiscal year, the Government has moved swiftly to introduce relaxation of existing controls on the use of foreign exchange. For several types of foreign exchange transactions, transparent Bangladesh Bank (BB) or BOI guidelines have been established and the requirement of prior BB permission has been withdrawn. Around mid-October last, the Government also declared the Taka as fully convertible for permissible current account foreign exchange transactions. However, the Taka remains on a managed float basis as before.

14. Some of the exchange control liberalizations introduced prior to the Taka convertibility measure include:

- a) Allowing exporters to retain 5 to 10<sup>1</sup> per cent of earned foreign exchange.
- b) Allowing increased foreign exchange for business and personal travels.
- c) Allowing certain miscellaneous foreign exchange business transactions and allowances.
- d) Withdrawal of restrictions on non-residents' portfolio investments.

15. The foreign exchange liberalization has not, however, gone as far as it could. The areas of exchange control still remaining are as follows:

- a) Private borrowing from abroad on terms outside those set for automatic authorization is subject to approval by the BOI. Such cases seem to be marginal. It, therefore, makes little sense to make these loans subject to BOI control.

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<sup>1</sup> Raised to 15 as "the printing presses were rolling".

- b) Foreign exchange retention benefits allowed to exporters are not of much value to them since such retention allowed, in a special account, are not allowed both-way convertibility, even after the Taka has been made "convertible".
- c) Foreign exchange is not generally available for imports on non-letter of credit basis.
- d) While Bangladesh nationals living abroad are allowed to import against direct payments abroad, this privilege is not explicitly available to foreign investors.
- e) Current though relaxed restrictions on personal and business trips are still too restrictive.
- f) Unnecessary restrictions remain on educational tours or those for seminars and workshops, etc.
- g) There remains an unnecessary restriction on imports with cash foreign exchange for those who import on a back-to-back letter of credit (LC) basis such as the garments and leather industries.

16. Current remaining restrictions in the form of quantitative restrictions and high tariffs translate into a substantial degree of exchange control. This control combined with other remaining exchange controls, including controls on capital transfers, highly circumscribe the benefits that can be reaped from the Taka convertibility. Taka convertibility has been made largely meaningless because Taka has not been put on a free float against other currencies and in practice it is not convertible except under clearly defined circumstances.

### **Quantitative Controls on Imports**

17. The Government has made substantial recent progress in the phasing-out of quantitative restrictions (QRs) on imports as an important first step toward import liberalization. In the new Import Policy Order 1993-95 incorporating changes announced last October, QRs remain on only 110 four-digit harmonized systems (HS) code items among which eight contain only inspection requirements and 47 of the others are for non-trade reasons. This is a considerable improvement from the situation at the end of FY 1991-92, when nearly one-fifth of all trade items at eight-digit level were subject to QRs.

18. Remaining QRs which are for trade reasons, and number 55 at the four-digit level, including 14 for pharmaceutical products, should be removed. Only those QRs which can be justified on non-trade reasons of health, religion or safety should be continued. Among the domestic industries currently being protected by import QRs are pharmaceutical products and some of their

raw materials, grey and finished textile fabrics, sugar, newsprint, salt, films, some electronics, engineering and metal products and some transport equipment.

## **Export Controls**

19. Despite the Government's stated export-oriented stance and recent liberalizing changes, a few controls still remain. These include controls on (1) the re-exporting business, (2) exports and imports of samples for export purposes and (3) an export ban on a number of goods for trade reasons.

20. Re-exporting of imports has been recently allowed on a limited scale for goods not produced within the country for export purposes. These are subject to the goods having a minimum 15 percent export over import price and prior permission for re-export from the Ministry of Commerce. The limitations and conditions attached to this trade are unnecessarily restrictive.

21. To receive export privileges, a minimum of 30 per cent local value addition was being required for all woven garments until recently. This restriction has now been relaxed to 25 per cent for all non-quota categories of woven garments and for those quota categories of woven garments whose fob value per dozen is above US\$ 40. This is a welcome reform. However, the rationale for the distinction being maintained now between quota and non-quota garments is unclear.

22. Exports of samples are subject to value ceilings and require prior clearance from the Export Promotion Bureau (EPB) and, in some cases, also from the Chief Controller of Imports and Exports (CCIE). Both value controls and permission requirements are unhelpful restrictions on export trade. Similarly, imports of samples beyond certain limits, to copy for export purposes, are subject to prior approval from the CCIE on recommendation from the EPB while lower amounts are subject to clearance from the EPB only. All these restrictions seem unnecessary unless the items are on the restricted import list.

23. An export ban for trade reasons remains on a few agricultural products such as wheat, pulses, onion, jute and sunn-hemp seeds, unprocessed prawns and shrimp, whole bamboo and cane, and a few manufactured and processed products such as ferrous and non-ferrous metals and their scraps, petroleum and petroleum products except naphtha and furnace oil, 'gur' and khandseri sugar, rice bran except de-oiled type, and wooden logs. Exports of oil seeds and milk, molasses, de-oiled rice bran, wheat bran, and stainless steel scrap require prior clearance from the Ministry of Commerce. These export bans and restrictions are harmful to the country's export industry as well as to agriculture.

24. Other controls on exports include (1) a ban on exporting on consignment basis except for perishable goods, (2) a ban on exports of jute yarn by composite jute mills producing woven jute products, and (3) reportedly, a recalcitrant attitude of customs toward clearing imported goods for re-exporting purposes without the importer first having to make an unrequired duty payment. These controls and restrictions are also inappropriate and deserve to be withdrawn.

## **Banking Regulations**

25. Significant progress has been made in recent years in financial deregulation. Except for regulations which are required for prudential and supervisory purposes, the central bank controls on financial transactions have been largely eliminated and the terms of such transactions are left to the banks and their customers. However, there still remain a few regulations which are counter to the principles of free enterprise operations and competitive market economy requirements.

26. Interest rates on bank lending and deposits have been deregulated, with some exceptions maintained for lending to three sectors, - - agriculture, exports and small and cottage industries - - and for term and savings account deposits. Specified interest rate bands are being maintained for lending to the three referenced sectors and floor rates are maintained on the terms and savings deposits. Lifting of these remaining restrictions is worth consideration to complete interest rate deregulation.

27. Government or central bank directed credit has been largely discontinued with a few exceptions. The Government continues to direct its owned nationalized commercial banks (NCBs) to lend to the jute sector. This directed credit is reportedly linked to the restructuring of the jute sector now in process as an interim arrangement. Serious effort should be made to phase out this credit arrangement as quickly as possible.

28. Other types of bank credit which still remain subject to Bangladesh Bank controls include some personal loans, the provision of L/Cs to bank loan defaulters, and advances against hire purchase with some exceptions. To control some of this credit, BB has specified margin requirements and/or repayment periods. Most of the controls deserve to be fully removed. In the case of L/C restriction for bank loan defaulters, consideration may be given to allowing the banks flexibility to use loan rescheduling or temporary moratorium measures on existing loan defaults to meet genuine business credit needs where defaulters are suffering temporary cash liquidity crunches. Also, in the case of lending for hire purchase purposes, while the current ban should not apply to hire purchase for trading purposes, its application to consumption loans may be considered as in order in view of low savings in the economy.

29. Interest rates are not, in practice, satisfactorily liberalized because of the oligopolistic market structure of banks and the inefficiency of the NCBs. To increase competitiveness in the financial sector, the Government should actively encourage entry and growth of private banks.

## **Labor Regulations**

30. Streamlining existing labor laws and enhancing the effectiveness of their enforcement are critical needs for improving labor-market efficiency and ensuring a sustained period of good labor-management relations. These are essential prerequisites for an environment conducive to private sector development. Labor regulations and practices affect wages, other employment and termination terms, the labor dispute resolution process and general labor-management relations.

31. Trade unionism is currently allowed outside the Export Processing Zones (EPZs). As the labor conditions in these zones are far better than those outside, ideas of extending unionism rights to these workers would be premature at the current stage of development when Bangladesh is in dire need of foreign investment.

32. The current regulation, which allows retrenched or terminated workers of an establishment to become members or office bearers of the establishment's trade union, contributes to an unhealthy pattern of unionism. This regulation should be removed.

33. Current regulations allow formation of three trade unions in an establishment, each union requiring a minimum support of only 30 per cent of the workers. It would be desirable to reduce this multiplicity of unions and allow only one union, with majority worker support, to represent the workers in an establishment. This should help depoliticize union activity as well as place the representative union in a stronger bargaining position.

34. The regulations currently impose a restriction which does not allow employers to change the service conditions of union executives during the time an application for union registration is pending. This restriction needs to be modified by providing a time limit for registration.

35. Current regulations oblige employers to pay compensation in terms of gratuity and employer's contribution to the provident fund to workers dismissed on disciplinary grounds. The relevant regulation needs to be suitably amended to exclude dismissed workers from benefiting from full compensation.

36. Current regulations do not provide for sufficient flexibility in the type of employment contracts and hence should be amended to allow employment of workers on a fixed-term contract basis.

37. The laws do not appropriately define wages for determining overtime allowance and provide for excessive compensation for work on festival days. These laws should be appropriately reformed.

38. Currently private sector wages are affected (1) by the collective bargaining process exercised by labor unions, (2) by minimum wages set by the Minimum Wages Board for private sector workers in different industries, and (3) indirectly by minimum wages set by the Government for public sector workers. A national minimum wage has been recommended by the National Wages and Productivity Commission which, if put into effect, would increase private sector wages. The practice of centralized wage determination, in disregard to industry's productivity and profitability, has resulted in insupportable increases in labor costs in Bangladesh. This has adversely affected industry's profitability and competitiveness as well as labor's prospects for jobs. The practice has ignored the plight of the vast pool of unemployed and underemployed labor who are finding it difficult to obtain any kind of job in the formal sector. The National Wages Commission's recommended national minimum wage at Tk 900 per month is 17 per cent higher than the current average of private sector wages and as much as 30 per cent higher than wages in some key sectors like readymade garments. It would be undesirable to put into effect such a high minimum wage in the face of the unemployment and underemployment levels that currently exist in the country.

39. The labor management dispute resolution process is currently delayed due to loopholes in the law. The process should be expedited by assigning time limits at each stage of the dispute resolution process: direct labor-management negotiation; tripartite conciliation involving labor, management and the Government Labor Department; arbitration by an arbitration authority; settlement by labor courts; etc. Also, the requirement, for a joint labor-employer referral of a dispute to a labor court for adjudication upon failure of conciliation proceedings, should be rewritten to enable such a referral by a single party.

40. The labor market has been adversely affected by Government interference in labor disputes. The legal clause giving the Government the right of interference in labor disputes should be appropriately amended to proscribe such acts as forcing the employer of a firm to end a lock-out or to re-open a factory if it is unilaterally declared as closed on the basis of unprofitability. The Government should also not interfere in wage negotiations outside the legally prescribed procedures, but allow the bilateral collective bargaining process to fully take hold.

41. Enforcement of labor legislation should be enhanced by strengthening the Labor Department, further streamlining labor court procedures, penalizing illegal strikes and lock-outs in accordance with the law and introducing and ensuring enforcement of necessary job security measures for workers, e.g., ensuring that workers are provided with appointment letters incorporating employment and termination terms and, when their jobs are terminated, requiring employers to provide them with termination compensation in accordance with the law.

## Legal Reform Issues

42. The existing legal system is deficient in providing effective support to the conduct of orderly business transactions such as enabling enforcement of contracts, resolving disputes and providing for the orderly exit of unprofitable business activities. A start has been made by the Government in reforming the legal system. Reforms in this area need to be accelerated to create a congenial legal environment for private sector business and to promote industrialization based on foreign investment and growing international trade.

43. Recent initiatives taken by the Government to improve the legal framework include: (1) enactment of the Banking Companies Act, 1991 which provides for the central bank's supervisory control over private banks' lending to single borrowers, (2) enactment of the Financial Institutions Act, 1993 providing for the central bank's prudential control over non-banking financial institutions, (3) enactment of the Industrial Relations (Amendment) Act, 1993 providing for speedier disposal of labor disputes in labor courts by allowing the courts to proceed with cases even in the absence of the disputing parties, (4) preparation of a draft of the Companies Act (Amendment), 1913<sup>2</sup> which addresses deficiencies in the existing Act to meet modern-day requirements of corporate business, (5) preparation of a draft amendment to the Bankruptcy Act (Amendment), 1920 to provide for orderly exit of unprofitable business activities, (6) establishment of the Securities and Exchange Commission to improve capital market operations, and (7) formation of the National Labor Law Commission. Other steps taken include establishment of special loan courts to help recover bank loans and the appointment of committees for updating other laws such as the Foreign Private Investment (Promotion and Protection) Act, 1980 and the existing Patents and Trademark Laws.

44. Further actions needed to accelerate legal reform are expeditious finalization and enactment of the amendments to the Companies Act, 1913, the Bankruptcy Act, 1920, the Foreign Investment Act, 1980, and laws relating to patents and trademarks and consideration of a number of other recommendations made by the Foreign Investment Advisory Service (FIAS) for implementation.

## Industry-Specific Regulations

45. At least three industries are currently adversely affected by specific regulations. These are pharmaceutical products, 'gur' and readymade garments.

46. The pharmaceutical industry has been subjected to many economically undesirable regulations, such as bans on the production and import of many drugs, special production controls for foreign firms, quantity and price controls on imports of raw materials, controls on product prices and on advertising expenses. These controls are currently being reviewed by a Government Committee. The review should be done on a priority basis to free the industry from these unhealthy

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2 The Act was passed by Parliament as "the printing presses were rolling".

for foreign firms, quantity and price controls on imports of raw materials, controls on product prices and on advertising expenses. These controls are currently being reviewed by a Government Committee. The review should be done on a priority basis to free the industry from these unhealthy controls.

47. There is a ban on the crushing of sugarcane in specified sugar mill zones to restrict 'gur' production and protect sugar production. Such a control is economically unjustified.

48. The readymade garment industry is currently adversely affected by two regulations. First, the garment manufacturers are only allowed to import on a back-to-back L/C basis. They are not allowed to meet even part of their import requirement by drawing on their retained 5 per cent foreign exchange. Second, they are not allowed to import grey fabrics unless they have their own dyeing and finishing facilities. These restrictions are inappropriate and unnecessary.



# 1. INTRODUCTION

1.1 During the past decade, Bangladesh has progressively made a fundamental shift from what was a tightly regulated and state-dominated economic framework to one with a greater market orientation and greater reliance on the private sector. The latter has been described as the new engine for economic growth. Economic policy reforms have accelerated in recent years and months especially after a liberal industrial policy was adopted by the new Government and announced in FY 1991-92 under the name of "Industrial Policy 1991" (GOB-1, 1991). This policy underwent some revision incorporating further liberalizing features, and the new version (incorporating revision up to December 1992) was published recently (GOB-2, 1992).

1.2 Despite these reforms, the performance of the industrial sector has remained poor throughout much of the eighties and early nineties and there is no sign of industrial growth and investment picking up significantly. During much of this period, industrial growth has been at a moderate rate of about 4 percent. Private investment as a percentage of GDP, an indicator of the dynamism of the private sector in the economy, has been stagnant at around 6 percent, and rose to only 7 percent last year. Private investment has been well below the average for other South Asian economies and even below the average for Sub-Saharan Africa (FIAS, 1992). Bangladesh has been able to attract little foreign direct investment (FDI). FDI flows have averaged only three to four million US dollar on an annual basis in recent years. This is in sharp contrast to the FDI flows that some of Bangladesh's neighboring and similarly situated countries like Pakistan, Sri Lanka, Thailand and Vietnam, have been receiving.

1.3 Apparently, private investors still do not view the business climate in Bangladesh as conducive or attractive enough for investing. The perceived constraints to private domestic and foreign investment are attributable to a whole host of factors such as inadequate financing; infrastructural deficiencies; labor problems and government wage policies; administrative, bureaucratic and legal problems; a controlled and questionable trade policy and foreign exchange regime; a high tax, high incentives but unstable tax regime; poor public enterprise performance; slow privatization initiatives; and last but not least, the dramatically increasing world-wide competition for industrial investment.

1.4 The Government economic reform process is being supported by several donor agency assistance programs, the most notable of which is the World Bank's Second Industrial Sector Adjustment Credit (ISAC-2) program. The Government has embarked upon a program of further economic policy reforms in such areas as import liberalization and tariff reform, export promotion, investment deregulation, reform of the foreign exchange regime, etc. As part of this program, PIAG has undertaken this study to identify regulatory problems that continue to adversely affect industrial investment and performance in Bangladesh.

1.5 The goal of this study is to survey the key elements of the regulatory framework for industry to provide a clear indication of where Bangladesh stands with respect to the process of implementing regulatory policy reform. The objectives are to:

- a) Identify areas where deregulations, aimed at opening up markets and creating a competitive economy, have been accomplished in law, but not in fact;
- b) Identify the obstacles to effective implementation;
- c) Develop an action plan to overcome these obstacles;
- d) Identify other areas where unnecessary regulations remain in effect; and
- e) Devise further initiatives at deregulation.

Particular areas that will be covered under these sub-tasks include:

- Quantitative restrictions on imports;
- Exchange controls;
- Investment controls;
- Export controls;
- Labor regulations;
- Banking regulations;
- Legal reform issues; and
- Industry-specific regulations.

The study also attempts to identify, in some of these areas (e.g., import controls and banking regulations), those regulatory policies that may be retained or introduced on reasons of health, public safety or on other legitimate grounds, e.g., environmental concerns but does not go into the details of such regulatory concerns. The terms of reference of this study, which were prepared by the PIAG contractor, International Management and Communications Corporation (IMCC), in consultation with USAID, Dhaka and the World Bank and approved by the Ministry of Industries, is reproduced as Attachment 1.

1.6 The study is commensurate with PIAG's objectives and represents Task 1 of PIAG's first-year work program. This study will result in an Operative Regulatory System (ORS) document which will provide a comprehensive overview of the regulatory system. The document, which can be updated from time and time, will hopefully increase the transparency to Government policies.

1.7 To carry out this study, up-to-date information relating to various regulations was collected from all concerned offices such as the Board of Investment, Ministry of Commerce, Bangladesh Bank, a commercial bank, Environment Department, Drugs Administration, and National Labor Law Commission. In addition, information was available also from the World Bank Resident Mission and the Metropolitan Chamber of Commerce and Industry. A mini survey was conducted to determine

private sector perceptions of the problems they face from regulations or laws in place, from regulatory practices and from their administration or enforcement or from lack of or weak enforcement of such policies. For the private sector survey, the terms of reference for the study were used as a guide. Business organizations and firms with the names of persons interviewed are listed in Attachment 2. The sample of firms visited was not a random one. For convenience, the sample was taken from among firms the offices of which are located within the metropolitan area of Dhaka city. The firms are from a cross-section of industries and some of them are from multinational/joint-venture groups. A few were chosen from the list of those who recently registered with the Board of Investment. The choice of firms was dictated in part to meet persons in industry who are reputed to be knowledgeable about policy issues affecting the private sector. One visible deficiency of the surveyed group is that it poorly represents small-scale enterprises. This is thought not to be a serious omission since the regulatory problems being faced by the large firms are similar to those faced by small ones. Possibly small firms, however, are more disadvantaged by regulatory constraints than the large ones.

1.8 The remainder of this report is organized as follows. Since business start-up problems should be dealt with first, investment controls are looked at in Chapter 2. This is followed in Chapter 3 by an analysis of foreign exchange regulations. Chapters 4 and 5 respectively take up import controls and export controls. Banking regulations and labor regulations are analyzed respectively in Chapters 6 and 7. Chapter 8 briefly examines legal reform issues. This is an area where substantial work has already been done by the Foreign Investment Advisory Service (FIAS). In Chapter 9, some industry-specific regulations are analyzed. Finally, in Chapter 10, a summarized and consolidated set of specific recommendations are offered.

## **2. INVESTMENT CONTROLS**

### **2.A. Deregulation of Investment Controls**

2.1 A series of measures undertaken in the past has led to progressive elimination of controls on private investment. These measures have been mainly two-pronged: (1) widening the areas for private investment by reducing those exclusively reserved for the public sector and (2) relaxing / liberalizing the investment approval / sanctioning process. In both cases, commendable progress has been made to date. There has also been substantial success in deregulation/improvement in other areas which directly or indirectly affect domestic and foreign private investment.

2.2 The most notable feature of current industrial policy is that private investors investing outside the export processing zones (EPZs) are no longer required to take any formal approval from Government authorities to invest in new industries or to invest in replacement/modernization or expansion of existing plants if such industries are not pre-empted by the Reserved List or regulated sectors. Even registration of such investments with the designated Government authorities is not mandatory at present. However, registration is required if the investors want to avail themselves of the benefit of importing machinery at a special duty concession and/or some other facilities like import entitlement benefits, access to public land, etc. Outside the EPZs, the government offices authorized to register industries have been reduced to two: the Board of Investment (BOI) for medium and large industries and Bangladesh Small and Cottage Industries Corporation (BSCIC) for other industries. For investing in EPZs, the Bangladesh Export Processing Zone Authority (BEPZA) has been authorized not only to register but also to approve such projects.

2.3 Currently, the industries reserved for exclusive public sector involvement remain limited to five groups:

- a) Arms, ammunition, defence equipment and machinery;
- b) Nuclear energy (production);
- c) Security printing (printing of money and minting);
- d) Forest plantation and the mechanical extraction of timber in the reserved forest areas;  
and
- e) Railway and international air transport.

Recent changes include removal from the Reserved List of power and telecommunication sectors and just lately of air transport in domestic routes other than those where the government-owned airline operates.

2.4 Certain recent procedural simplification and other regulatory changes in other areas have also contributed to an improvement in the investment climate. These changes include the following:

- a) Removal of the requirement of prior central bank (Bangladesh Bank) approval for:
  - i) Foreign borrowings including suppliers' credits if the terms are within the Board of Investment-set guidelines;
  - ii) Remittances on account of royalties, technical fees and training within the BOI guidelines;
  - iii) Remittances on account of dividends and capital gains subject to advance withholding of tax, if any;
  - iv) Remittances on account of savings of expatriate personnel within BOI guidelines as approved and specified in the employment contract issued by the BOI for each foreign firm;
  - v) Foreign investors to invest in or disinvest stocks and shares traded in the Dhaka Stock Exchange; and
  - vi) Foreign investors to borrow term and working capital loans from banks;
- b) Exemption of income tax on capital gains on government securities and stocks and shares traded in the stock exchange;
- c) Easing of the procedure of issuing work permits to expatriate personnel with multiple-entry visas;
- d) Abolition of the mandatory requirement of newly floated companies to register as public limited companies when their capital amount exceeded a certain limit;
- e) Certain other foreign exchange control relaxation and some import policy procedure simplifications (these are discussed below under foreign exchange and import controls); and
- f) Lately, introduction of an automatic and simple process of registration of private industrial investments with the Board of Investment.

2.5 The simple and automatic registration process, introduced since the beginning of March this year, replaced an earlier system which required proof that investment was in progress (e.g., papers showing land purchases and machinery orders). The earlier versions of this PIAG report recommended the replacement of the earlier system into a simple automatic one. It is heartening to note that this single regulatory reform has produced a very positive investor response : the intended

foreign investments registered with the BOI in the very first few months of the reform far outweigh those registered during the previous three years.

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## **2.B. Traces of Still Remaining Investment Control**

2.6 The above investment deregulation measures amount to a revolutionary change in the current industrial policy of the country and have made it theoretically at least very liberal. However, discussions with industrial entrepreneurs reveal that the investment climate is not so liberal in practice, especially for foreign investors. Significant traces of direct or indirect control on private investment still remain, which take place due to non-definition or ill-definition of regulated sectors and lack of transparency and complexity of regulatory procedures and due to miscellaneous other reasons. These are outlined below.

2.7 A significant source of control on private investment arises from the uncertainties about which industries are regulated and what discretionary powers are held by the BOI and the Environment Department in designating industries for regulation on environmental grounds. Neither the 1991 Industrial Policy nor the 1992 Environment Policy and Implementation Program clearly spells out which industries need clearance on environmental grounds. For those projects for which regulation is required on environmental grounds, the Environment Department must provide approvals. But again, there are no set guidelines formulated or in practice regarding the approval process. The Environment Department (ED) reports that it has prepared guidelines which are under the consideration by the Government (Environment Ministry). The situation that stands at present, however, is that (1) the Bangladesh Export Processing Zones Authority (BEPZA) sends all projects to the ED for an opinion on the need for an approval on environmental grounds; (2) the BOI does not send all project proposals for ED's opinion but applies discretion: in some cases it sends the proposals to the ED and in other cases it advises the investors to themselves go to the ED for their clearance; (3) in the case of bank-financed projects, banks also apply discretion in this regard. This lack of transparency about (1) what industries need to be cleared for environment reasons and (2) what the approval criteria are, creates scope for both the investment registering authorities and the ED to have rent-seeking opportunities. The current problems being faced by industrial projects on environmental grounds can be illustrated by one example narrated to the author by a former Managing Director of the Bangladesh Shilpo Bank (BSB).

The sponsors of a BSB-sanctioned zipper making project were told that the project would require clearance from the ED and to obtain this an environmental impact statement from a consultant would be required. The firm was told that this examination would cost Tk 150,000 and it would take 3 months. However, when the BSB Managing Director spoke to Secretary of the Ministry of Environment about the undue demands placed on this firm, the problem was quickly resolved.

In certain industries, reportedly, all new projects require site clearance. These are industries such as tanneries, cigarette manufactures, oil refineries, industrial spirit production, industries based on industrial wastes, and manufactures of polythene/polypropylene sheets/bags, and cement and

industrial chemical manufactures. The current site clearance procedure required by ED for most projects is reported by entrepreneurs to be an irritating lengthy process where they have to procure clearance first from local authorities. They report that these clearance certificates can be obtained by sizeable unofficial payments to the concerned officials.

2.8 The purport of the above documentation is definitely not to suggest that environmental aspects of industrial projects, which are often an important social consideration, should be slighted. However, it is crucially important for a poor developing country such as Bangladesh that the delays and costs of investment which are associated with environmental regulations are held to a minimum. Currently investment is being delayed or has to bear a significant additional cost due to lack of clear-cut and sensible environmental regulations. It is, therefore, very important that the Government (Environment Ministry/Department) quickly come out with clear-cut policy guidelines on such regulations.

2.9 A second current source of control emanates from the existing unnecessary restriction on imports of second-hand/reconditioned machinery. Such machinery worth over Tk 200,000 requires a certification from an international surveyor that it has at least a ten-year economic life. The current restriction is founded on an unnecessary Government concern for a need to guard against imports of junks and flight of capital. The decision to judge the usefulness of a piece of machinery should be best left to the private investors whose vital stakes are involved.

2.10 A third element of investment control arises due to de jure and/or de facto controls being applied to some industries. The (revised) 1991 Industrial Policy requires industrial promotion agencies to ensure against over-saturation of particular industries through new private investment by providing relevant information on present and future market demand and existing and future production capacities. Accordingly, the BOI has reportedly advised financing institutions not to finance investment in edible oil refining because the BOI believes the market is saturated. The BOI is reportedly considering also other industries such as electric fans, corrugated iron sheets, mild steel rods and single-phase electric meters for inclusion in the over-saturated category. Such control is reinstatement in disguise of the old Discouraged List of Industries which was scrapped to remove controls on investment. While information on market demand and production capacity is a valuable input into the private investor's decision making, his decision on investment is best left to him and his banker. The ambiguity remaining in the Industrial Policy needs to be cleared up.

2.11 In the seminar held to discuss this report, some commentators thought that the report downplayed the need for information on the market situation of industries. Some also felt that the investment financing institutions lacked expertise to appraise industrial projects without such information. However, it needs to be recognized that although available market information can be a valuable help to both investors and bankers, it is not always a sure guide to investors. For one thing, an investor may indeed like to invest in a product the market for which may apparently look saturated. The investor may have a **better product** or a **cheaper one** in mind which he can produce and market with a **superior technology**. Thus to block investments in a so-called saturated market would amount to discouraging technological progress and dynamic development in the

economy. Hence any controls on investment on the basis of market information are economically unjustified.

2.12 The Industrial Policy discourages the production of jute substitute synthetic fibers, especially polypropylene bags by imposing high tariffs on related imports and by ensuring compulsory use of jute bags for packing of food grains, sugar, cement, fertilizer, etc. Guided by this Industrial Policy directive, a tacit ban has been in place on new capacity creation for the production of polypropylene bags. The Government decided in October 1993 to impose an explicit ban on the production of polythene shopping bags by existing units to be effective from January 1994. This latter ban has been suspended later by a Cabinet decision. The ban on investment on new capacity creation and the threatened ban on production seem to have stemmed more from concerns over polypropylene bags presenting competition to jute bags than to any environmental consideration which is given as the official reason. Such production and investment bans are not defensible on sound economic logic if private sector-oriented free market philosophy is to be followed as was professed by the 1991 Industrial Policy to maximize economic growth. The edible oil refining industry was, until recently, saddled with another kind of control which indirectly affected its ability to expand or restructure along optimal lines. The established industries were given entitlement to import only a small fraction (only 4.5 percent during January-June 1993) of total unrefined oil required for full capacity operation. Such control on imports of industrial raw materials cannot be economically justified. It is a definite deterrent to investment in a new factory. In this particular case, the import restriction reportedly prompted the owners of established industries to either artificially inflate their real production capacities or to make further incremental investment in some auxiliary machinery to augment capacity and thereby to secure a greater import entitlement. This was a perverse effect of the import control.

2.13 The National Drug Policy as adopted under the Drugs (Control) Ordinance of 1982, cancelled or suspended the registration of 1,666 harmful, unnecessary or otherwise undesirable drugs and these products were gradually withdrawn from the market. Although this Policy has yielded some undeniably positive results (e.g., relatively greater production of essential drugs and elimination of harmful drugs on health grounds), it has also given rise to certain economically undesirable outcomes. A fuller discussion of this Policy and the accompanying controls on the pharmaceutical industry will be provided in the chapter on industry-specific controls. Here, a few things that are worth noting in the context of investment control are mentioned as follows:

- a) Some of the banned drugs fall into a category of internationally recognized safe drugs. Illegal imports of these are occurring on a wide scale. The current policy, therefore, has arbitrarily limited pharmaceutical products that can be manufactured in Bangladesh, while encouraging smuggling.
- b) The Drug Policy discriminates against foreign companies as they are barred from producing certain product ranges of some medicines, which include their own foreign brand name products, when the same or similar products are available or are manufactured in Bangladesh. This is a clear contradiction of the Foreign Investment Act clause that offers equal treatment to domestic and foreign investors.

- c) The Policy also bans imports of pharmaceutical raw materials or their substitutes to protect local production of such materials. This sort of ban is economically unjustifiable as it discourages desirable investment in some of the pharmaceutical products and prevents the expansion and growth of the industry along the most economical lines.
- d) The Policy has also led to imposition of price and quantity controls on pharmaceutical raw materials and price controls on finished products. These are administered by the Drugs Administration. These controls do not stand scrutiny on economic grounds as they discourage the production of quality medicines and production up to a free market demand.

2.14 Recognizing the need for reviewing the Drug Policy, a committee was formed by the Health Ministry in 1992 to review this Policy and the Drug (Control) Ordinance, 1982. However, towards the end of 1992, an order from the High Court led to suspension of the Committee's work. The Government has recently appointed a new committee to revive this review work. This review should be completed on a priority basis.

2.15 A fourth source of control on investment arises because the investment registering authorities also perform the functions of determining the production capacities and required raw material import entitlements for each firm and then of recommending these to the Chief Controller of Imports and Exports (CCIE) for issuing a Passbook to the firm for industrial imports. The current import policy requires the Passbook only for those import items which are in the restricted import category. The Import Policy Order explicitly mentions that import of freely importable items does not require the Passbook except in the case of import by readymade garments, hosiery and specialized textile industries operating under the bonded warehouse system and pharmaceutical (allopathic) industries. Outside these exceptional cases, imports of restricted import- category items are restricted according to the entitlements approved and specified in the Passbook. However, there are reports that manufacturers using Passbooks issued previously by the CCIE, wherein import entitlements for also freely importable items are specified, are facing difficulties with customs in importing higher than specified amounts of such imports. It will, therefore, be desirable for the CCIE to recall all old Passbooks and replace them with new ones where only restricted import items are listed. In addition, consideration should be given to transferring the function of recommending input requirements of firms from the BOI to the Ministry of Commerce in consultation with the chambers of commerce and industry.

2.16 A fifth kind of control on investment is exercised by the BOI through the review of proposals for foreign borrowings when their terms are not within the BOI-set guidelines for requiring no prior BOI approval of such loans. Reportedly, such proposals coming to the BOI are marginal. The author was informed of only two such cases during less than a year after the new guidelines had been introduced. In both cases, the requests for foreign loans were rejected by the BOI. The controls currently in place on foreign exchange borrowings will be discussed in more detail in the next chapter on foreign exchange regulations. The point that can be made here is that the controls that still remain on such borrowings by private investors, and which hardly make sense on close scrutiny, work as

some disincentive to both local and foreign private investment.

2.17 A sixth source of control on investment is exercised through the requirement that investors procure a special passbook from the BOI for the remittances they can effect on account of royalties, technical know-how and technical assistance fees, consultancy fees and overseas training costs. The passbook is kept with a bank nominated by the firm and the firm can send remittances on the above accounts unto the prescribed limits. These controls on foreign exchange remittances will be discussed in more detail in the chapter on foreign exchange regulations.

2.18 Foreign investors are required by the BOI to also obtain an Employment Contract wherein the salaries paid by the firm to its expatriate personnel are approved and noted after such salaries are verified by the company's board of directors or by its chief executive officer. The Employment Contract enables the firm's employees to send foreign exchange out of the country equivalent to a specified percent of their regular salaries plus their other savings.

2.19 The current regulations and some practices of the BOI continue to be regulation-minded. The BOI has not yet fully made a switch from a regulatory to a promotional role, although the original purpose for its establishment was promotional in nature. Complaints are heard from some private investors, both local and foreign, about the delays and/or side costs involved in getting things done at the BOI. To give an example, a foreign firm reported that for its recent registration of a new investment with the BOI, the organization asked about foreign equity holdings and other things, The firm had to talk to one of its members to expedite the registration process; yet it took 1.5 months. The BOI's current image to foreign investors does not appear to be good. The story of one such investor going to Sri Lanka after visiting the BOI in Bangladesh and deciding to invest in Sri Lanka was narrated to the author during an interview with the Foreign Investors' Chamber of Commerce and Industry. Under a technical assistance project, the BOI's functions are reportedly being recast and it is being reorganized to enable it to perform as a promotional rather than a regulatory agency. Most of the regulatory functions it now performs should be eliminated to transform it into an effective promotional agency.

2.20 Besides, some pharmaceutical product ranges, foreign investments in ready made garments are also subject to certain special restrictions. Such discriminations against foreign investors contravene the Foreign Investment Act provision for no discrimination between the domestic and foreign investors.

2.21 Some foreign investors are concerned about the lack of or weak enforcement of patents and trade marks. This situation also works as a disincentive to foreign investment. During the interview with one foreign firm, some logos of local products closely resembling or imitating those of the foreign firm's products were shown. These legal weaknesses will be discussed in more detail under legal reform later. A Government committee has worked on this problem and come up with an updated draft of the legislation in this area, which is undergoing further steps of processing to be ready for placement before Parliament for passage.

2.22 Foreign firms' commercial imports are subject to certain special restrictions, a factor which also works as a disincentive to foreign investment. Such imports require a prior permission from the Chief Controller of Imports and Exports and submission of a number of documents. These restrictions are inconsistent with the general provision that goods which are not on the Control List are freely importable by commercial importers.

2.23 Another issue that can be troublesome to foreign firms is the remaining difficulty they can face in winding up business and repatriating their capital. While foreign investors investing in stocks and shares of the Stock Exchange can freely invest and disinvest and repatriate without requiring any permission, this is not the case with non-portfolio investors. Until recently, the latter group of investors needed permissions from the Securities and Exchange Commission (SEC) to transfer shares and the Bangladesh Bank to remit their disinvested share capital. The earlier version of this report mentioned the permission requirements from both these organizations. The SEC subsequently removed its permission requirement for transfer of shares. The Bangladesh Bank permission requirement still remains, which should also be removed.

2.24 While the power sector has been opened to private sector investors, difficulties still remain for private investors to go into this field because the Energy Ministry has reportedly yet to make certain rules to facilitate private investment. Also, power generation in the private sector is treated as an industrial activity. Currently the prices charged by the public gas supplying firms are differentiated according to its use in power generation by public Power Development Board (PDB) and private industry, with PDB getting a lower price. Such differentiation discriminates against the private investors in this field.

2.25 Difficulties experienced in customs clearance of goods at ports and unofficial payments required to be made to customs officials, which has become a rampant practice, are another significant deterrent to investment. One entrepreneur reported that his machinery valued at Tk 20 million had been held up for two months under the open sky even after he paid Tk 30,000 to customs officials. Another consignment of machinery valued at Tk 6.4 million was being held up for one and a half months. The importer already paid Tk 110,000 to the officials but they reportedly wanted a further sum of Tk 40,000.

2.26 It is also worthy of note that some of the policy documents used by the Government need updating if these are to serve their avowed purpose of making the current investment-related rules and regulations transparent, up-to-date and non-inhibiting to investment. Two documents which need to be updated are the Foreign Investment Act and the BOI's "Guide to Investment in Bangladesh". The Foreign Investment Act is currently under the process of being revised by the Government. The BOI Guide has recently been updated in the edition dated August 1993. However, some more recent policy changes have made this revised document already out of date. The BOI has recently published another booklet titled "Foreign Investment in Bangladesh". This booklet also needs updating.

### 3. EXCHANGE CONTROLS

3.1 Liberalization of the foreign exchange regime forms an important part of an economic reform program, which in turn is necessary to promote economic growth and efficiency. To ease existing foreign exchange controls, the Government (through Bangladesh Bank) has recently made some rapid and visible changes. In addition, in October 1993, the taka was declared as convertible on current account. These developments in the area of liberalization of the foreign exchange regime looked encouraging. Below, we first document the recent liberalization measures in this area, then analyze what foreign exchange controls still remain to be eliminated or relaxed further and finally touch on the proposed taka convertibility measure and other reform efforts needed to make this measure a fully successful exercise.

#### 3.A. Recent Liberalization Measures

3.2 During the fiscal years, 1991/92 and 1992/93 and the first few of months of the fiscal year, 1993/94, and buoyed by the recent emergence of a comfortable foreign exchange reserve situation, the Bangladesh Bank (BB) introduced several swift and successive batches of measures to relax existing controls on the use of foreign exchange. The changes have been made in such quick succession that, according to one foreign banker interviewed, it became a little difficult for the banking system to cope with the new changes.<sup>3</sup> He thought that the changes were being made too fast, without giving adequate attention to the preparatory ground work that should have first been made in the implementing and applying agencies. This he felt because the liberalization measures introduced shifted some of the burden of work from bank customers to the banks themselves as well as significantly increasing the paper work of the commercial banks in reporting to Bangladesh Bank. However, for launching taka convertibility, the banks were alerted already and certain steps to prepare them for effectively moving to such a system had already been announced.

3.3 Recent changes in relaxing exchange controls are summarized as follows.

- a) Withdrawal of the Prior Bangladesh Bank Approval Requirement: For several types of foreign exchange transactions, transparent Bangladesh Bank or BOI guidelines have been established and the requirement for prior BB permission has been withdrawn. These transactions are:
  - i) Contracting for suppliers' credits or other forms of foreign borrowings in the private sector, within prescribed BOI guidelines.
  - ii) Remitting foreign firms' profits.
  - iii) Remitting royalties and technical fees within prescribed BOI guidelines.

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<sup>3</sup> Complaints of Government's rapid action have been rare. Perhaps this presages a new style of policy implementation on the part of the Government.

- iv) Remitting foreign exchange for training and consultancy fees of producers for the domestic market, within prescribed BOI guidelines.
  - v) Remitting salary payments and savings of foreign nationals working in Bangladesh, within prescribed BOI guidelines.
  - vi) Remitting dividends on shares and securities held by non-residents. These remittances can be effected prior to payment of taxes provided the required tax payment is withheld by the firm providing the dividends.
  - vii) Remitting dividends and sale proceeds including capital gains on shares and other securities which are quoted on the Stock Exchange and held by foreign investors, subject to payment of taxes, if any.
  - viii) Opening back-to-back letters of credit (L/Cs) for recognized export-oriented readymade garments, hosiery and specialized units operating under bonded warehouse system.
  - ix) Obtaining short-term foreign currency (FC) loans by both 100 percent foreign-owned and joint-venture firms located in the export processing zones (EPZs);
  - x) Obtaining interest free short-term FC loans by foreign firms located outside EPZs.
  - xi) Releasing foreign exchange for studies abroad.
  - xii) Issuing and transferring of company shares to nonresidents.
- b) Allowing Exporters to Retain Some Foreign Exchange in Foreign Currency Accounts: For facilitating their foreign exchange expenses on business trips abroad, participation in international fairs and seminars, and imports of raw materials, machinery and spare parts, etc., exporters have been allowed to retain 10 percent<sup>4</sup> of export earnings from most products and 5 percent from low value-added garments and other products (such as naphtha, furnace oil, bitumen and electronic goods). Previously, exporters and export houses could utilize 2 percent and 2.5 percent respectively of their previous year's export earnings, subject to certain limits. Service exporters, except indentors and agencies earning commissions originating from Bangladesh sources, are also entitled to a foreign exchange retention benefit up to 5 percent of their repatriated foreign exchange income.
- c) Allowing Increased Foreign Exchange for Business and Other Travels,

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4 Raised to 15 percent "when the printing presses were rolling".

and Health, Education and Family Expenses.

- i) New exporters' annual foreign exchange entitlement for business travel has been raised from US \$4,000 to US \$6,000. In addition, according to a later Bangladesh Bank circular, new exporters will be allowed foreign exchange beyond US\$6,000 and other business travels will be allowed foreign exchange by Bangladesh Bank upon presentation of supporting documents establishing the requirement for such foreign exchange.
  - ii) Private travel entitlement per year has been raised to US \$2,500 for visits to countries other than SAARC countries and neighboring Myanmar. For the latter countries, the entitlement increases stand at US \$500 for travel by air and at US \$250 for travel by land. However, the Bangladesh Bank has with effect from July 26, 1993, decided to release foreign exchange in excess of the above personal travel quota limits at their discretion if supported by documents of actual requirements.
  - iii) Foreign exchange of up to US \$10,000 is allowed for medical treatment abroad if recommended by the medical board of the Health Directorate and is supported by a cost estimate from the foreign medical institution.
  - iv) Foreign exchange is released to private individuals as well as officials of government, semi-government and autonomous bodies to undertake educational tours and to attend seminars, workshops, etc., if requested by non-governmental organizations (NGOs) or international organizations and by debiting the latters' convertible taka accounts.
  - v) A more recent Bangladesh Bank circular relaxes the previous restrictions on remittances for education up to the secondary level and for unapproved courses and for maintenance of families abroad. Authorized banks have been allowed to release foreign exchange for all authorized educational programs abroad and the Bangladesh Bank will allow a moderate amount of foreign exchange for maintenance of families of Bangladeshi nationals living abroad. According to the Bangladesh Bank, this was the remaining foreign exchange liberalization to be done to make the Taka fully convertible on current account, which fulfils Article VIII provision of the International Monetary Fund.
- d) Allowing Certain Miscellaneous Foreign Exchange Business Transactions/Allowances: The foreign exchange remittances now allowed include:
- i) Remittances because of short weight, quality claims, partial shipments, etc., up to 10 percent of export proceeds realized.
  - ii) A discount is allowed to exporters of up to 10 percent of invoice values where

foreign importers refuse to clear goods due to discrepant documents, conservative arrest, etc.

- iii) Remittances of general average collected from consignees in Bangladesh.
  - iv) Remittances of premia for re-insurance.
  - v) Remittances of pre-shipment inspection fees.
  - vi) Issue of bank guarantees and performance bonds on behalf of merchandise exporters in favor of non-resident importers.
  - vii) Remittances of surplus earnings of foreign airlines, shipping companies and courier service companies.
  - viii) Remittances for the charter hire of foreign ships.
  - ix) Remittances of the cost of ships purchased by private firms.
- e) Withdrawal of Restrictions on Foreign Firms' Borrowings from Domestic Banks: Previously, the borrowings of working capital by foreign companies were subject to a ceiling determined on the basis of their foreign exchange contributions to the firm and there was no provision to extend term loan facilities to such companies. These restrictions have now been withdrawn.
- f) Withdrawal of Restrictions on Non-residents' Portfolio Investments: Previous restrictions on the use of foreign exchange funds of non-residents for purchase of stocks and shares quoted in the Stock Exchange have now been withdrawn. Such investments are allowed against inward remittances.
- g) Greater Liberalization Offered to Bangladeshis to Open and Operate Foreign Currency Accounts with Domestic Banks: Bangladeshis, ordinarily resident in Bangladesh, are now allowed to open foreign currency accounts with foreign exchange brought in from abroad, when they are returning to Bangladesh, and they are allowed to freely remit abroad such foreign exchange or foreign exchange which they have kept in hand. Bangladeshis operating foreign currency accounts have now been allowed to operate them as long as they want after permanent return to Bangladesh.

### **3.B. Elimination or Relaxation of Remaining Foreign Exchange Controls**

3.4 The above changes have eliminated many existing restrictions on foreign exchange use and provided for automatic approval of some foreign exchange transactions. However, the progress made thus far is still limited in terms of liberalization of the foreign exchange regime. Unnecessary and excessive controls still remain. Further progress, therefore, needs to be made in eliminating or easing the remaining controls. An outline of the remaining controls and what should be done to eliminate or ease them is provided below.

#### **3.B.1 Remaining Restriction on Private Borrowing from Foreign Sources**

3.5 What the Government has done in easing existing controls on private foreign borrowings including suppliers' credits is to allow these transactions without prior approval of Bangladesh Bank within the ranges of specified terms as set by the BOI. If private borrowers wish to contract borrowings outside these ranges, such cases would be subject to BOI approval. The terms specified are:

- a) Maximum rate of interest payable is London Inter-Bank Offer Rate (LIBOR) plus 4 percent.
- b) Minimum repayment period is 7 years.
- c) Maximum down payment is 10 percent.

Although the terms are presently more liberal than the previous ones (the interest rate previously allowed was LIBOR+2 percent), the conditions for automatic approval are too rigid and do not permit internal flexibility to allow, for example, a shorter repayment period combined with or without a variation in the other terms. Variations in the effective rate of interest over LIBOR plus 4 percent and repayment in less than 7 years would be considered by BOI on the basis of the importance of the industry concerned in terms of export orientation, export linkage, technological development, employment generation, value added, etc, and down payment up to 15 percent would be considered if the credit is essentially required from tied sources. These conditions are still based on excessive concern for conservation of foreign exchange resources and unnecessary and unrequested public sector risk aversions on behalf of private borrowers. Private borrowers do so at their own risk. Therefore, it is not clear why the terms at which they borrow should be dictated by the Government. One legitimate concern of the Government could be that multinational companies might take undue advantage of full liberalization, in this area, through "transfer pricing" i.e., by paying higher interest rates on capital borrowed from their parent companies than is available in the market. This does not, however, call for any prior public dictation of the terms of such loans. The Government (through the central bank) can always intervene if loans are contracted with visibly exaggerated rates of interest or at other starkly unfavorable terms. Furthermore, the potential foreign exchange liabilities that are involved in such transactions are not likely to be very substantial. As already mentioned in the preceding chapter, only a few such cases are actually found to be involved. Restriction of such

borrowings amounts to restriction of the inflow of foreign capital. Taking these considerations into account, it would be appropriate to allow the private borrowers to contract for foreign borrowings including suppliers' credits, at any terms they may negotiate with the suppliers of such credits, without prior BOI approval.

3.6 Short-term foreign exchange borrowings by foreign-owned and foreign-controlled firms in EPZs are allowed without BOI approval. Outside an EPZ, such borrowings are allowed only if these borrowings are interest free. The distinction maintained between EPZs and outside-EPZs is not based on any economic rationale. Only allowing borrowings at zero interest rate, without requiring approval from a public institution, is a too prohibitive restriction. Therefore, the distinction currently maintained between short-term borrowings for EPZs and non-EPZs should be eliminated. It is a misconception that EPZ industries, which are export industries, can bear any foreign exchange liabilities from their own resources and not become a burden on the national foreign exchange resources while non-EPZ industries, which may not be export industries, can not. Both export and import-substitution industries should stand on an equal footing. While export industries earn foreign exchange, the latter industries save foreign exchange. A dollar saved has the same value to the economy as a dollar earned.

### **3.B.2 Restriction Remaining on Foreign Exchange Retention Benefit for Exporters**

3.7 Discussions with export firms reveal that the privilege for exporters to have up to 5 percent to 10 percent of their gross foreign exchange earnings in foreign currency accounts has not proved to be of much value to them as they do not like to have their funds blocked in an account. Instead, a more useful provision would be to allow them to draw on the foreign exchange resources up to the current limits in case of their business expenses. The problem arises, even after the taka has been declared as convertible, because of the one-way convertibility allowed to these foreign currency deposits. Once exporters convert foreign exchange into taka, to meet their domestic expenses, they are not allowed to reconvert such amounts into foreign currency. If both-way convertibility were allowed, the avowed purpose, for which this foreign exchange retention benefit was created, would be served. The current restriction remaining on reconversion of taka into foreign currency for exporters should, therefore, be withdrawn.

### **3.B.3 Restriction on the Use of Foreign Exchange for Non-Letter of Credit Imports**

3.8 Currently drawings on foreign exchange resources for import purposes are normally allowed only through letters of credit (L/Cs) opened with banks. Imports on non-L/C basis are allowed in some exceptional cases (e.g., for imports of books, journals, magazines and periodicals on sight draft or usance bill basis; for imports under loans and grants if required by specific procurement procedures; etc.) and imports against remittances made from Bangladesh are allowed for general cases only for a small amount not exceeding US \$2,500 during a financial year. As gathered from business people, such remittances need prior permission from Bangladesh Bank as commercial banks are not authorized to directly remit any foreign exchange money for import purposes. Importing with

the backing of L/Cs is an international practice, a device which helps the involved parties to recover their money in case of default. However, L/C procedures are complex and lengthy and opening an L/C entails significant costs. For facilitating business, therefore, it would be appropriate to allow imports on non-L/C basis up to a satisfactory minimum amount without requiring prior permission of Bangladesh Bank.

### **3.B.4 Remaining Restriction on Imports against Direct Payments Abroad**

3.9 Imports against direct payments abroad have been allowed without requiring any prior permission or import permit from the import control authority with effect from February, 1993, but applicable only for Bangladeshi nationals living abroad. This means that foreign investors are not allowed to effect imports against direct payments abroad. This is a needless restriction and should be withdrawn.

### **3.B.5 Remaining Foreign Exchange Restrictions for Business and Personal Travel**

3.10 Although restrictions on the access to foreign exchange for business and personal travels have been substantially eased recently, the foreign exchange restrictions still remaining for such travels are perceived by business circles as excessive. Bangladesh Bank currently (according to the BB press release dated July 26, 1993) allows BB releases of foreign exchange in excess of the present limit of personal quota in genuine cases against supporting documents in favor of actual requirement. This is a substantial improvement from the too limited personal travel quotas. However, it would be more appropriate to raise the general quota first to a reasonably high level at which travellers can access foreign exchange without requiring BB approval. As noted earlier the personal annual quotas maintained are US \$2,500 for visits to countries other than SAARC countries and neighboring Myanmar and US \$250 to US \$500 for the latter countries according to whether travel is by land or air. It makes little sense to maintain such low travel quotas when travellers always manage to take recourse to the 'Hundi' market to meet their required foreign exchange needs. The current limits, however, impose some extra cost on business travels. Sufficient relaxation of the travel quotas would not impose significant additional burden on the country's foreign exchange balances, but would rather mainly impart *de jure* status to what is happening *de facto*. Relaxation of current foreign exchange restrictions would not prompt people to unnecessarily incur foreign exchange expenses just because foreign exchange is more liberally available. Considering these factors, the current personal travel quotas should be at least doubled, to US\$ 5,000 for countries other than SAARC countries and Myanmar and US\$ 500 to 1,000 for the latter countries, or raised to other appropriate levels which can be determined by the Bangladesh Bank upon examination of the cases of requests for foreign exchange in excess of the present limits.

3.11 For business trips, access to foreign exchange should be available on a much more liberal basis, be it for exporters or other business people. Currently new exporters are eligible for a general foreign exchange travel quota of US\$6,000 and they are allowed foreign exchange beyond US\$6,000 and other business travels are allowed foreign exchange by the Bangladesh Bank upon presentation

of supporting documents. To make a distinction between these two groups of businessmen is not tenable, since local manufacturers catering to the domestic market may well need to incur significant business-related foreign travel expenses to negotiate, say, a joint-venture proposal or a technical assistance collaboration deal or a purchase of plant and machinery. Hence, it would be appropriate to either withdraw foreign exchange restrictions altogether for business travel or to fix the quotas for such travel well above the personal travel quota limits. The fear that more liberal travel quotas would encourage capital flight has no valid basis, for if there is any perceived need for capital flight, it would take place in any case whether there is exchange control or not. Experience of other developing countries suggest that foreign exchange liberalization has helped those countries earn more foreign exchange and encourage more foreign investment.

### **3.B.6 Foreign Exchange Restriction for Educational Tours or for Seminars / Workshops, etc.**

3.12 It makes little sense to maintain the current restriction on education travel that requires foreign exchange costs to be borne by an international organization or on NGO withdrawals from their convertible accounts. There should remain no foreign exchange restrictions for such travel, regardless of the source of foreign exchange. The overall foreign exchange used for such travel is hardly of significance. Such a restriction is an unnecessary irritant to multinational companies and discourages foreign investment.

### **3.B.7 Cash Foreign Exchange Restriction for Back to Back Letter of Credit Importers**

3.13 Currently export industries, such as readymade garments, which import their raw and packing materials on back-to-back L/C basis are barred from having access to cash foreign exchange for any of their import needs. They are not even allowed to utilize their retained foreign exchange quotas for such import purposes. This restriction does not make any sense, as these industries also may need to import on non-back-to-back L/C basis occasionally. Not allowing foreign exchange for such imports only hurts their business and the country's export and industrialization process. There is in fact a strong case for giving a general option to such exporters to import their requirements either on the back-to-back L/C basis or on cash foreign exchange basis. Given such a choice, the exporters may at times like to import their requirements on cash foreign exchange basis as the other basis requires exporters to get their imported raw materials on deferred payment basis, which can at times entail higher working capital costs for exporters compared to the local bank lending rates due to differing interest rates ruling in different countries from where the raw materials are sourced. Furthermore, importers on cash basis can some times have the additional advantage that they can import their raw materials from the cheapest source. The current conditions that there is a limited use of an existing Export Development Fund and that there is a satisfactory general foreign exchange reserve situation seem to permit allowing access to cash foreign exchange for exporters operating under the back-to-back L/C basis.

### **3.B.8 Foreign Exchange Restrictions on Technology Transfer-Related Payments**

3.14 Firms wishing to enter into agreements with overseas collaborators for using their license, manufacturing know-how, or other technology transfer arrangements are required to procure a passbook from the BOI incorporating BOI-approved foreign exchange remittances for such services by foreign collaborators. Approval is automatically granted for remitting fees on account of royalties, technical know-how and technical assistance fees if the total fees and other expenses connected with the technology transfer (service fees, marketing commission, etc.) are within the following prescribed limits :

- a) For new projects, 6 percent of the cost of imported machinery; and
- b) For established firms, 6 percent of the previous year's sales of the firm as declared in the firm's tax return.

Automatic authorization of remittances on account of consultancy services and overseas training is also provided in the passbook subject to a maximum limit of 1 percent of sales of firms. However, these limits may be found to be too restrictive in some cases. Technology transfer arrangements involving higher remittance requirements require prior BOI approval. Since, the Government should vigorously encourage introduction of new and improved technologies and since the way to do this on a fast and large scale would be to bring such technologies from outside, the existing foreign exchange restrictions on payments for such transfers, where foreign exchange involvements are also unlikely to be too large, are both undesirable and unnecessary.

### **3.C. Exchange Controls Due to Import Controls**

3.15 A restrictive import policy results in exchange control. As policy efforts to bring about import liberalization have, in the past, been rather slow, imports are being restricted through fairly significant quantitative restrictions as well as through continued high tariffs. Quantitative restrictions on imports will be discussed in detail in the next chapter. Import restriction-created exchange control is the most important source of suppression of the demand for foreign exchange. This has served to distort the effective protection rates for import substitution and export industries as well as to overvalue the exchange rate. Both of these effects have created a significant anti-export bias of the current trade policy regime and retarded export expansion and the pace of industrialization. To liberalize the exchange control regime, import liberalization should, therefore, also be given a top priority.

### **3.D. Making Taka Convertible**

3.16 Convertibility of the taka on current account, which has taken effect just recently, is a very welcome measure as this will pave the way for a much greater liberalization of the foreign exchange control regime in Bangladesh than many of the other measures which have been taken. The current

account of a country's external balance of payments comprises the merchandise goods trade account and transactions on services and current unrequited transfers. It leaves out capital transfers. Convertibility of taka in the current account then means freeing access to foreign exchange from controls for all permissible trade and current account business. Authorized foreign exchange dealers are allowed to convert taka into foreign exchange without any restriction for all trade and current account transactions which are not otherwise restricted. This thus allows the market forces of supply and demand for foreign exchange to have a freer play. Taka convertibility would, therefore, be a potentially far-reaching liberalizing economic reform measure. India has recently moved to convertibility of its rupee on trade account. Nepal has made its currency convertible on current account. Achieving convertibility on the current account is a more liberalizing measure than achieving it on the trade account. Some developing countries have also moved toward some measure of convertibility of their capital account as well.

3.17 The Bangladesh Bank proclaimed, effective August 8, 1993, some new measures as preparation for moving to taka convertibility. These measures include the following:

- a) BB has ceased to fix exchange rates at which authorized dealers can sell and buy foreign currencies to and from the public. Authorized dealers have been given the task to fix these rates themselves.
- b) To permit greater foreign exchange liquidity with authorized dealers, their ceiling for foreign exchange has been increased to 20 percent from 15 percent of the outstanding L/C holdings liabilities.
- c) To activate inter-bank foreign exchange transactions, the spread between buying and selling rates of foreign exchange to and from the authorized dealers by BB has been increased to Tk.0.20 from Tk.0.10.
- d) BB has ceased to extend any forward cover facility to the authorized dealers against any foreign currency. The dealers have been left free to take counter-cover among themselves or they may cover themselves in the overseas foreign exchange markets.

3.18 In spite of the proclaimed measures, the matter of fixing exchange rates by authorized dealers has not yet been freed from centralized managed float control. The Bangladesh Bank continues to exercise control on the exchange rate by using its generally inflexible reference rates for conversion of US dollar into taka. The authorized dealers, i.e., the banks dealing with foreign exchange, in fact find themselves placed in a situation where they do not find it worthwhile to fix and vary their own exchange rates except within a very narrow margin. The taka exchange rate against the US dollar budged little from its original rate at the time when the task of fixing the exchange rate was shifted from BB to the authorized foreign exchange dealers. Recently taka was devalued by BB by a small margin from Tk 39.85/US\$ 1 to Tk 40.07/US\$1 in one instance, to Tk 40.13/US\$ 1 in a second instance, and to Tk. 40.25/US\$ 1 in a third instance. This is the official exchange rate (mid-rate) ruling at present. The issue of completely freeing the exchange rate from a managed float will be central to the success of the taka convertibility as a liberalization measure. Freeing the exchange

rate would allow the taka to be valued appropriately in terms of other currencies and in line with market forces that would ensure full flexibility in the exchange rate. Putting the taka on a free float against all other currencies should, therefore, be an essential element of the taka convertibility scheme. This would result in a possible devaluation of the taka, if indeed the taka remains overvalued. However, as the experience of other countries introducing currency convertibility suggests, the immediate swing in value may not be great after the exchange rate liberalization. One factor that also affects the exchange rate is foreign capital flow. With greater foreign exchange liberalization, countries are usually found to attract greater capital inflows, which acts as a brake on the exchange rate depreciating too rapidly (and which sometimes even leads to an appreciation of the domestic currency). India has attracted a sharply higher foreign investment flow following its recent foreign exchange and other liberalization. A greater inflow of foreign capital is a great boon in itself to a capital-poor low-investment economy.

3.19 An adverse effect of a capital inflow on the exchange rate (putting pressure on it to appreciate) will arise only when investment does not rise commensurately. With substantial increases in the current low levels of both private and public investment, which need to rise substantially to significantly raise the current moderate growth rate and with further import liberalization, the downward pressure on the exchange rate to depreciate is likely to be strong in a short to medium term. This consideration makes the case for freeing the exchange rate from the centralized float quite strong.

3.20 Other prerequisites for the full effectiveness of taka convertibility as a liberalization measure would be a swift and substantial liberalization of the import policy regime and elimination or sufficient relaxation of other remaining exchange controls, which have been discussed above. With the current restricted import trade regime and other exchange controls in place, the taka convertibility by itself will not provide the needed stimulus to industrialization.

## **4. QUANTITATIVE CONTROLS ON IMPORTS**

### **4.A. Introduction**

4.1 Use of quantitative restrictions (QRs) on imports as an instrument of protecting domestic industries is unwise, because such QRs lead to arbitrary, non-transparent and often inordinately high levels of effective protection to domestic industries. The elimination of QRs on imports for trade reasons is an essential element of import liberalization. While successful developing countries in South Asia and Latin America are found to have eliminated almost all non-tariff restrictions on trade, Bangladesh still depends on import bans and restrictions to protect domestic industries.

4.2 The stated policy goal of the Bangladesh Government is to liberalize trade and bring down effective protection received by industries to low levels over the next few years. To realize this goal, both elimination of import QRs and rationalization of import tariffs, which are very high on average and widely disparate, are necessary. This study is concerned only with import QRs.

4.3 As a first essential step towards its stated goal, and under a trade reform program supported by the World Bank and the International Monetary Fund, the Government undertook to abolish, by July 1993, all import controls that cannot be justified by the non-trade considerations of religion, security, public safety, or other social reasons. However, the existing controls were only partially lifted in October 1993. This chapter will analyze the current status of the still remaining import controls after accounting for recent progress in their reduction. Parts of the analysis draw on some recent unpublished work of the World Bank done in the context of ISAC-2.

### **4.B. Recent Progress in the Reduction of QRs on Imports**

4.4 The Government initiated a gradual process of phasing out the QRs on imports in the mid-eighties with World Bank support under its Industrial Sector Credit (ISC)-1 program. This followed a series of effective protection studies carried out under a Government Trade and Industrial Policy Reform Program (TIP) project. Under ISC-1 program, the Government agreed on a 20 percent annual reduction of the then Negative List (now the banned import part of the Control List) starting with FY 1987-88 (FY 88) and phasing out of all such restrictions by FY 1990. However, this agreement was only partially implemented and QRs were still widely in place in 1990, when 36 percent of tariff headings were still subject to QRs. More importantly, these early liberalizing changes related mainly to less important trade flow items, while many major products receiving protection through QRs were left untouched.

4.5 Since 1988, trade flows and restrictions became amenable to a more systematic classification under a Harmonized System (HS) of coding. At the end of FY 90, the QR items on the explicit Control List (CL) of the Import Policy Order (IPO), which combined both fully banned and partially restricted import categories, numbered 320 at the HS four-digit level. In addition, there were QRs in the IPO text which were not codified and listed on the CL. The four-digit CL items were reduced to 250 in the FY 91 IPO and further reduced to 193 in the FY 92 IPO. At the end of FY 92 (i.e., in June 1992), there remained in addition some 130 broad groups of non-codified restrictions in the IPO text.

4.6 In February 1993, the 1991-93 Import Policy Order was amended incorporating reduction of the CL QRs by another 100 items leaving 93 CL items at the four-digit level. In addition, there remained:

- a) Restrictions and procedures described in sections 15 and 16 of the text of the Order, but not codified on its CL, affecting:
  - i) 135 other four-digit headings including 62 for pesticide inputs, mostly active ingredients but a few general goods (foil, starch, etc.), and 22 for textile fabrics which are importable subject to certain conditions.
  - ii) Animals, plants and plant products (many HS headings);
  - iii) Food and beverages, other than wine and liquor, and second-hand machinery (many HS headings).
- b) Public monopoly imports, other than those prescribed in the Order, which included crude oil, petroleum products, and sugar.

Among these CL and non-CL items together, about 75 four-digit items remained with trade restrictions while the remaining ones were subject to restrictions for non-trade reasons.

4.7 Further progress has been effected, in October 1993, through the new 1993-95 IPO which has been made effective from November 1, 1993. The new changes involved codification and transfer of the non-CL items to the CL and reduction of all the codified items to 111 four-digit headings, actually 110 of them as one of these is redundant.<sup>5</sup> Of these:

- a) Eight contain only inspection requirements.<sup>6</sup>
- b) 47 unambiguously contain only non-trade restrictions (for reasons of public safety, religion, etc).
- c) 14 are associated with the Drug Administration and may be considered in that context.

This leaves 41 headings within which the bans or restrictions are imposed for trade or semi-trade reasons. This number is close to 39 to which the Government agreed to reduce the existing trade-restricted items as part of the effectiveness conditionalities of the World Bank's Second Industrial Sector Adjustment Credit (ISAC-2). The October changes involved reduction of the import QRs by some 20 four-digit items. Those removed from the list include milk food; non-fat dried milk; baby

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<sup>5</sup> The ban on hair and yarn of pigs (coarse haired animals) requires five headings (51.02 to 51.05 and 51.10), not six as listed (51.02 to 51.05, 51.08 and 51.09).

<sup>6</sup> These are baby food with fat (19.01), cement (25.23), coal and hard coke (27.01, 27.04), steel billets (72.07), corrugated iron sheets (72.10), weighing machines (84.23), and weights and measures (90.16).

food (with fat); betel nuts; unrefined edible oil; coal and hardcoke; soaps; cotton yarn; PVC pipes, tableware, kitchenware and other household articles of plastic; steel billets; corrugated iron sheets; certain motor vehicles; weighing machines; domestic sewing machines; weights and measures; pesticide inputs; electric ceiling fans; etc.

4.8 Recent simplifications of import restrictive procedures (supported by the pre-negotiation requirements for ISAC-2) are also worth noting. These simplifications include:

- a) Deletion, from the IPO, of the mandatory provision for using indents issued by local agents for import purposes.
- b) Allowing imports by Bangladeshi nationals living abroad against direct payments abroad and without requiring an import permit from the Chief Controller of Imports and Exports (CCIE).
- c) Allowing general waiver of the mandatory use of Bangladeshi flag vessels for imports and exports by export industries.
- d) Requiring the use of pass books by industrial importers only for restricted items.
- e) Allowing 100 percent export-oriented industries operating under the bonded warehouse system to import their raw and packing materials either on back-to-back L/C basis or up to four months' requirement without any master export L/C, and requiring no authorization from the Bangladesh Bank for these industries for importing against back-to-back L/Cs.
- f) Deletion from the IPO of the requirement for foreign firms to obtain a permission from the Board of Investment for production capacity changes.

With the partial elimination of the passbook requirement for import purposes, industrial importers are entitled to import freely importable items without the pass book, except in the case of import by the readymade garments, hosiery and specialized textile industries operating under the bonded warehouse system, and the pharmaceutical (allopathic) industries. There are, however, reports that this reform has not been fully implemented, as manufacturers still possessing old passbooks which list all import items of the firms face difficulties with customs in importing any quantities they like of the freely importable items. To address this situation, either the CCIE should recall all old passbooks and replace them with new ones or, the National Board of Revenue should issue a Statutory Regulatory Order (SRO) stating that henceforth restriction of imports of the passbook items which should be subject to any entitlements noted therein would apply only in the cases of restricted import category items under the current import policy.

## 4.C. Remaining Controls on Imports

4.9 As noted above, QRs currently remain on 110 four-digit items among which eight contain only inspection requirements. Of the 102 remaining items, 47 items are those where the restrictions are based on non-economic reasons of public safety, religion, etc. These items include most of the 56 which were identified in the February 1993 CL listing of the IPO as being there for non-commercial reasons. These can be found listed in Attachment 4.

4.10 The remaining four-digit 55 items subject to trade restrictions include 14 which have controls exercised by the Drugs Administration. The items involved are:

1. Vegetable saps and extracts (excluding opium, agar and pectin)
2. Dextrose and saline
3. Medical alcohol
4. Sulphanomides
5. Vitamins, etc.
- 6 - 8. Hormones, etc.
9. Antibiotics
10. Organs
11. Blood and vaccines
- 12 - 13. Medicaments
14. Enzymes

The import controls on these items are not based on sound rationales. If the quality of these items is what needs to be ensured, this can be done by streamlining import procedures rather than restricting imports. Quality checks can and should be made by the Drugs Administration conducting tests of samples of the imported consignments and if necessary, introducing other additional appropriate measures such as banning the sale of sub-standard drugs. The import controls on these items should, therefore, be replaced by a streamlining of the procedures for importing them.

4.11 This finally leaves 41 four-digit HS headings where import controls remain on trade or semi-trade reasons. These items are summarized in Table 1<sup>7</sup>. Table 2 repeats them along with corresponding HS heading numbers, the nature of import restrictions applied, and those which should be withdrawn. Among the domestic industries, besides pharmaceutical products and some of their inputs, that are currently being protected by import QRs are grey and finished textiles fabrics, sugar, newsprint, salt, films, some electronics, engineering and metal products and some transport equipment. The import QRs underlined in Table 2 should be removed. For greater clarity, the recommended changes are repeated in the last column of the Table.

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<sup>7</sup> One item, newsprint, was taken off the list, (i.e., restriction on which was withdrawn) and restriction on part of another item, grey fabrics, was relaxed for export-oriented readymade garments producers as "the printing presses were rolling".

**Table 1: GOODS CURRENTLY SUBJECT TO QRS ON TRADE REASONS**

<b>TARIFF HEADING</b>	<b>GOOD ITEMS</b>	<b>TARIFF HEADING</b>	<b>GOOD ITEMS</b>
<b>Textile Group</b>		<b>Non-Textile Group</b>	
50	Silk fabric	4	Eggs
52	Various types of cloth	7	Seed potatoes (standardized varieties)
54	Ditto	14	'Tendu' leaves
55	Ditto	16	Sausages (including non-pork)
56	Ropes	17	Sugar
60	Various types of cloth	25	Salt
63	Used clothing	37	South Asian films
63	Rags and scrap rope	48	Newsprint
		56	Fishing nets
		83	Padlocks
		84	Boilers
		84	Used engines/gear boxes
		85	Radio equipment
		85	Navigation equipment
		87	Used motor vehicles
		89	Used ships
		90	Single-phase electric meters and parts of electric meters

**Table 2: CURRENT CONTROL LIST WITH RESTRICTIONS FOR TRADE REASONS**

HS HEAD-ING	HS CODE NO. (ITC NO.)	DESCRIPTION OF ITEMS	IMPORT-STATUS	RECOMMEN-DATION
04.07	0407.00	Eggs	<u>Import banned. However, imports of hatching eggs are allowed subject to certification from concerned government agency from exporting country and prior clearance from Director, Livestock Department.</u>	Withdraw the import ban on eggs and import restrictions on hatching eggs.
07.01		Seed potatoes	(a) <u>Only imports of approved varieties allowed.</u> (b) Foreign quarantine certification required; (c) Examination on entry by seed agency and plant protection authority	Allow imports of all varieties
14.04	1404.901	Tendu leaves (biri leaves)	<u>Import banned</u>	Withdraw the import ban
16.01	1601.00	All items including sausages and similar product of meat	Importable only by foreign exchange earning hotels subject to prescribed conditions. ( <u>Import restrictions relating to Non-pork sausages and similar products</u> )	Allow unrestricted import by all importers of non-pork sausages and similar products
17.01		Sugar	<u>Import subject to conditions prescribed by Government</u>	Allow unrestricted import by all importers
25.01	All HS codes	a) Common salt except table salt b) Table salt	(a) <u>Importable subject to prescribed conditions.</u> (b) <u>Importable only by the foreign exchange earning hotels subject to prescribed conditions</u>	Remove all existing restrictions on import

HS HEAD-ING	HS CODE NO. (ITC NO.)	DESCRIPTION OF ITEMS	IMPORT-STATUS	RECOMMEN-DATION
48.01	4801.00	Newsprint	<u>Import banned</u>	Remove the import ban <sup>8</sup>
50.07	All HS codes	Woven fabrics of silk or of silk waste	<u>Import banned</u>	Remove the import ban
52.08 52.09 52.10 52.11 52.12	All HS Codes	(i) Long cloth (white only) up to 33s counts and width up to 36";  (ii) Poplin including shirting -- white, dyed, printed, striped and checks up to 40s counts and width up to 36";  (iii) Cambric including shirting white, dyed, printed, striped and checks up to 40s counts and width up to 36";  (iv) Serge and gabardine of width up to 45" of all constructions;  (v) Twill and corduroy of width up to 45" of all constructions;  (vi) Mull, organdie, lawn and voile -- white, dyed or printed up to 65s counts and width 35";  (vii) Flannel -- white, dyed and printed up to 45" width;  (viii) Cotton -- synthetic and blended, suiting of all constructions up to 60" width;  (ix) Cotton -- synthetic and blended, shirting -- white, dyed and printed up to 45" width;  (x) Umbrella fabric	<u>Import of all items except those mentioned in:</u>  <u>(i) to (x) in the third Column is banned. Items mentioned in (xi) to (xiv) in the third column are importable subject to conditions mentioned against each in the fourth column (below)</u>	Remove all existing ban and restriction on import

8 As noted in the previous footnote, the import ban was withdrawn as "the printing presses were rolling".

HS HEAD-ING	HS CODE NO. (ITC NO.)	DESCRIPTION OF ITEMS	IMPORT-STATUS	RECOMMEN-DATION
		<p>(xi) Grey cloth, all sorts;</p> <p>(xii) Indigo denim (Jeans fabrics), 100% cotton fabrics above 36" width (in than or rolls) not in cut pieces or cut into size;</p> <p>(xiii) Combat cloth;</p> <p>(xiv) Drill and cellular dyed cloth including 'mineral khaki'</p>	<p>(xi) <u>Importable subject to prescribed conditions.</u></p> <p>(xii) <u>Importable against back to back L/C by export oriented ready made garments units operating under bonded warehouse system.</u></p> <p>(xiii) <u>Importable only by the defense services</u></p> <p>(xiv) <u>Importable by public sector agencies only on recommendation by the Ministry of Textiles</u></p>	
54.07 54.08	All HS Codes	<p>(1) Shirting and suiting of 85% or more by weight of synthetic or manmade fibre (synthetic, regenerated or blended yarn of both) and similar fabrics in any form, including fents and cut pieces except polyester shear of mesh 80-150 required for screen printing machines and tables and saree fabrics, of 85% or more by weight, of synthetic or manmade fibre (synthetic, regenerated or blended yarn of both) in pieces of 5 1/2 yards to 6 yards not in than or roll;</p> <p>(2) Fents, cut pieces and fabrics cut into sizes or piece goods;</p> <p>(3) Cotton -- synthetic and blended suiting of all constructions above 60" width.</p>	<u>Import of items mentioned at (1) to (3) in the third column is banned</u>	Withdraw the import ban

HS HEAD-ING	HS CODE NO. (ITC NO.)	DESCRIPTION OF ITEMS	IMPORT-STATUS	RECOMMEN-DATION
55.12 55.13 55.14 55.15	All HS Codes	(1) The following except polyester shear of mesh 80-150 required for screen printing machines and tables. (i) Shirting and suiting of 85% or more by weight of synthetic or man-made fibre (synthetic regenerated or blended yarn of both) and similar fabrics in any form; (ii) Fents, cut pieces and fabrics cut into sizes and piece goods; (iii) Cotton and synthetic blended shirting -- white, dyed and printed above 45" width; and (iv) Cotton synthetic and blended suiting of all constructions above 60" width.	<u>Import of items mentioned at (i) to (iv) in the third column is banned.</u>	Withdraw the import ban
55.16		(v) Grey cloth, all sorts  (vi) Combat cloth	(v) <u>Importable subject to prescribed conditions</u>  (vi) <u>Importable only by the Defence Service</u>	(v) Remove existing import restrictions (vi) Allow import by all importers
56.07	5607.41 to 5607.90	Ropes made of nylon and polythene except nylon cord for V-belt	<u>Import banned</u>	Withdraw the import ban
56.08		Fishing nets	a) <u>Import of gillnets with mesh under 4.5 cm banned,</u> b) <u>Others importable only by deep-sea fishing units with prior permit of Directorate of Fisheries</u>	Withdraw the existing import ban and restrictions
63.09	All HS codes	Worn clothing and other worn articles (secondhand clothing)	<u>Importable subject to prescribed conditions.</u>	Withdraw the existing import restrictions

HS HEAD-ING	HS CODE NO. (ITC NO.)	DESCRIPTION OF ITEMS	IMPORT-STATUS	RECOMMEN-DATION
63.10	All HS codes	All items including used or new rags, scrap twine, cordage, rope and cables	<u>Import banned</u>	Remove the import ban
83.01	8301.10	Padlocks up to 3 inches size	<u>Import banned</u>	Ditto
84.02 84.04		Boilers	<u>Importable subject to clearance of Chief Inspector of Boilers</u>	Remove the clearance requirement
84.07 84.08		Used engines and gearboxes for road vehicles	a) <u>Imports of old/reconditioned engines and gear boxes of buses, trucks, minibuses and microbuses subject to requirement that these are not older than 6 years</u> b) <u>Secondhand/reconditioned marine diesel engines of coasters, launches, motor-driven barges with horse power above 35 only importable</u>	a) Remove the engine and gear box age restriction b) Remove the horsepower restriction
85.25	All HS code	Radio transmitters and trans-receiver wireless equipment, walkie-talkie and other radio broadcast receivers including receivers incorporating sound recorders or reproducers	<u>Importable by Radio Bangladesh and Bangladesh Television with clearance from the sponsoring ministry. Also importable by other government, semi-government and autonomous agencies on the basis of clearance from the concerned administrative ministry and the Ministry of Posts and Telecommunication. Only telecommunication equipments are also importable in the private sector on the basis of NOC from the Ministry of Posts and Telecommunications.</u>	Remove the clearance requirement for telecommunication equipment for private imports

HS HEAD-ING	HS CODE NO. (ITC NO.)	DESCRIPTION OF ITEMS	IMPORT-STATUS	RECOMMEN-DATION
85.26	All HS Codes	Radio navigational aid apparatus, radar apparatus and radio remote control apparatus	Importable by user agencies with clearance from the sponsoring Ministry ( <u>Import restrictions relating to private imports</u> )	Remove restrictions for private imports
87.02 87.03 87.04		Used motorcars, minibuses, jeeps, vans, pick ups and microbuses	(a) <u>Not over 6 years old;</u> (b) <u>Supplier's guarantee of spare parts available for 3 years</u>	Remove existing restrictions for private imports
89.01 89.02		Ships, oil tankers and trawlers	(a) <u>Not over 15 years old,</u> (b) <u>Prior approval required from Ministries of Fisheries or Shipping</u>	Ditto

## **5. EXPORT CONTROLS**

### **5.A. Introduction**

5.1 The Government's stated goal is rapid export development to accelerate the industrialization of Bangladesh. However, policies have not yet been fully geared to this end. In addition to wide-scale control on imports, which leads to an anti-export bias, there still remain some explicit controls on exports.

5.2 The purpose of this chapter is limited to a review of some recent eliminations and relaxations of export controls and to an analysis of the remaining controls. The purpose is not to examine the whole export policy matrix. (See PIAG-3 for an evaluation of current export policy).

### **5.B. Recent Progress in Export Liberalization**

5.3 One policy change relates to the re-exporting of imports, which is now allowed on a limited scale. The change came through two Ministry of Commerce Orders (same no. BM/R-1/1//2/90) dated 12th May, 1992 and 28th October, 1992. According to these orders:

- a) Re-exporting would be considered for goods other than readymade garments/textiles and those products which are exported through local production /processing.
- b) The re-exporting trade would be allowed on a case by case basis with permission from the Ministry of Commerce.
- c) It is allowed against an export master L/C when imported items are exported through back-to-back L/C.
- d) It can be effected through customs authority- approved bonded warehouse facilities at the port or at any other place.
- e) It is permissible with a minimum price difference of 15 percent over the value of imports.

The re-exporting is allowed also to a third country through back-to-back LCs against a master L/C without requiring the importing into the country. Alternatively, such business can be done through a transferable and divisible L/C. The 1991-93 Export Policy mentions that at the initial stage, the Trading Corporation of Bangladesh and established exporters would be allowed this facility in a limited way.

5.4 Another change is the general waiver, accorded to export-oriented industries, from the requirement of using Bangladeshi flag vessels for importing raw materials and exporting products of these industries.

5.5 A third change is the lifting of an export ban on rice. Exporting of rice has been permitted following a good harvest last year. The export ban has also been lifted from beef, mutton and animal fats; eggs and poultry; feature films; and oil-cake.

5.6 A fourth change is the abolition of the requirement of the prior Bangladesh Bank's approval for exporting on back-to-back LCs, under the bonded warehouse system, for all goods including readymade garments, hosiery and specialized textile products, provided such exports meet the value addition criteria in force. Formerly, only these latter industries could export on a back-to-back L/C basis without prior BB approval.

5.7 Fifth, banks have been authorized to issue bank guarantees and performance bonds, on behalf of the merchandize exporters of Bangladesh, in favor of non-resident importers. This change came recently (on 23 April, 1993) as a measure of foreign exchange liberalization for exporters.

5.8 Sixth, another recent foreign exchange liberalization measure is an enhancement of new exporters' annual foreign exchange quota for business travel abroad from US \$4,000 to US \$6,000, and more recently, a further relaxation that such exporters could be allowed foreign exchange beyond US\$6,000 upon presentation of supporting documents.

5.9 Seventh, the export value of samples, required to qualify for participation in export fairs abroad, has been increased to US \$1,000, subject to a clearance from the Export Promotion Bureau (EPB). Samples valued up to US \$2,000 are also allowed with prior approval from the office of the Chief Controller of Imports and Exports (CCIE), on the recommendation from the EPB.

5.10 Eighth, exporters have also been allowed to import samples up to the value of US \$1,000 with clearance from the EPB but without requiring any prior permission from the office of the CCIE and above US \$1,000 with prior approval from the office of the CCIE on the recommendation of the EPB. Imports of samples for export-oriented readymade garments have been allowed on a more liberal basis, up to a maximum of 100 pieces each financial year with not more than 20 in each garment category, without requiring any prior permission from the CCIE and without any import permit.

### **5.C. Remaining Controls on Exports**

5.11 A number of the above changes do not, however, go far enough to bring about the desired liberalization. The re-exporting trade is still subject to unnecessary limitations and conditions. One condition which stipulates that the difference of the value of exports over that of imports must be at least 15 percent is needlessly restrictive. Such a restriction violates private enterprise principles. Such a regulation encourages regulation avoidance behavior to bypass it through under-invoicing of imports and/or over-invoicing of exports. Also, limiting this trade for a restricted number of products and making it subject to approval from the Ministry of Commerce are remaining restrictions which should also be removed. Many countries have entre-pot facilities and earn substantial amounts of

foreign exchange through re-exporting. It makes little sense for Bangladesh to forgo the benefits of this trade.

5.12 Requiring a permission from the EPB and/or CCIE for export of samples is an unnecessary restriction. Likewise, imports of samples of goods which are not on the Control List should be freely allowed without any value limit. Finally samples should be freely allowed to be exported without any value limit.

5.13 An export ban remaining on a few agricultural products reflects excessive caution by the Government against the risk of domestic scarcity that could be created by their exports. These products are wheat, pulses, onion, jute and sunn-hemp seeds, prawns and shrimp except when frozen and processed, and whole bamboo and cane. Although lifting of the export ban does not appear at present to make any practical difference in the case of these agricultural products, except probably jute seeds, continuation of the ban does not make any economic sense either. Two other agricultural products still remaining on the banned export list are oil seeds and milk. These, however, could be exported with prior permission from the Ministry of Commerce. These restrictions based on trade concerns are also inappropriate.

5.14 Export bans also remain on a few manufactured and processed products for trade reasons. Such products are ferrous and non-ferrous metals and their scraps, petroleum and petroleum products except for naphtha and furnace oil, 'gur' and khandseri sugar, rice bran except for de-oiled rice bran and wooden logs. Edible oils and milk products still remain on the export ban list, but their exports will now be allowed with prior permission from the Ministry of Commerce. Molasses, de-oiled rice bran, wheat bran and stainless steel scrap can also be exported with prior permission from the Ministry of Commerce on a case by case basis (in the case of de-oiled rice bran and wheat bran, if the Ministry of Fisheries and Livestock Directorate fails to arrange marketing or take delivery of the items within a fixed time limit and at a reasonable price). These bans and restrictions which rest on trade reasons (to protect domestic consumers) should be removed. (Domestic consumers would be better served by removing import restrictions.)

5.15 There are a few items to which export ban is apparently applied for non-trade reasons. These are live animals, skins of animals and wildlife covered by the Bangladesh Wildlife (Preservation) Order, 1973, except for those species detailed in a schedule to the order; arms, ammunition, explosives and their ingredients; fissionable materials; maps and charts with some exceptions; rare items of archaeological interest; human skeletons; sea water shrimp below certain specified sizes and fresh water shrimp except for two varieties; and frogs, of all species (live or dead), and frog-legs. These bans, for environmental and other legitimate non-trade reasons can be retained except for arms and ammunition export which can be allowed if such export is found to be economically feasible. Many countries are found to profit from engaging in arms trade.

5.16 Exporting of non-perishable goods on consignment (sale or return) is banned. Firms wishing to export such goods are unable to export trial consignments on a sale or return basis since such exports are required to be against confirmed L/Cs. While banks may not like to take risks and finance such exports, individuals who want to take risks themselves should not be barred from doing so.

Relaxation of the current regulation is necessary to permit exploration and tapping of new product markets.

5.17 For exporters of woven garments, the domestic value addition requirement raised to 30 percent from a previous 25 percent had been in place until recently. The increased requirement, which was a misguided attempt to force exporters to obtain greater value added for these products, was seen by the producers as overly restrictive. As the actual value added often fell short of the 30 percent requirement, it forced the producers either to source their additional input requirements domestically at a higher cost or to import excess import requirements beyond the official limits illegally in collusion with customs officials, which also raised their costs. The regulation also discouraged the producers to produce high-value garments which required input content higher than 70 percent. The Government has now reverted to the earlier 25 percent domestic value addition requirement but with some qualification. The 25 percent requirement will be applicable for all non-quota categories of woven garments and for those quota categories of woven garments whose fob value per dozen is above US \$40. However, the rationale for the distinction being maintained now between quota and non-quota garments is unclear.

5.18 A manufacturer of jute products reported that jute mills which produce both jute yarn and other jute products from jute yarn are barred from exporting jute yarn. This ban was imposed when jute spinners producing only jute yarn protested against other mills engaging in export trade. This sort of ban violates private enterprise principles and should, therefore, go.

5.19 Another manufacturer reported that imports for re-exporting are subject to serious customs clearance problem. Duties are not due on imports for re-export. However, customs employees wanted duties to be paid on a consignment he recently imported for re-exporting purpose. It took three months for him to square up this problem with the customs authority but the process additionally cost him Tk 45,000 as demurrage for the delay in clearing the goods.

5.20 A ban also remains in place on the export of wet blue leather, although the policy document does not explicitly mention this. The ban was imposed with effect from a recent year to impel manufacturers to switch to production of finished or crust leathers. While the Government's objective may be good, a ban on the production of a certain good to achieve this objective is inappropriate as this does not duly take into account the adjustment costs to the private producers. Use of such an instrument is a bad substitute for that of an appropriately designed indirect economic incentive.

## **6. BANKING REGULATIONS**

### **6.A. Introduction**

6.1 Because of recent progress made in financial sector deregulation, currently only a few banking regulations remain in place which need to be reviewed in relation to their links to competitive market economy requirements and their consistency with the Government's industrial deregulation efforts. We first document recent progress made in financial deregulation and then review the current banking regulations.

### **6. B. Recent Progress Made in Financial Sector Deregulation**

6.2 Significant progress has been made in recent years in financial sector deregulation. Some of this progress falls in the realm of liberalization and relaxation of foreign exchange controls, which were examined earlier. The deregulations include:

- a) Interest rate deregulation.
- b) Discontinuation of central bank-directed credit.
- c) Discontinuation of subsidized central bank refinancing facilities.
- d) Relaxation of controls on private foreign (exchange) borrowing.
- e) Elimination of controls on foreign firms' access to domestic bank credit.
- f) Simplification of a number of foreign exchange-related transactions without requiring prior central bank approval.
- g) Withdrawal of central bank-fixed margins on loans against import L/Cs.
- h) Lifting of credit restrictions on trade in foodgrains and a number of other goods of daily necessity.
- i) Withdrawal of central bank-fixed margins and repayment periods on credits to certain transport sector transactions.
- j) Lifting of restrictions on post-import financing against all goods, imports of which are allowed by the import policy. The particular goods from which the financing restrictions have been withdrawn are edible oil and seeds, palm oil, refined salt, corrugated iron sheets, second-hand clothes and sugar.
- k) Lifting of restrictions on bank advances against land security.

- l) Withdrawal of restrictions on bank financing of stocks of airconditioners, complete bicycles, domestic refrigerators, electric fans, motor cars, trucks and buses.
- m) Lifting of restrictions on personal loans by banks against the security of gold and gold ornaments, fixed deposits and financial and security bonds such as Government Savings and Defence Certificates, Wage Earners' Development Bonds and ICB Unit Certificates, loans to hosiery industry and loans for internal trading activities in some products.

Of these deregulations, the last five were effected by Bangladesh Bank BCD Circular No.25 dated 25 October, 1993, and BCD Circular No.28 of 20 November, 1993 and BCD Circulars No.11 and 12 dated 6 and 7 June 1994. Liberalization of foreign exchange-related banking regulations was covered in Chapter 3. Elaboration of some of the other deregulations is in order and provided below.

### **6.B.1. Interest Rate Deregulation**

6.3 Deregulation in interest rates was initiated in FY 1989-90 in the form of (1) establishing interest rate bands within which banks were allowed to fix their lending and deposit rates and (2) making interest rate subsidies to their customers more transparent and reimbursable by the Bangladesh Bank. More recently (in March 1992), interest rates have been further deregulated. Lending interest rate bands have been abolished except for three sectors. These are agriculture, exports and small and cottage industries. The ceiling deposit rates have also been lifted, but floors are maintained on interest rates for term and savings account deposits. The current lending interest rate bands respectively for agriculture, exports and small industries are as follows:

- Agriculture : 11 - 15 percent (for all loans).
- Exports : 7.5 - 10.5 percent (for all loans).
- Small and cottage industries: 8 - 13 percent (for term loans only).

The current interest rate floors maintained on term and savings account deposits respectively are 5 and 4.5 percent. The floor rates were recently brought down from 6.5 and 5 percent.

### **6.B.3. Discontinuation of Central Bank-Directed Credit**

6.4 Quantitative credit restrictions, previously administered by Bangladesh Bank(BB), have been mostly eliminated. The scheme operated by BB to refinance directed credits by the commercial banks has been replaced by the regular rediscount window through which banks can borrow at the normal bank rate. Even credit norms previously prescribed by BB for working capital lendings in various sectors are no longer binding on commercial banks. Banks have been given near full freedom to make their lending decisions on the basis of banker-customer relationships. There are a few restrictions remaining which are being maintained on prudential grounds. These will be discussed later.

Nationalized commercial banks (NCBs), however, continue to remain subjected to directives from the Government (Ministry of Finance). This will also be discussed later.

#### **6.B.4. Elimination of Controls on Foreign Firms' Bank Borrowing**

6.5 Previously foreign-owned or foreign-controlled firms' working capital borrowing from banks were subjected to a ceiling and there was no provision for banks to extend term loans to them. These restrictions have been abolished.

### **6.C. Review of Current Banking Regulations**

#### **6.C.1. Remaining Credit Restrictions**

6.6 BB-directed credit has been generally discontinued. Some central bank restrictions, however, still remain on the following bank loans:

- a) Personal loans;
- b) L/C restriction for loan defaulters; and
- c) Advances against hire purchase with some exceptions.

6.7 Personal Loans: The central bank restrictions on personal loans against certain collateral securities have been withdrawn just recently in June 1994. However, some restrictions still remain: (1) advances against deposits in foreign currency accounts are subject to a maximum 50 percent limit of such deposits at the official exchange rate for a maximum period of 15 days; (2) advances against shares of companies are subject to a 20 percent margin requirement (at face value or at market value of shares, if less) for a maximum period of 30 days; (3) advances against life insurance policies are subject to a margin requirement of 20 percent of surrender value; and (4) advances against non-resident foreign currency deposits are subject to a 25 percent margin requirement. These restrictions also seem to be worth reviewing for their possible relaxation.

6.8 Ban on Import Letters of Credit Opening for Loan Defaulters: Banks have been advised not to open new L/Cs on behalf of importers until they have cleared their overdue loans. While this ban is based on a genuine concern regarding debt repayment, in some cases, loan repayments could be delayed for genuine temporary liquidity crisis. Banks could, therefore, be allowed to apply some flexibility in opening import L/Cs on banker-customer relationship basis. At the same time, BB could play some supervisory role to monitor such financing in order to provide a check against banks' fraudulent practices once the rigid ban on such financing is lifted.

6.9 Advances Against Hire Purchase: Bank advances for purchase or sale of goods on an installment or a hire purchase basis are banned except for machinery and equipments used in industry and agriculture and purchase of vehicles for commercial purposes. This ban should not apply to hire purchase for general trading purposes. However, its application to consumption loans seems in order in view of low domestic savings.

### **6.C.2. Prudential Regulations**

6.10 There are some credit restrictions and other regulations in place, which are based on prudential banking reasons. More stringent accounting regulations have been imposed on the banks to make provisions for bad debt and interest suspension and certain debt recovering measures have been introduced in order to improve the viability of the financial institutions to service financing functions on a long-term basis. In addition, for prudential and supervisory purposes, the Government has recently enacted the Banking Companies Act, 1991 replacing the Banking Ordinance, 1962. The Act is addressed to regulating private banking, especially to prevent misuse of funds by the controlling directors. It provides for more stringent capital adequacy standards. It restricts exposure limits in case of advances to loan defaulters and bank directors, and limits lending to a single borrower to 15 percent of the bank's capital for unsecured borrowing and 25 percent of capital for fully secured borrowing without prior approval of BB. Loan proposals exceeding such limits are required to seek BB's approval. Approval may be provided in appropriate cases after review of the concentration of the bank's loan portfolio. In order to ensure transparency of BB's approval procedures of such credits and reduce its discretionary powers, the Government/BB needs to establish some norms and criteria for approving such credits beyond the statutory limits for automatic approval.

6.11 A new Financial Institutions Act, 1993 has recently been passed by Parliament. This Act gives the central bank necessary powers to oversee and regulate the functioning of private non-banking financial institutions. This Act comes on the heels of the failure of two such financial institutions.

### **6.C.3. Financial Deregulation: An Evaluation**

6.12 Both the World Bank 1993 country economic memorandum (see World Bank 1993) and a very recent review of the FSRP project suggest that financial deregulation has not brought about the desired decrease in lending rates which are rather high considering the current low rate of inflation. The high interest rates are accompanied by high cash liquidity in the banks and a sluggish pace of investment. The key reason cited for interest rate liberalization not achieving the desired result is the dominance of the nationalized commercial banks (NCBs) in the banking system and their inefficient and uncompetitive banking operations. Some instances of lack of competition in the

operation of the Sonali Bank (the largest of the NCBs) are as follows:

- a) It does not engage in inter-bank buying and selling of foreign exchange; it sells only to BB.
- b) It did not participate in the buying of some government securities for profit taking.
- c) It does not close losing branches.

The burden of bad debt suffered by the NCBs was underestimated and the Government infusion of Tk 17,000 million to recapitalize them still leaves a very large amount of the banking system's bad loans, which may be in the order of Tk 60,000-80,000 million, according to the FSRP estimates. The capital infusion did not lead to any improvement in the performance of the NCBs.

6.13 Interest rates are, therefore, not satisfactorily liberalized because of the oligopolistic market structure of banks and the inefficiency of the NCBs. In this situation, greater competition in banking should be encouraged by the Government by allowing new private banks to operate. The Government has already started some action in this direction. Recently it was disclosed by the Finance Minister in Parliament that there was a lot of private sector enthusiasm to launch new banks. Some 42 applications seeking permission to launch new banks have been received by the Finance Ministry. Eleven of these applications have been approved by the Government and the remaining proposals are being examined. This is an encouraging development and the Government should ensure an ease of entry into this vital financial market. The Government should not restrict the number of new entrants into this business, but make the criteria for entry transparent.

6.14 Further interest rate deregulation through lifting of the interest rate bands retained for the three sectors mentioned previously is also worth consideration. Inter-sectorial interest rate differentials should be based on banks' perceptions of returns relative to risks of lendings to any sector and should, therefore, be left to the banks and financial institutions themselves. The three sectors are considered as priority sectors, and current general opinion among both businessmen and policy makers seems to favor preferential interest rates to be maintained for these sectors. However, experience suggests that getting access to credit rather than the interest rate is the more intractable problem. The supply-side problem appears to be a binding constraint rather than the demand for finance. In such a situation, it does not make any economic sense to maintain any sector-specific preferential interest rates. On the other hand, to the extent, such interest rates affect incentives, they distort the incentives and result in misallocation of resources.

6.15 In another important way, financial deregulation has not gone far enough. Although central bank-directed credit has been largely abolished, the Government, being the owner of the NCBs, directs their credit to specific sectors like that of jute. For example, up to June 1993, the jute sector was financed according to Government instructions routed through BB. Under the proposed jute sector adjustment credit of the World Bank, under negotiation, a transition period is envisaged when Government-directed credit to this sector would be temporarily allowed but not in the same form as before. Until June 1993, banks extended credit to this sector against hypothecation of stocks, which

led to inflation of stocks in the existing depressed market situation. A new formula has been devised for extending credit to this sector, which is related to export performance of the mills and a part of the mill's export proceeds is used to adjust outstanding loans. If this does not adjust the outstanding debt fully, the unadjusted part would be financed by the Government (1) in the case of private mills, to the extent of two-thirds of average losses incurred by the best five private and best five public mills and (2) in the case of public mills, to the extent of 100 percent of the above average losses. This new-formula government-directed credit is more market-oriented than before and ensures some debt recovery. This is understood to be an interim arrangement as part of the restructuring of the jute sector. However, directed credit in any form to a large industrial sector may not be an efficient way to promote optimal use of financial resources. It should, therefore, be phased out as quickly as possible.

## **7. LABOR REGULATIONS**

### **7.A. Introduction**

7.1 Weaknesses in the current labor laws and regulations and in their effective enforcement, which have a bearing on the needs for ensuring an efficient and competitive labor market, are subjects of review in this chapter. Labor laws of Bangladesh are, by and large, not so bad, but their effective enforcement is what is starkly lacking. Hence both these aspects, legal deficiencies and enforcement problems, need to be dealt with.

7.2 The labor market is considerably influenced by regulations and practices that affect wages, labor employment and termination terms, the labor dispute resolution process and general management-labor relations. A sustained period of good labor-management relations is an essential prerequisite for an environment conducive to private sector investment and growing production. The labor situation in Bangladesh is viewed by private entrepreneurs as, by and large, good. However, there have been strikes, lock-outs and other forms of labor unrest by organized labor on many occasions that have resulted in unwarranted ripples in the labor market. The environment has on occasions been made worse by inappropriate Government intervention.

7.3 Labor laws are contained in 46 or more existing pieces of legislation. There are inconsistencies in these various laws and it is necessary to simplify and consolidate them into an integrated comprehensive labor code. In what follows, we provide a review of the regulations which, we think, raise pertinent issues and need to be addressed. We note that a National Labor Law Commission, established in June 1992, has reviewed labor laws, and recently submitted its report to the Government. Since its report has not been made public, our review below could not take into account the Commission's views and recommendations on the various labor issues. However, references to some of the recommendations it has made according to some reports from the press and other sources are made in parentheses. It may also be noted that an earlier version of this PIAG report was made available to the National Labor Law Commission while it was finalizing its report.

### **7.B. Review of Labor Regulations**

7.4 These are discussed under the following headings:

- a) Regulations relating to trade unionism.
- b) Regulations relating to employment terms.
- c) Regulations relating to worker compensation.
- d) Regulations relating to the dispute resolution process.

#### **7.B.1. Regulations on Trade Unionism**

7.5 With some exceptions, labor laws allow industrial workers the right to form trade unions to establish a collective bargaining process for negotiating better wages and other employment terms for workers. One exception has been for industries set up in the Export Processing Zones. Trade unionism has also been banned in the state-owned Security Printing Press Corporation by a just

enacted Industrial Relations (Amendment) Act, 1993. Transport workers engaged in bus, truck and other transport business who hitherto could not engage in trade unionism have been allowed to do so by this Act. The Government is reportedly thinking of extending the right of trade unionism also to workers employed in industries in the EPZs. However, such a move would be neither necessary nor desirable at the present state of development. The EPZ industries are mostly foreign-owned or controlled and run by multinational firms. Workers in such firms already enjoy a much better status than average workers in non-EPZ industries. Unionism in these firms would definitely discourage foreign investors, a factor which should receive utmost consideration in view of the current very low flow of foreign direct investment.

7.6 Existing regulations allow retrenched or terminated but not dismissed workers of an establishment to remain or become members or office bearers of a trade union of that establishment. This provision is resented not only by employers but also by the majority of workers. Such workers cease to have any real stake in what happens to the status of a factory and it does not hurt them if it is closed. It would, therefore, be proper to disqualify all ex-employees for membership in an establishment's trade unions. This should promote healthier industrial relations at plant and industry levels. (The National Labor Law Commission has also reportedly made the same recommendation, but it was not supported by the workers' representatives. Despite the dissent shown by the workers' representatives, it would seem very important to disallow outsiders including ex-employees to engage in trade union activity as part of an essential process of depoliticizing labor.)

7.7 Regulations permit formation of a trade union in a business establishment if the union can command support of 30 percent of the workers, a provision which allows three unions in one establishment. This is an in-built invitation for unions to become rival organizations and to become politicized. Indeed, labor unions are highly politicized in Bangladesh. Some have links to the political party in power and others align themselves more closely with the mainstream opposition political parties. One of the trade unions can become the officially recognized Collective Bargaining Agent (CBA) for each establishment. To become the CBA, a trade union needs to enlist the support of only 33 percent of workers. A serious flaw of the current regulations is that the CBA could give notice of a strike, if such a move is approved in a secret ballot by 75 percent of its members. Thus the legislation permits workers to resort to a strike with support of only (75 percent x 33 percent) or 24.75 percent of the workers in an establishment. This legislation, therefore, allows a minority of the workers to decide for them in vital matters like calling a strike. Considering the undesirable possibilities under the current laws, it would seem desirable to change these to permit only one union in a factory and then only with majority worker support.

7.8 The current regulations do not allow the employers to change the employment conditions of union executives without prior permission of the Registrar of Trade Unions during the time when an application for registration of the union concerned remains pending with the Registrar. They also do not permit the employers to transfer president and general secretary of a union from one of its sections to another. These regulations unduly curb the power of the employer side to exercise legitimate control over his business. These restrictions should be either removed or modified appropriately by providing a time limit for registration.

7.9 Unionized labor in Bangladesh covers only 3 percent of the labor force but they are often found to exercise considerable influence because of their concentration in large industries in urban centers and because of their links with political parties. The labor unions are able to exert pressure through visible strikes, demonstrations or other forms of labor unrest. This situation enables the trade unions to often come up with unreasonable wage and other claims particularly in the public sector, which are not consistent with their productivity and a firm's profitability situation. Some have suggested that it would be desirable to restrict and ban trade unionism in new industries for a certain period, say, 3 to 4 years. This would encourage new investments and accelerate industrial development and would be more beneficial to labor as well in the long run in view of the current acute unemployment problem. (It is heartening to note that the National Labor Law Commission has also reportedly recommended a 3-year moratorium for trade union activity in new industrial enterprises.)

### **7.B.2. Regulations Regarding Employment Terms (Other than Wages)**

7.10 Regulations affecting hiring and firing of workers have an important impact on private sector competitiveness and employment creation. The regulations allow nearly full freedom to terminate worker's services. In two ways, however, the regulations are weak. First, employers are obliged to pay compensation in terms of gratuity and an employer's contribution to the provident fund for workers dismissed on disciplinary grounds. Although such compensation is hardly significant in terms of business cost involved, it encourages other workers to indulge in indisciplinary activities. This regulation should be suitably amended to exclude dismissed workers from benefiting from full compensation. Second, and as mentioned earlier, the law restricts the power of employers to change the service conditions of high union executives when an application for registration of that union remains pending. This regulation also needs to be appropriately amended. Hiring and firing of workers should be freely allowed by the law. The real problem faced in practice by employers in terminating worker jobs is undue union pressure brought against such terminations. This problem comes under labor law enforcement issues, which is discussed later.

7.11 The current regulations related to employment terms are deficient in another way. They do not allow for sufficient flexibility in employment contracts. Employers need to hire workers either on a permanent basis or on a daily casual basis. The law requires that a probationer is given a permanent status within a maximum period of six months. It should be possible for employers to employ workers on a fixed-term contract basis as well, which could be periodically renegotiated and renewed. The law should explicitly allow it. Fixed-term employment will enable employers to exercise more flexibility in meeting their production requirements, encourage them to hire more workers when a need arises, and lead to a healthier labor-management relationship. Furthermore, this contract basis would save the employer the requirement of going through the tedious process of determining the termination benefits at the end of the worker's contract.

7.12 The law provides for workers' termination or severance benefits in the form of gratuity at a minimum rate of one month's pay per year of service. Such severance benefits are high, compared to those in India and Sri Lanka, where gratuity is calculated at a minimum rate of a half month's pay for every year of service, with a ceiling on the absolute amount in India. The contributory provident

fund is not yet a statutory requirement in Bangladesh. Given the more generous practice observed in regard to gratuity, it would not be desirable to provide for the contributory provident fund requirement in the law, as this would raise the severance costs of workers and thereby affect prospects for employment expansion.

7.13 The regulations require employers to pay overtime allowance at double the wage rate. However, this creates a practical problem in calculating the overtime rate as wages defined in the Payment of Wages Act include bonus and all allowances which are paid annually. In India, overtime allowance is calculated on the basis of basic wages plus dearness allowances<sup>9</sup> only. A similar definition of overtime allowance should be adopted here also. Workers working on festival holidays are entitled by the law to compensation equivalent to two additional holidays plus a substitute holiday which is excessive compared to the practice, for example, in Singapore where such workers are paid an extra day's pay in addition to the pay for that day. A modification of the law to reduce the compensation on account of work on festival days entitlement would be in order.

### 7.B.3. Regulations on Wages

7.14 Wage determination in the private sector is affected by current regulations in at least three ways:

- a) By the regulations covering collective bargaining in industrial establishments where workers have become unionized.
- b) By minimum wages set by the Minimum Wages Board for private sector workers in different industries.
- c) Indirectly by minimum wages set by the Government for public sector workers.

A National Wages and Productivity Commission has recommended a national minimum wage, which if accepted and put into effect by the Government, would also affect private sector wages. In all of these ways private sector labor costs tend to be pushed beyond levels which would have been determined in a competitive labor market. The current regulations ignore the implications of increases in wages on employment and the existing unemployment situation as well as on private sector profitability and competitiveness. Furthermore, minimum wage legislation is primarily based on the legislators' perception of the cost required to support a worker and his family's minimum standard of living and has no link to his productivity. The trade-off between minimum wages, which push wages beyond market-determined levels, on one hand and employment and growth on the other is very serious for Bangladesh where poverty reduction and employment generation are the primary goals to achieve. Raising the income of some 2 to 3 million workers in the formal sector is less important than proper employment and poverty alleviation of a much larger block of informal day laborers.

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<sup>9</sup> This is an allowance added to the basic monthly wage in consideration of an inflation-caused increase in the cost of living.

7.15 In cases where the collective bargaining process fails or proves inadequate, wages are determined on the basis of the recommendations of the Minimum Wages Board, which recommends different minimum wage rates for different categories of workers in consultation with workers' and employers' representatives. The current minimum wages in force are those decided by the Minimum Wages Board in December, 1992. These wages range between Tk 630 per month in garments manufacturing and Tk 910 per month in fishing trawlers. The current practices of sectoral minimum wage setting are not only incompatible with the market principle, but also unorderly due to the weak institutional capacity and analysis on which they are based.

7.16 On the basis of the recommendations of the National Wages and Productivity Commission which presented its report in January 1993, the Government announced, in September 1993, minimum wages for public sector wages which have been increased in line with pay increases of government servants. The minimum wage has been set at Tk 950 plus other allowances. Such centralized wage setting ignores the universally recognized norms of the firm's ability to pay and the worker's productivity. The World Bank estimates that the current minimum wage means for jute workers more than 15 percent increase in worker's total compensation and around 29 percent increase compared to the compensation a year earlier (World Bank, 1993). Such increases in public sector minimum wages in total disregard of the industrial performance of public enterprises have been clearly unwarranted. This increase will directly affect the wages of workers in privately owned jute and textile mills and will exert an indirect influence on private sector wages in other industries.

7.17 The Government should not accept the National Wages Commission's recommended minimum national wage at Tk 900 per month. If given effect, this minimum wage would imply a 17 percent average increase in minimum wages currently paid by the private sector and as much as 30 percent increase in some key export sectors, such as, garments. Such a wage increase will affect private sector profitability and competitiveness and could discourage private investment and hamper the expansion of manufactured exports. A national minimum wage will also be difficult to enforce and if not fully enforced, it will probably lead to a deterioration in labor-management relations and thereby in the investment climate.

#### **7.B.4. Regulations Affecting Dispute Resolution Process**

7.18 The labor management dispute resolution process often goes through several steps, such as direct negotiation between labor and management, tripartite conciliation involving labor, management and the Government Labor Department, arbitration by an arbitration authority, settlement by labor courts, etc. This process often proves too time-consuming as there is no time limit specified from one step to another except from conciliation to the notice of a strike or lock-out which can be served by the Collective Bargaining Agent or the employer. The dispute resolution process would be expedited with reasonable time deadlines specified for each movement from one step to another in the chain. The time limits to be considered should be neither too long, to avoid delays, nor too short, for not jeopardizing the prospects for peaceful settlement of disputes. From this viewpoint, the current time limit of 10 days, specified for tripartite conciliation, is probably too short and a longer time limit in this case should be considered.

7.19 The current labor law requires a joint labor-employment reference of a dispute to a labor court for adjudication upon failure of conciliation proceedings. The requirement for joint reference, which seldom takes pace, means that disputes tend to linger on. To facilitate more expeditious dispute resolution, the current law should be amended to allow the labor courts to take up cases on reference by either party. The 1965 law on industrial relations allowed such a procedure.

7.20 The law allows Government intervention in the case of a strike or a lock-out. The Government has been empowered to terminate a strike or lock-out if it lasts for more than 30 days or at any time before the expiry of 30 days if it is satisfied that continuation of such a strike or lock-out is causing serious hardship to the community or is prejudicial to the national interest. This clause provides for unlimited government interference in labor disputes, which, instead of helping the dispute resolution process, sometimes hampers it. In a free market economy, the prescribed procedure for settlement of labor-management disputes should be given its fullest chance. It is important to ensure that failing firms can exit from the market when it is so required. When a private firm makes a decision to close, Government should not unilaterally interfere and force it to re-open. In the past, Government has forced some unviable private enterprises to re-open. The legal clause giving the Government the power of interference in labor disputes should, therefore, be appropriately amended to proscribe certain acts of interference, such as forcing the employer of a firm to end a lock-out or to reopen a factory if it is unilaterally declared as closed. The collective bargaining process has been harmed by frequent government interference. This is a subject we turn to in the next section.

### **7.C. Labor Law Enforcement Problems**

7.21 Non-enforcement of labor laws presents a serious problem. The Government is particularly lenient to labor. For political reasons, it often does not take any punitive action for an illegal strike. Some of the labor problems emanate from political motivation rather than for reasons of genuine labor welfare. Political parties maintain close links to labor leaders to woo labor support. Labor thus becomes politicised. This creates a hindrance in maintaining sound industrial relations and in effective enforcement of labor laws. On the other hand, existing labor law enforcement machinery, the Labor Department of the Government, the Labor Courts, etc., has not been very effective in resolving labor disputes. As a result, the labor code is often not applied.

7.22 Government interference in labor disputes has been too much and too frequent and its handling of the labor situation weak and inept. For example, the earlier Government's agreement in 1984 with the Sramic Karmachari Oikya Parishad (SKOP), which is the main representative body for all trade union federations, led to a sudden undue increase in wages and certain other changes. This agreement by-passed private sector employers and was inconsistent with the principle of tripartite consultations. The legal status of SKOP is questioned by employers. The present Government has also recently signed agreements with labor federations in jute and textile sectors and with SKOP, in the face of labor demands and agitation, including calls for country-wide strikes. These agreements have resulted in formation of a National Wages Commission to review wages in public sector enterprises and in increases in these wages before and following recommendations of the Wages Commission. These agreements also included a promise for establishing a statutory national

minimum wage to be applicable to the private sector workers and an assurance for further discussions with the labor bodies on the Government's denationalization program and other issues. As earlier pointed out, the recent wage increases in public enterprise workers are not economically justified. The other points of agreements also do not make economic sense. To establish labor-management relations on a sound footing, it is important that the Government cease to interfere in labor disputes outside the legally established formal machinery so that this machinery can play its due role.

7.23 It is necessary also to strengthen the existing labor law enforcing machinery. Illegal strikes and lock-outs should be dealt with in the manner provided for in the law. The Labor Court procedures are too lengthy, resulting in delays in the disposal of cases. These procedures need to be simplified to avoid delays. The Government in this context has taken an important step and has just enacted the Industrial Relations (Amendment) Act, 1993, which among other things, provides for speedy disposal of labor dispute cases in the courts by empowering these courts to dispose of cases without requiring the presence of any or both of the disputing parties. Other measures required for further simplifying existing procedures should also be taken. At the same time, it is necessary also to introduce, and ensure enforcement of, job security measures for workers, e.g., ensuring that workers are provided with appointment letters incorporating employment and termination terms and, when their jobs are terminated, requiring employers to provide them with termination compensation in accordance with the law. Cases of employment of workers without providing them formal appointment letters are not very unusual in the private sector, as complaints from some labor representatives seem to suggest.

## 8. LEGAL REFORM

### 8.A. Introduction

8.1 A sound legal system is an important ingredient of a congenial business environment. The laws and the judicial system in Bangladesh are inadequate to the demands of a modern economy. The system has serious deficiencies for providing effective support to the conduct of orderly business transactions. Some of the inadequacies of the legal system are reflected in the following facts. The system does not provide adequate assurances to the investors that contractual obligations will be honored or can be enforced and that the legal process will function properly. There is not an adequate guarantee that business loans can be recovered. The system does not enable speedy resolution of disputes. To promote efficiency of existing enterprises and accelerate growth, it is as important for failing firms to exit from the production system as for new firms to enter it. Existing laws and the legal process do not permit easy exit of firms as the necessary laws do not exist to establish the accountability of a company's directors when a company turns insolvent. The system does not guarantee that the audited accounts of business firms can be relied upon. There is no security of land titles. Undisciplined worker behavior is not properly dealt with.

8.2 Legal reform, therefore, remains an essential element of private sector development. Following a recent study made by FIAS (FIAS, 1992), the Government has made some start in reforming the legal system. Reforms in this area need, however, to be accelerated to gain private sector confidence and to promote industrialization based on foreign investment and international trade. In view of the FIAS work, this chapter will provide a brief update on the recent legal reform efforts and what remains to be done in this area.

### 8.B. Recent Progress in Legal Reform

8.3 Recent measures undertaken by the Government to improve the legal framework include the following:

- a) Enactment of the Banking Companies Act, 1991: As mentioned earlier, in Chapter 6, this Act has been recently enacted replacing the Banking Companies Ordinance, 1962 to empower the Bangladesh Bank to have some prudential control over the lending operations of private banks to prevent them from taking undue risk in providing secured or unsecured large loans to single borrowers.
- b) Enactment of the Financial Institutions Act, 1993: This Act also passed recently by Parliament provides for more prudential control of the Bangladesh Bank over non-banking financial institutions. This legislation followed the recent failure of two such institutions.
- c) Enactment of Industrial Relations (Amendment) Act, 1993: As mentioned in the preceding chapter, this amendment has been enacted, also recently, to provide for speedier disposal of labor disputes in labor courts by allowing these courts to proceed with cases even in the absence of any or both of the disputing parties. This Act also provides for restriction of trade unionism in the Security Printing Press.

- d) Preparation of a Draft on Amendment of the Companies Act, 1913.<sup>10</sup>: A draft revision of the Companies Act, 1913 has been prepared by a Law and Justice Ministry Committee, which is aimed at correcting the weaknesses and inadequacies of the existing law and making it more equipped to meet the modern-day requirements of corporate business. Some of the deficiencies of the existing law are lack of transparency of its provisions, the complexity of its legal procedures, inadequate provision for financial reporting requirements, unaccountability of the company directors, lack of assurance of protection for minority shareholders, etc.
- e) Preparation of a Preliminary Draft on the Amendment of the Bankruptcy Act, 1920: A draft for amending the 1920 insolvency law has been prepared with the help of US advisors. It is designed to modernize the legislation and legal process affecting bankruptcy. The old laws of 1909 and 1920 are not being used, and these laws suffer from serious shortcomings (e.g., absence of a provision for making the directors of a company liable who permit the company to continue business while insolvent and absence of or time-consuming court proceedings on bankruptcies and liquidation) which present a severe barrier to firms' exit or financial reorganization. The new draft is a first step in overcoming legal deficiencies in this area.
- f) Establishment of the Securities and Exchange Commission: This commission has recently been established following adoption of a new law to this effect. Its role would be to oversee and exercise general control over operation of the capital market and to help this market develop on a sound basis. The establishment of this Commission coincided with the dissolution of the office of the Comptroller of Capital Issues. The functions of the latter organization have been mostly taken over by the Commission.
- g) Formation of the National Labor Law Commission: As earlier noted, this Commission was established in June, 1992 to review labor laws and formulate recommendations for their amendment. The Commission has recently completed its work and submitted its report to the Government. The report has not been made public. The Government should make it public to elicit public reaction and evaluation of its recommendations by concerned people.
- h) Other Recent Legal Reform Steps Taken: One step taken is the establishment of special loan courts to help recover bank loans. The Foreign Private Investment (Promotion and Protection) Act of 1980 is being reviewed for appropriate amendment. This Act has certain provisions (e.g., some of those stipulating conditions for approval of foreign investment proposals) which have been overtaken by recent investment deregulation as well as other additional deficiencies. The amendment being considered will correct these deficiencies and is aimed at giving categorical assurance against nationalization or expropriation of the invested capital assets of the foreign investors. Work underway in another area relates to a review of the legislation on intellectual property which concerns the protection of trade marks and patents rights.

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<sup>10</sup> This Act was passed by Parliament as "the printing presses were rolling".

The 1911 Patents Law and the 1940 Trademark Law are outdated. They discourage innovation as they do not offer appropriate protection to developers. They particularly discourage investment in technology-based industries and discourage foreign investment.

### **8.C. Remaining Legal Reform to be Done**

8.4 While a good start has been made on improving the legal framework for trade and industry, the legal reform process should be accelerated to ensure a sound legal environment for business and to support more rapid industrialization based on foreign investment and international trade. Much work remains to be done in improving the judicial process as well as in basic law reforms.

8.5 Some of the key legal issues that need to be addressed include the following:

- a) The basic autonomy of the judiciary is missing. Some action is afoot to make the judiciary independent from the executive. The work needs to be accelerated.
- b) The litigation process in the courts has become unduly time-consuming due to legal shortcomings, understaffed judicial system and other problems. Reforms in this area are urgently needed. While shortcomings in some of the existing laws (e.g., faulty provisions for labor court procedures) have been addressed, those in others remain to be addressed along with improvements in the legal procedures themselves and judicial administration.
- c) The existing commercial legislation is outdated. The work in process to update this legislation (e.g., the Bankruptcy Act, the Patents and Trademarks Laws, etc.) should be completed with due urgency. Certain other pieces of legislation (e.g., the 1882 Land Transfer and Stamp Acts and the 1908 Registration Act) which also need updating should be considered for review.

8.6 The real problem with the Land Transfer Act, 1882, the Stamp Act, 1882 and the Registration Act, 1908 is that they are not practically implementable. In reality, dealing with real property has become an acute problem. With false title documents commonplace, parties avoid the registration of mortgages, liens and encumbrances of land because stamp duties and charges are excessively high. Another provision which creates considerable difficulty is that registered instruments, once they are registered, take effect from the date of execution (when the agreement is signed) and not from the date of registration. This means that until registration takes place title is uncertain, so that a bonafide purchaser or mortgagee can still be defeated by a title or interest purportedly created earlier but registered subsequent to this. Another, more intractable, problem is the difficulty of ascertaining title to land and the existence of any encumbrances because of poor record keeping practices and storage facilities in many of the registration offices. It is also not clear, under the present law, whether foreign investors can purchase and own land in Bangladesh, or whether they can only lease.

8.7 Recent studies and surveys on impediments to investment in Bangladesh list access to credit as a major constraint to investment. Traditionally, finance for purchase of machinery and equipment has been from the investor's own funds or from banks. The alternative method of finance, leasing of equipment, has not really developed in Bangladesh, unlike other parts of Asia. Also unlike the situation in India, a bank in Bangladesh cannot engage in leasing activities because of a prohibition in the Banking Companies Ordinance.

8.8 The FIAS study has offered numerous specific recommendations to deal with the legal system problems and issues noted above. A summary of the key recommendations, a number of which have already received Government attention, are reproduced as Attachment 3.

## **9. INDUSTRY-SPECIFIC REGULATIONS**

9.1 While more research needs to be done in this area, it appears that many of the relevant regulations are import-control-related. These were reviewed in Chapter 4. In addition, a few industries have been identified as being adversely affected by specific regulations. Below we review these regulations by industry.

### **9.A. Regulations Affecting the Pharmaceutical Industry**

9.2 The pharmaceutical industry appears to be most severely affected by a plethora of regulations. Brief accounts of the regulations affecting this industry were provided in the chapters on investment controls and import controls. The controls on this industry fall into the following categories:

- a) General production controls.
- b) Special production controls for foreign firms.
- c) Controls on imports of raw materials.
- d) Controls on imports of finished drugs.
- e) Controls on product prices.
- f) Controls on advertising expenses.

#### **9.A.1. General Production Controls**

9.3 Under the Drugs (Control) Ordinance, 1982, registration of 1,666 harmful, unnecessary or otherwise undesirable drugs was cancelled or suspended, which means that their production remains banned. No drug can be manufactured and/or imported and sold in Bangladesh without prior registration with the Directorate of Drugs Administration of the Government. The banned drugs appeared in a Drug Administration publication in 1985 (Drug Admin., 1985). There are three lists:

Schedule I: This is a list of what were identified as harmful drugs.

Schedule II: This is a list of drugs which cannot be produced without reformulation as prescribed and noted in the Schedule.

Schedule III: This is a list of drugs which have been banned for various other reasons.

9.4 These elaborate controls on the production of drugs need to be critically reviewed not only because the reasons used in the case of many of the drugs are either protectionist in nature or just some notion of essentiality of the particular products or some concern for 'wastage' of foreign exchange, reasons which are not economically justifiable, but also because the reason of 'harmfulness to health' used in the case of many drugs can also be suspect on critical scrutiny. There is no good rationale for banning internationally recognized safe drugs which can and do find their way into Bangladesh illegally. The continued ban on such products only encourages smuggling and deprives the economy of an opportunity to itself produce these goods. Furthermore, Bangladesh could produce

some of these drugs for the export market. These controls are hindering the expansion of the pharmaceutical industry.

### 9.A.2. Special Production Controls for Foreign Firms

9.5 Foreign (multinational) firms have been barred by the National Drug Policy (Drugs Administration, 1986) from producing certain products or product ranges such as antacids and vitamins except injectable vitamins. Vitamins in syrups were previously banned for all producers, but B-complex syrup was later allowed for local producers, but not for foreign firms. The Drug Policy also does not allow production of foreign brand medicines under license if the same or similar products are available or manufactured in the country. Foreign firms are also not allowed to market on commission basis any products produced by another factory in Bangladesh. Although the number of explicitly mentioned drugs which are banned for foreign firms is not large, they seem to face some additional *de facto* (if not *de jure*) discrimination *vis-a-vis* local producers through the control exercised by the Drugs Administration in the process of registering or licensing drugs. Although, all foreign firms may not view the production restrictions for them as too serious, the current policy as such is inappropriate as a matter of principle. It definitely works as some disincentive to foreign investment. Such restrictions contradict the Foreign Investment Act clause that foreign private investment shall not be accorded a less favorable treatment than what is accorded to similar private investment by the citizens of Bangladesh in the application of relevant rules and regulations.

### 9.A.3. Controls on Imports of Raw Materials

9.6 Producers of pharmaceutical products are restricted to import only up to the quantities and values of raw and packing materials as mentioned in a Block List approved by the Drugs Administration, irrespective of their entitlement for those items entered in their Pass Book. They are not allowed to import any items outside the Block List even if such items are otherwise freely importable. Since the manufacturers have to restrict themselves to the Block List-specified quantities of each and every item of raw material, the restrictions create the following problems for them:

- a) The restrictions add to the inventory cost of manufacturers; to reduce uncertainties associated with obtaining raw materials under the Block List systems, they are required to keep extra 4 to 6 weeks of stockpiles.
- b) The manufacturers face a delay in introducing a new product as it requires a revision of the Block List; a Block List revision is cumbersome and time-consuming; it also requires registration of the new product with the Drugs Administration;
- c) The Block List restrictions also prevent the manufacturers from exercising full freedom in the choice of sources of supply of their raw materials since orders for small specified quantities cannot be placed with the cheapest sources of supply.

9.7 The existing raw material controls, therefore, do not make any sense. Such controls on inputs do not in any way ensure product quality although one of the stated purposes of such controls is to ensure product quality. Product quality should be ensured by random sampling tests carried out by the Drugs Administration, by publicizing these results through the mass media so that consumers can take precautionary measures and if necessary introducing other additional appropriate measures such as banning the sale of sub-standard drugs. Controls on raw material prices (these are controlled through quantity and value ceilings) also do not make any sense since these discourage the production of quality drugs and together with controls on product prices they discourage the production of drugs in relatively high demand and thus they hamper the growth of the industry. Imports of some of the pharmaceutical raw materials are also restricted for purposes of protecting domestic industries which are producing them. These restrictions are also unjustified and should be withdrawn.

#### **9.A.4. Controls on Imports of Finished Drugs**

9.8 Imports of reportedly as much as 95 percent per cent of the commonly used medicines are banned. This ban is applied to protect the local drug manufacturers. The ban should be withdrawn along with the withdrawal of restrictions on imports of raw materials. Manufacturers will then operate in a competitive market environment which will ensure both quality of products and competitive prices.

#### **9.A.5. Controls on Product Prices**

9.9 The maximum retail prices of drugs are set by a Price Fixation Committee chaired by the Secretary, Ministry of Health. Price controls, as already mentioned, discourage production of goods in higher demand and hamper the growth of an industry. Without complete freedom of pricing, quality of production also cannot be ensured. If a competitive market situation is ensured through the lifting of controls on the imports of finished drugs, the market will automatically guarantee that manufacturers do not charge unduly high prices. The controls on prices should, therefore, go.

#### **9.A.6. Controls on Advertising Expenses**

9.10 Drug manufacturers are subject by the Drug Policy to a ceiling restriction on their advertising expense, of 5 per cent of sales. Also, under the current policy, they are not allowed to provide samples as a way of promoting their products. The manufacturers feel that the control over advertising should be removed from the drugs licensing authority (Drugs Administration) and administered by a separate self-regulating body within the industry.

9.11 The above account shows that the pharmaceutical industry has been subject to a plethora of controls, which are hurting the growth of this industry. The Ministry of Health appointed a committee in 1992 to review the Drug Policy, 1982 and the Drug (Control) Ordinance, 1982. That committee's work was suspended because of a high court injunction towards the end of 1992. A new

committee has been recently appointed by the Government to resume the review of controls in this industry. The review should be done on a priority basis to free the industry from so many unhealthy controls.

## **9.B. Regulations Affecting the Sugar and 'Gur' Industries**

9.12 The Government protects the country's public sector sugar industry (1) by a strict quantitative regulation of imports, generally allowed only by the Trading Corporation of Bangladesh (TCB) on behalf of the Bangladesh Sugar and Food Industries Corporation (BSFIC), the same corporation producing sugar by its 16 sugar mills, and (2) by restricting sugarcane supplies to indigenous 'gur' producers by banning the use of power crushers for gur production in specified sugar mill zones. The Government thus protects the domestic sugar industry (1) by giving monopoly rights of importing and distributing sugar to the BSFIC to meet the gap between domestic consumption and production, (2) by allowing the mill authorities to sell sugar at a protected government determined price, and (3) by restricting gur production in sugar mill zones.

9.13 All these controls are economically unjustifiable. The level of protection which the sugar industry is presently being accorded should be subjected to critical review by the National Tariff Commission. The protection should be provided not by a pre-determined price but in the form of an appropriate tariff on sugar imports. Sugar should be allowed to be imported freely by private importers. The restriction on gur production should be lifted. All of these controls limit competition in the sugar industry. The argument that the industry has a right to coerce sugarcane farmers to supply sugarcane to only sugar mills as they benefit from the mills' supervised credit deliveries does not carry much weight. Restricting the production of one good for purposes of protecting another industry is economically unacceptable. The sugar industry should be allowed to compete freely with gur.

## **9.C. Regulations Affecting the Readymade Garments Industry**

9.14 The readymade garments industry of Bangladesh has been an outstanding success story. A reference to regulatory problems which affect this industry may, therefore, sound rather strange. Two key measures which have particularly helped this industry are the special bonded warehouse arrangement by which it can import its inputs duty and tax-free and the back-to-back letter of credit arrangement under which it can import its requirements on a deferred payment basis against a master export L/C. However, two regulatory irritants they currently face are as follows:

- a) Restriction on cash imports.
- b) Restriction on imports of inputs.

### 9.C.1 Restriction on Cash Imports

9.15 As mentioned in paragraph 3.13, all of the garments manufacturers' raw and packing materials import requirements have to be met through back-to-back L/C arrangements. They are not even allowed to draw on their retained 5 percent foreign exchange (in addition to 70 percent that goes to pay for imports under back-to-back L/Cs) to import these materials. They can only use this foreign exchange for such things as importing machinery, travel, and participation in international fairs. It would be desirable to permit these producers to also use their cash foreign exchange for importing raw and packing materials. As argued in Chapter 3, there is in fact a strong case for offering a general option to all importers on back-to-back L/C basis to have the alternative facility of importing on cash foreign exchange basis.

### 9.C.2 Restrictions on Imports of Inputs

9.16 One import restriction applies to grey (greige) fabrics. Garments manufacturers are not allowed to directly import grey fabrics (in lieu of finished fabrics) except for pocketing and interlining requirements as determined by the Utilization Expert Committee constituted by the Ministry of Commerce or the relevant customs Statutory Regulation Order (SRO). This seems to be an unnecessary limitation. Textile finishing units, operating under the bonded warehouse system, are, however, allowed to import grey fabrics for finishing purposes and for sale to export garment units and for direct export. Export garments units should also be allowed this facility, regardless of whether they have finishing facilities themselves, since they can arrange to have them finished by others. The only thing to be noted carefully by customs people will be to guard against import of fabrics on a duty-free basis in excess of the requirements to meet export orders. This can be done easily. The garments manufacturers will of course, normally prefer to import finished fabrics rather than grey fabrics. However, the choice should be left to them. There is no point in imposing a regulatory restriction on them.

9.17 Another import restriction applied is with respect to the form in which fabric imports are allowed. Such imports are allowed in rolls or 'thaans' of regular or continuous lengths of 20 yards or above. Imports of fabrics cut into pieces or sizes are not allowed. It is not clear why this restriction was introduced. The restriction prevents the garment manufacturers from choosing cheaper fabrics. It might have been introduced for administrative convenience as the standard prescribed sizes allow the customs people to keep track of the imports more easily. Whatever be the reason, the regulation needs to be critically evaluated for its possible removal or streamlining.

## **10. RECOMMENDATIONS**

The survey of the industrial regulatory system presented in the preceding chapters enables us to offer a number of specific recommendations aimed at its further liberalization and improvement to facilitate and accelerate private sector-led industrial development in Bangladesh. Rationales for the recommendations are not repeated here. For the rationales, the reader is referred to the relevant sections of the report. The recommendations are grouped and presented according to the various regulatory policy areas covered in the paper.

### **10.A. Recommendations on Investment Controls**

10.A.1 Identify and publish transparent and well-defined guidelines for industries to obtain clearance on environmental grounds.

Action: By the Ministry of Environment and Forest and the Environment Directorate

10.A.2 Withdraw the existing ban on investment in and threatened but temporarily suspended ban on the production of polythene shopping bags and amend the relevant 1991 Industrial Policy provision which urges discouragement of the production of jute substitute synthetic fibers.

Action: By the Ministry of Industries in consultation with the Ministry of Environment and Forest

10.A.3 Remove all existing general investment and production controls in the pharmaceutical industry and special controls applied to foreign investors in the pharmaceutical and readymade garments industries.

Action: By the Cabinet Division and the Ministry of Health and Family Welfare

10.A.4 Accelerate the transformation of the Board of Investment into an investment promotion agency and remove its following regulatory functions:

- a) Eliminate the functions of approving terms for private foreign loans that fall outside of a Government-established range of conditions and of approving foreign exchange remittances of royalties, technical know-how and technical assistance fees, consultancy fees and overseas training costs.

Action: By the Cabinet Division and the Ministry of Finance and Bangladesh Bank

- b) Consideration should be given to transferring the function of recommending input requirements of firms from the BOI to the Ministry of Commerce in consultation with the chambers of commerce and industry.

Action: By the Board of Investment and the Cabinet Division

- 10.A.5 Remove the Industrial Policy provision which discourages bank financing of industries on market saturation grounds. (Such decisions would best be left to the investors and financing institutions themselves and not be dictated by Government bureaucracy. The current ban on bank financing of investment in edible oil refining should be removed. The probable prospective categorization of some new industries, such as electric fans, corrugated iron sheets, mild steel rods, and single-phase electric meters as over-saturated industries should not be allowed to materialize. However, it would not be inappropriate for the Government to provide the results of its market analyses to banks and potential investors.)

Action: By the Cabinet Division and the Ministry of Industries

- 10.A.6 Remove the existing restriction on imports of second-hand or reconditioned machinery requiring certification that it has a minimum economic life.

Action: By the Ministries of Industries and Commerce

- 10.A.7 Remove the existing requirement of approval by the Bangladesh Bank for the repatriation of foreign exchange from the divestment of foreign invested capital. [The remittances should be a normal bank transaction on the production of relevant documents showing the invested amounts involved.]

Action: By the Ministry of Finance and the Bangladesh Bank

- 10.A.8 Accelerate enactment of the updated draft of the patents and trademarks laws and ensure their rigorous enforcement.

Action: By the Ministry of Industries and the Ministry of Law, Justice and Parliamentary Affairs

- 10.A.9 Remove the existing restrictions on foreign firms' commercial imports and treat them on the same footing as domestic firms.

Action: By the Ministry of Commerce

- 10.A.10 Make transparent the rules and facilities available for entry of new private investment in energy (gas and electricity) and telecommunications sectors. Remove the difference in prices of gas charged to the Power Development Board and industrial users for power generation purposes<sup>11</sup>.

Action: By the Ministry of Energy and Mineral Resources and the Power Development Board and the Ministry of Posts and Telecommunications

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11 The Government decided to reduce the price of gas charged to private users of gas in power generation by about 30 percent as "the printing presses were rolling", but this still does not fully remove the price discrimination between the Power Development Board and the private users of gas.

- 10.A.11 Engage the services of international agents to perform offshore duty assessment in association with import pre-shipment inspection. Introduce the requirement of pre-shipment inspection on a compulsory basis for non-tariff-value items and extend this system to tariff-value items by phasing out the system of tariff values.

Action: By the Ministry of Finance and the National Board of Revenue

## 10.B. Recommendations on Exchange Controls

- 10.B.1 Free private borrowing from abroad from the remaining approval control of the Board of Investment.

Action: By the Cabinet Division, the Ministry of Finance and the Bangladesh Bank

- 10.B.2 Allow exporters to operate their foreign currency accounts with retained foreign exchange (the permitted five to ten percent of export earnings) with the facility of both-way convertibility. (Currently, once exporters use these funds for local purchases, they are not allowed to reconvert them into foreign exchange.)

Action: By the Bangladesh Bank

- 10.B.3 Allow exporters, operating on a back-to-back letter of credit basis, to import raw and packing materials and spare parts with cash foreign exchange up to their retained foreign exchange -- five to ten percent of exports. Provide a general option to exporters operating on back-to-back L/C basis to import on cash foreign exchange basis if the latter basis is preferable to them.

Action: By the Ministry of Commerce and the Bangladesh Bank

- 10.B.4 More liberally allow access to cash foreign exchange for imports without the requirement for letters of credit.

Action: By the Ministry of Commerce and the Bangladesh Bank

- 10.B.5 Extend the facility of import against direct payments abroad to foreign investors. (Currently, this facility is available to only Bangladeshi nationals living abroad.)

Action: By the Ministry of Commerce

- 10.B.6 Considerably relax, at least double, the current general modest ceilings on official foreign exchange available for personal trips abroad. Withdraw foreign exchange restrictions altogether for business travel by both producers of export and import-substitution products,

or at the least, fix their general foreign exchange entitlements well above those for personal trips.

Action: By the Bangladesh Bank

10.B.7 Remove the existing foreign exchange restrictions for educational tours and those for seminars and workshops, etc.

Action: By the Bangladesh Bank

10.B.8 Lift the control on capital transfers and make the Taka convertible also on the capital account as early as possible.

Action: By the Ministry of Finance and the Bangladesh Bank

10.B.9 Put the Taka on a free float against other currencies.

Action: By the Ministry of Finance and the Bangladesh Bank

### 10.C. Recommendations on Quantitative Import Restrictions

10.C.1 Eliminate remaining quantitative restrictions (QRs) on imports for trade (i.e., protection) reasons. (Items which in the Import Policy Order 1993-95 remain subject to QRs number 111 at four-digit HS level, of which one is a heading redundancy and eight are subject to only inspection / labelling / quality requirements, 47 are unambiguously identified as subject to QRs for non-trade reasons of health, security, religion, etc. and the remaining 55 items are subject to QRs for trade reasons. Of the 55 items, 14 are associated with controls by the Drugs Administration, and the rest are subject to other types of restrictions as detailed in Table 2 of Chapter 4.) The recommendation applies to items shown in Table 2 and further specifically breaks down into:

- a) Allowing unrestricted import of sugar by private importers.
- b) Removing the Drugs Administration-associated restrictions on imports of 14 four-digit items.
- c) Removing QRs from imports of another 40<sup>12</sup> four-digit items.

Action: By the Ministry of Commerce in consultation with the Ministries of Industries and Health and Family Welfare

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12 Import restriction on one of these items, newsprint, was withdrawn as "the printing presses were rolling".

## 10.D. Recommendations on Export Controls

- 10.D.1 Allow re-exporting (entre pot trade) on a more liberal basis than at present by rescinding the requirement for value addition after import, extending its applicability to all products and removing the official permission requirements. Allow duty-free status to imports for re-export.

Action:

- a) By the Ministry of Commerce
- b) By the National Board of Revenue for according duty-free status to imports for re-export.

- 10.D.2 Allow exports on consignment (sale or return) basis for all goods.

Action: By the Ministry of Commerce

- 10.D.3 Allow exports of samples and imports of samples of unrestricted-import-category items for export purposes without value restrictions.

Action: By the Ministry of Commerce

- 10.D.4 Remove remaining bans and restrictions on exports of a number of agricultural and manufactured products, with the exception of those which can be retained for non-trade reasons of environment, resource depletion, etc.

Action: By the Ministry of Commerce

## 10.E. Recommendations on Banking Regulations

- 10.E.1 Review for possible removal or relaxation remaining central bank restrictions on personal loans by banks against the security of deposits in foreign currency accounts, shares of companies, life insurance policies and non-resident foreign currency deposits.

Action: By the Bangladesh Bank

10.E.2 Quickly phase out Government-directed credit to the jute industry through the nationalized banks.

Action: By the Ministry of Finance

10.E.3 Lift the remaining Government-directed interest rate bands for loans to agriculture, exports and small and cottage industries.

Action: By the Ministry of Finance and the Bangladesh Bank

10.E.4 Relax the existing ban on loan defaulters opening letters of credit to accommodate credits to such defaulters who are suffering temporary cash liquidity crunches. The decisions can be left to the commercial banks.

Action: By the Ministry of Finance and the Bangladesh Bank

10.E.5 Encourage the entry and growth of private banks to make the banking operations more competitive.

Action: By the Ministry of Finance

10.E.6 Extend the application of lending for hire purchase to general trading purposes, while keeping the ban on consumption loans.

Action: By the Bangladesh Bank

## 10.F. Recommendations on Labor Regulations

10.F.1 Do not interfere in labor disputes other than through the legally established machinery. Remove legal loopholes (e.g., the authority given to the Government to intervene in the case of labor strikes or employer lock-outs) which allow excessive Government interference in labor disputes.

Action: By the Cabinet Division and the Ministry of Labor and Manpower

10.F.2 Cease the Government practice of reaching wage agreements with unions or their national federation, the SKOP (the Sramik Karmachari Okkya Parishad), by-passing tripartite consultations.

Action: By the Cabinet Division and the Ministry of Labor and Manpower

- 10.F.3 Cease the current centralized practice of determining wages for public sector workers without regard to profitability of firms and productivity of workers.

Action: By the Ministry of Labor and Manpower

- 10.F.4 Do not attempt to impose a national minimum wage for private sector workers.

Action: By the Cabinet Division and the Ministry of Labor and Manpower

- 10.F.5 Repeal the regulation that allows retrenched or terminated workers of an establishment to become or remain members or office bearers of that establishment's trade union.

Action: By the Ministry of Labor and Manpower and the Ministry of Law, Justice and Parliamentary Affairs

- 10.F.6 Eliminate the multiplicity of trade unions in an establishment. Workers should be represented by the union with majority worker support.

Action: By the Ministry of Labor and Manpower and the Ministry of Law, Justice and Parliamentary Affairs

- 10.F.7 Impose a time limit to the inability of a firm to change the employment conditions of union officials, or to transfer union presidents or general secretaries among sections of its plant, during the pendency of a union's application for registration.

Action: By the Ministry of Labor and Manpower and the Ministry of Law, Justice and Parliamentary Affairs

- 10.F.8 Relieve the employers from the requirement to pay workers dismissed on disciplinary grounds both gratuity and the employer's contribution to the provident fund.

Action: By the Ministry of Labor and Manpower and the Ministry of Law, Justice and Parliamentary Affairs

- 10.F.9 Allow the provision for employment of workers for fixed term contracts in addition to the presently allowed employment on the basis of permanent and casual (daily) statuses.

Action: By the Ministry of Labor and Manpower and the Ministry of Law, Justice and Parliamentary Affairs

- 10.F.10 Impose appropriate time limits on progress between most steps of the dispute resolution process to accelerate dispute resolution, and increase the insufficient time limit specified for the tripartite conciliation step to give reasonable scope for this step to have success.

Action: By the Ministry of Labor and Manpower and the Ministry of Law, Justice and Parliamentary Affairs

- 10.F.11 Amend the current legal requirement, seldom met in practice, for joint labor/employer reference of disputes to labor courts for adjudication.

Action: By the Ministry of Labor and Manpower and the Ministry of Law, Justice and Parliamentary Affairs

- 10.F.12 Amend the labor law appropriately to remove the lack of a clear definition of the basis for double pay for overtime (which should exclude annual bonuses), and the excessive requirement for triple pay and substitute leave for work on festival days.

Action: By the Ministry of Labor and Manpower and the Ministry of Law, Justice and Parliamentary Affairs

- 10.F.13 Enhance enforcement of labor legislation by strengthening the Labor Department, further streamlining labor court procedures, penalizing illegal strikes and lock-outs in accordance with the law and introducing and ensuring enforcement of necessary job security measures, e.g., ensuring that workers are provided with appointment letters incorporating employment and termination terms and, when their jobs are terminated, requiring employers to provide them with termination compensation in accordance with the law.

Action: By the Ministry of Labor and Manpower

## **10.G. Recommendations on Legal Reform**

- 10.G.1 Expeditiously finalize and enact the completed draft amendments to the Bankruptcy Act, 1920, the Foreign Investment Promotion and Protection Act, 1980, and the laws relating to patents and trade marks.

Action: By the Ministries of Industries, Commerce and Law, Justice and Parliamentary Affairs

- 10.G.2 Accelerate the process started to ensure the basic autonomy of the judiciary.

Action: By the Cabinet Division and the Ministry of Law, Justice and Parliamentary Affairs

- 10.G.3 Remove legal shortcomings and understaffing of the judicial system, and address other existing problems including deficiencies in the legal procedures themselves and judicial administration to quicken the litigation process.

Action: By the Ministry of Law, Justice and Parliamentary Affairs

- 10.G.4 Enable commercial banks to finance equipment leasing.

Action: By the Ministry of Finance and the Bangladesh Bank

- 10.G.5 Update other antiquated legislation, e.g., the Land Transfer Act, 1882, the Stamp Act, 1882 and the Registration Act, 1908, and consider implementing other still relevant recommendations for legal reform made by the Foreign Investment Advisory Service (Refer to Attachment 3 for the FIAS recommendations).

Action: By the Ministries of Land, Industries and Law, Justice and Parliamentary Affairs

## **10.H. Recommendations on Industry-Specific Regulations**

- 10.H.1 Remove general bans on the production of many drugs and special production restrictions applied for foreign firms, bans and restrictions on imports of drugs and on raw materials of drugs being applied for protecting domestic production of such products, and controls on the quantities and prices of importable raw materials of drugs and those on the prices of drugs and advertising expenses of pharmaceutical firms.

Action: By the Cabinet Division, the Ministry of Health and Family Welfare and the Drugs Administration

- 10.H.2 Remove the ban on the crushing of sugarcane applied to specified sugar mill zones to restrict "gur" production.

Action: By the Ministry of Industry and the Bangladesh Sugar and Food Industries Corporation (BSFIC)

- 10.H.3 Allow manufacturers of readymade garments for export to import part of their import requirements outside the back-to-back letter of credit system, up to their foreign exchange retention benefit.

Action: By the Ministry of Commerce in consultation with the Ministry of Finance and the National Board of Revenue

- 10.H.4 Allow readymade garments units, producing for export, to import grey fabrics regardless of whether they have dyeing and finishing facilities.

**Action:** By the Ministry of Commerce in consultation with the Ministry of Finance and the National Board of Revenue

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**TERMS OF REFERENCE  
STUDY ON INDUSTRIAL REGULATORY SYSTEM  
MINISTRY OF INDUSTRIES**

The objective of this regulatory study is to survey the key elements of the regulatory framework for industry so as to provide a clear indicator of where Bangladesh stands with respect to the process of implementing regulatory reform now underway. In particular, the goals are:

- i) To identify regulatory policies or interventions that may be justified by health, safety or environmental concerns or by considerations stemming from the role of the state in managing natural resources, preventing fraud or enforcing contracts.
- ii) To identify areas where past initiatives at deregulation aimed at opening up markets and creating a competitive economy have been accomplished in law, but not in fact; identify the obstacles to effective implementation; and develop an action plan to overcome these obstacles.
- iii) To identify other areas where unnecessary regulations remain in effect and devise further initiatives at deregulation.

Sub task (i) is intended to separate out regulatory policies involving legitimate reasons for industrial regulations from all other regulations. Some of these regulations are being analyzed in greater detail in other projects (i. e., the ADB study on environmental regulations). This regulatory study is intended to complement, rather than duplicate this work. PIAG will mainly concentrate on sub tasks (ii) and (iii) and work to eliminate remaining regulations that restrict competition or favor narrow interests rather than society at large.

Particular areas that will be covered under sub tasks (ii) and (iii) include the following.

**Quantitative Restrictions (QRs) on Imports:**

The stated policy is to eliminate QRs that cannot be justified by non-economic considerations (i.e., safety and national security). To what extent has this been accomplished in the Import Policy Order (IPO) to be effective July 1993? Are there any import restraints or requirements that are practiced but not authorized in the IPO? Propose an action plan for eliminating the remaining QRs that are protectionist in nature. Propose easy procedures for administering justified restrictions. Identify the scope for shifting consumer protection controls from the import regime to more general procedures that would also capture domestically produced and smuggled goods.

**Exchange Controls:**

Foreign exchange controls have been eased by eliminating some restrictions and by providing

automatic approval of other transactions that do not fall outside guidelines established relative to earnings or sales levels for firms. Have the efforts at decontrol been implemented successfully? Could the remaining restrictions be eased further or eliminated?

### **Investment Controls:**

A major effort has been undertaken to remove controls on investment activity that were used to protect existing capacity or to substitute government for private decision making on the potential profitability of new investment. Have all constraints been eliminated for private firms? If not, develop an action plan for eliminating any remaining constraints based on protectionist rationales.

### **Export Controls:**

Controls on exports have reportedly been eliminated with the exception of some constraints on re-exports, sales on consignment, and a short list of product specific bans or restrictions. Has this decontrol of exports been effectively implemented? Evaluate the rationale for continued constraints. Should these constraints be eliminated or phased out in line with further progress in foreign exchange market liberalization?

### **Labor Regulations:**

This is an area where some regulations may be justified on safety and health protection, but where others may mainly restrict competition or protect existing workers from competition from others in the labor market. The extent of deregulation should be documented and the potential for further deregulation evaluated.

### **Banking Regulations:**

The efforts to deregulate industry should be linked to simultaneous efforts to develop a more competitive banking and financial system. The study should identify regulations that impede on the financial transactions of private firms and identify those that are protectionist in nature. (Note: This section of the study should be conducted in close collaboration with the Financial Sector Reform Project, to ensure the appropriate balance between prudential banking and client convenience.)

### **Legal Reform:**

The impact of the legal system on investment and operations of industrial enterprises is being considered by a Committee on Law Reform, encouraged by the World Bank's ISAC-2 and a 1992 report coordinated by its FIAS arm for the MOI. Some regulations may be justified because the legal system is poorly developed (i.e., those aimed at preventing fraud). These linkages should be explored with an eye to the opportunities for further deregulation in line with improvements in the legal system.

### **Industry-Specific Regulations:**

There may be extensive remaining regulations set specifically for different industries. Again these need to be evaluated relative to the underlying rationales. Restrictions aimed at preventing competition should be identified and eliminated or phased out. A few industries may be selected in consultation with the Chambers to serve as case studies to illustrate the scope for such deregulation.

In examining the above areas of regulation and procedure, the study should place emphasis on how the regimes are implemented in practice. What type and magnitude of transactions costs are imposed on business in seeking to comply with (or avoid) them. Do these costs differ among small versus large, urban versus rural, old versus new, local versus foreign, public versus private, and production versus financial versus trading business enterprises? Are the local officials responsible for administration well informed of the current rules? Is the business community kept informed? Both discussion with organized business (the Chambers) and interviews with various classes of individual entrepreneurs should be used to assist these assessments.

The resulting study should also provide the basis for a decision on whether to try and produce a relatively comprehensive Operative Regulatory System (ORS) document for wider distribution. If developed, the ORS would be intended to make the system much more transparent and assist in assuring that reform initiatives are well publicized and effectively implemented. The ORS could be revised periodically as progress is made in deregulation.

**NAMES OF FIRMS OR ORGANIZATIONS AND PERSONS  
INTERVIEWED**

NAME OF FIRM / ORGANIZATION	NAME OF PERSON / DESIGNATION	REGULATORY ASPECTS COVERED
Board of Investment (BOI)	M. Mustafizur Rahman, Executive Chairman Dr. Syed Yusuf Faruk, Member Mashiur Rahman, Director, Services Charles Byron, Chief Technical Advisor	Investment controls
Ministry of Commerce	Nazem Ahmed Chowdhury, Secretary	Import controls
Bangladesh Small & Cottage Industries Corporation (BSCIC)	Md. Maniruzzaman Chowdhury, Chairman S. M. Altaf Hossain, Deputy General Manager Abu Taher Khan, Assistant General Manager	Investment controls
Dhaka Chamber of Commerce & Industry (DCCI)	A T M Waziullah, President Syed J. Haider, Senior Vice-President	Investment controls
Bangladesh Bank	Mahbubul Amin Khan, Deputy Governor Abdur Raquib, Executive Director  M. Mohsenur Rahman, General Manager, Foreign Exchange Murshed Kuli Khan, Deputy General Manager	General control aspects  Banking regulations  Foreign exchange regulations Banking regulations
Financial Sector Reform Program (FSRP) Project	Forrest Cookson, Consultant	Banking and foreign exchange regulations
World Bank Resident Mission	Dr. Shamsuddin Ahmed, Senior Program Officer Charles Cookson, Consultant  Syed Nizamuddin, Senior Program Officer	Import & export controls, banking & foreign exchange regulations, and investment controls Labor regulations
Metropolitan Chamber of Commerce and Industry (MCCI)	Latifur Rahman and C.K. Hyder, President and Secretary General C. K. Hyder, Secretary General	Some preliminary briefing on the survey Import controls, export controls

NAME OF FIRM / ORGANIZATION	NAME OF PERSON / DESIGNATION	REGULATORY ASPECTS COVERED
Bangladesh Employers' Association	M. Meherullah, Labor Advisor	Labor regulations
Ministry of Finance Bangladesh Shilpo Bank (BSB)	Dr. A. K. A. Mubin, Joint Secretary, Ministry of Finance and Managing Director, BSB	Banking regulations
Foreign Investors Chamber of Commerce and Industry	Mahbub Jamil, President (also Chairman & Managing Director, Singer Bangladesh) Jahangir Bin Alam, Secretary	Regulations affecting foreign investors
Environment Department	Mohammad Reazuddin, Deputy Director	Investment controls
National Labor Law Commission	Justice M. A. Quddus Choudhury, Chairman M. H. Sobhani, Legal Draftsman	Labor regulations
Bengal Fine Ceramics Opal Garments IMFEX Enterprises	R. Maksud Khan, Deputy General Manager	All regulatory aspects
Bengal Ceramic Industries Neaz Boat & Shoe Industries	Shamsuddin Ahmed, Managing Director	Ditto
DCCI	Mohammad Yunus, Ex-President	Ditto
Saudi-Bangla Fish Feed	A. Y. Md. Kamal, Managing Director	Some regulatory aspects
Sidko Limited (Garments) SKM Jute Mills	Feisal Siddiqi, Managing Director	All regulatory aspects
Transcom Electronics Bangladesh Lamps Bangladesh Electrical Industries	Obaidur Rahman Khan, Executive Director Aminul Huq, Accounts Officer	General regulatory aspects
Moqbulur Rahman Jute Mills	Momenur Rahman, Director	Banking regulations with respect to financing for jute
CONEXPO (Exporter of handicrafts)	Abu Alam Chowdhury, Director	Export problems affecting small exporters
Quasem Group Industries (Textiles & other)	Mayeedul Islam, Chairman. A. K. M. Mainul Islam, Managing Director	Foreign exchange, banking and labor regulations
Rahima Food Corporation (Edible oil refining)	Golam Quddus Chowdhury, Deputy Executive Vice President	Investment and import controls

NAME OF FIRM / ORGANIZATION	NAME OF PERSON / DESIGNATION	REGULATORY ASPECTS COVERED
Givenchy Group of Industries (Knitwear, dyeing, etc)	Khatib Abdul Zahid Mukul, Managing Director	Investment and other regulatory aspects
BASF Bangladesh (Producer of textile & leather chemicals)	K. H. Ruecker, Managing Director	Investment problems facing foreign investors
Grindlays Bank	David F. Robinson, General Manager, Bangladesh.	Banking and Foreign Exchange Regulations
Pfizer Laboratories (now renamed Renata Limited)	S. H. Kabir, Chairman & Managing Director Abdul Hai, Materials Manager	All regulatory aspects
New Zealand Milk Products, Bangladesh	Syed Fazle Rabbi, Chief Executive	General regulatory aspects
Bangladesh Tobacco Company	Malcolm Fry, Managing Director Khurram Hussain, Chief Accountant	Ditto
Drugs Administration	Chowdhury Mahmood Hasan, Director S. H. Sikdar, Superintendent	Controls on pharmaceutical industry
Ceiba-Geigy (Producer of pharmaceutical products, agro-chemicals, dyes and chemicals for textiles, leather, etc)	Mobarak Ali, Finance Director	Industry specific controls affecting pharmaceutical industry and foreign investors
Newage Group (Garments and knitwear)	A. S. M. Quasem, Managing Director	All regulatory aspects

## **FIAS STUDY RECOMMENDATIONS ON THE LEGAL SYSTEM**

1. Institute basic law reforms:
  - a) Ensure greater autonomy and independence of the judiciary.
    - \* Repeal the amendments to Articles 115 and 116 of the constitution.
    - \* Establish a Judicial Appointments Committee.
  - b) Establish a Permanent Law Reform Commission.
    - \* Permit commercial legislation to be enacted in both Bengali and English.
    - \* Establish a cadre of professional legal draftsmen.
  
2. Modernize outdated commercial legislation:
  - a) Update the 1913 Company Law.
    - \* Simplify procedures for company formation.
    - \* Provide for reporting requirements to ensure transparency and provisions for the removal and liability of directors to ensure accountability.
    - \* Include minority shareholder protective provisions.
  - b) Arrange for full enforcement of the 1909 and 1920 Insolvency Laws.
    - \* Establish director's liability for trading while insolvent.
    - \* Provide mechanisms, like the American "Chapter II" bankruptcy proceedings, to allow for the reorganization of companies.
    - \* Establish expeditious procedures with time limits for the payment of creditors and for winding up.
    - \* Include periodic reporting requirements with personal liability for making false or misleading reports and for the certification of such reports.
    - \* Establish a Bankruptcy Bench in the Supreme Court.
  - c) To review the 1861 Admiralty Act, engage the services of an international lawyer

specialized in Admiralty and Aviation Law to review and comment on the Corporate Laws Committee's 1990 draft revision recommendation.

- d) To review the 1911 Patent Law and the 1960 Trademarks Act, either resuscitate the now defunct committee established to re-examine the draft Trademarks Act and Patent Act submitted to the Government in 1990 or make this a priority matter for the proposed Permanent Law Reform Commission.
- e) The 1882 Land Transfer and Stamp Acts and the 1908 Registration Act.
  - \* Reduce the registration fees and stamp duties on mortgages.
  - \* Provide that the registration of instruments will be effective from the date of registration, not the date of execution.
  - \* Reform and modernize the Land Registration Offices so that title to land and any encumbrances can be determined quickly, reliably and efficiently.
- f) Leasing and Investment.
  - \* Amend the Banking Companies Ordinance to allow commercial banks to enter the leasing sector.
- g) Labor Legislation.
  - \* Enact a new comprehensive Labor Code to rationalize the now applicable 47 different codes, ordinances, rules and regulations to provide an integrated framework for establishing the rights and duties of both employers and employees, and to provide speedy and effective access to justice for aggrieved persons. This should be another priority item for either the ad hoc commission for Examination of Labor Laws which was recently formed, or for the proposed Permanent Law Reform Commission.
- h) Foreign Private Investment (Promotion and Protection) Act of 1980.
  - \* Update the Foreign Investment Act to bring it in line with the changes made in the 1991 Industrial Policy Statement.
  - \* Broaden the scope and interpretation of foreign investment.
  - \* Include more transparent entry criteria, liberalize approval requirements and build-in incentives where relevant.

### 3. Reform of Judicial Administration Process and Law Enforcement:

- a) Give original side jurisdiction to the High Court division of the Supreme Court in

cases involving more than Tk one million.

- b) Increase the number of sitting Supreme Court Judges through the appointment of additional judges under Article 98 of the Constitution and provide them with the necessary court rooms, chambers and facilities.
- c) Authorize the Chief Justice to implement a case management program and provide funding to modernize court facilities and equipment.
- d) Address the abuses of the judicial process.
  - \* Assess costs on a progressive scale for repeated adjournments.
  - \* Impose costs and discipline counsel for asserting senseless and frivolous defenses.
  - \* Impose interest at 2% above commercial bank rate on awards in commercial legislation.
  - \* Require the posting of a significant percentage of an award to lodge an appeal.
- e) Establish a Permanent Judicial Training Institute and a Practicing Law Institute and provide them with the necessary facilities.

#### 4. Reform of Administrative Procedures:

- a) Establish a Permanent Administrative Law Reform Commission to rationalize existing rules, regulations and procedures.
- b) Establish a cabinet level Administrative Law Committee to vet all regulations and to ensure that they do not conflict with other regulations.
- c) Reform administrative practices:
  - \* Establish deadlines for action and institute automatic approval procedures.
  - \* Establish an Inter-Ministerial Implementation Committee and an Administrative Law Tribunal.
  - \* Publish rules, regulations and procedures; establish public reporting requirements; and publish a Handbook of commercial investment laws, regulations and procedures.
  - \* Streamline anti-corruption procedures and appoint an Ombudsman as provided in Article 77 of the Constitution.

Attachment 4

**REMOVALS AND RETENTION ON THE CONTROL LIST, FEBRUARY, 1993**

A. Items made freely importable

The removal of controls over imports under 100 four-digit tariff headings<sup>13</sup> has been formalized with the publication of the Import Policy (Amended) Order, 1991-93 in February 1993. The deletions comprised (with no. of HS-4 headings in parentheses):

- \* Garments (excluding used clothing); carpets; fishing nets; footwear; umbrellas (34)
- \* CKD, CBU, used trucks, buses and 4 WDs; used motor cars; chassis and bodies; auto-rickshaws; CKD and used motor cycles; bicycle parts; aircraft and parts; oil tankers (13)
- \* Salted, dried or smoked meat; sugar, saccharine; confectionery, chocolate; tea; rice (7)
- \* Tobacco; cigarettes and other tobacco products (3)
- \* Refined petroleum products; gas (2)
- \* Printing ink; non-soap washing and cleaning preparations; matches, asbestos cement articles (4); welding electrodes; hand tools; razor blades (3); lanterns; toothbrushes; combs; pens and pencils (5)
- \* Used tires (1)
- \* Unscheduled newspapers and periodicals; paper correspondence products; cheque forms, bank notes and stamps; calendars (4)
- \* Jewellery, bangles; silver and gold products; coin (10)
- \* Lathes; bandsaw machines; plastic moulding machines; jute mill spares (4)
- \* Fluorescent ballasts and tubes; bulbs; rechargeable batteries; transformers; special accumulators; insulators (4)
- \* Plastic/ceramic sanitaryware; porcelain/glass table/ kitchenware; utensils (6)

B. Items remaining restricted

The items within 93 four-digit headings in the Control List (but not sugar, petroleum and those only in the IPO text) that remain under restriction or ban pending the new FY94-95 IPO may be grouped as follows according to their presumed rationale.

Protection (37):

- \* Unrefined edible oil (2)
- \* Biri leaves (1)

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<sup>13</sup>The same 100 headings which were "recommended for withdrawal" in a list provided to the IMF in September 1992 with the exception that kitchen and table utensils have been deleted instead of film censorship.

- \* Salt (1)
- \* Soap (1)
- \* PVC < 8" pipe; plastic housewares; padlocks < 3"; ceiling fans; newsprint; electricity meters (7)
- \* Cotton, synthetic, artificial, metallized and silk woven, mesh and knit fabrics; nylon and polythene rope; tape (18)
- \* Household linen; cloth and polythene wrapping; cleaning cloths, life-jackets and dress patterns (6)
- \* Rags and used clothing (2)

Religious and social concerns (18):

- \* Live swine; fresh, chilled and frozen pork; FCF offal of any meat except poultry; sausages; pig and poultry fat, lard and stearin; pig bristles (8)
- \* Ghas, bhang and opium; artificial mustard oil (2)
- \* Beer, wine, spirits and other fermented beverages and preparations; wine lees (7)
- \* Cinema films (1)

Public health and safety (27):

- \* Vegetable extracts, pectines etc; sulphonamide; vitamins; hormones; antibiotics; organs, blood and vaccines; medicaments; enzymes (12)
- \* Sulphur; phosphorous; potassium chlorate; nitrates; TNT; explosives (10)
- \* Radioactive materials and reactor fuel elements (4)
- \* Insecticides, fungicides and herbicides (1)

Political and defence (11):

- \* Tanks and AFVs; warships; arms (8)
- \* Radio transmitters and navigation apparatus (2)
- \* Civilian ships except tankers (1)



