"THE IMPACT OF CORPORATE GOVERNANCE ON FINANCIAL DISTRESS: EVIDENCE FROM LISTED FINANCIAL INSTITUTIONS IN SRI LANKA"

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Abstract

ETI finance (Private) Limited, Seylan bank, S. R. Property Sharing Investment (Private) Limited are a few entities among a large pool of other entities that collapsed due to financial distress in Sri Lanka during the past two decades. The fallout of each these collapses resulted in thousands of victims who had to suffer and bare these losses without any proper composition. And each of these collapses were accompanied by malpractices of the board of directors or the senior management and the overall failure of the corporate governance structure. So, this study is an attempt to understand the role of corporate governance in predicting financial distress within the finance sector of Sri Lanka. Several researches have been done on this topic, but none has solely focused on the financial sector of the country. So, a research gap exists within the literature in this context. Board Size, Board gender diversification, Frequency of board meetings, Audit quality, Board member remuneration, CEO duality, Education level of the board members, Board independence are the key measure of corporate governance of this study. Additionally, Firm size, profitability and firm leverage is incorporated to the study as control variables to enhance the findings of the study. And financial distress is measured on the basis of an institute having a negative profit, cash flow or worth for more than three years as the unique nature of financial institutions prevents traditional methods of measuring financial distress such as Altman Z score model in providing reliable results. This research has used all listed financial institutes of Sri Lanka as its population and seventy-two of them were selected as the sample of study. Data will be collected from primary data sources (i.e. financial statements) from 2017 to 2022. In this study, descriptive analysis, Pearson correlation analysis, and regression analysis are used to analyze the data. Accordingly, the findings of this study do provide a better understanding of how corporate governance structure of financial institutions can be used to predict institutions who are at the risk of being financially distressed. The findings of this study will supplement and enhance the decision-making process of investors, savings holders and any other related party. Also, the organizations that resides within the financial sector them self will be able to incorporate the findings of this study when incorporating corporate government policies to avoid future financial distress situations followed by inappropriate governance practices. And finally, the policy makers will be able to incorporate these finding of this paper when implementing new policies or modifying the existing governance policies.

Keywords – *Corporate governance, Financial distress, Code of best practice, Profitability*