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Evaluating Corporate Governance in Albania: A Comparative Study of Board of Directors, Mechanisms and Managerial Practices

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Abstract: *Corporate governance has become a critical issue globally, facing increasing scrutiny from regulators, investors, and the public, particularly in rapidly developing nations. This study examines corporate governance in Albania, focusing on board practices, challenges, and areas for improvement. Using a mixed-methods approach, it analyzes corporate governance through secondary data from annual reports and financial statements of the top 29 companies by income, alongside exploratory qualitative insights from interviews with key corporate stakeholders.*

Findings reveal a varied landscape, while some firms demonstrate effective governance, others face challenges like conflicts of interest, lack of board independence, and inadequate disclosure. Key improvement areas include stronger regulatory frameworks, more diverse boards, and increased shareholder engagement.

This research contributes to the limited literature on the corporate governance domain in Albania, offering insights into the local context as well as serving as a foundation for future studies and initiatives to enhance governance standards, fostering a corporate culture of transparency, accountability, and stakeholder protection.

1. INTRODUCTION

The foundation of corporate governance (CG) is a system of transparent interactions between an institution's management, board, shareholders, and other stakeholders, which also serves as a framework for determining internal dynamics. It serves as a structure or system of rules, policies, norms, practices, and processes that serve the purpose of directing and controlling a firm transparently. It is also considered a set of strategies that help align the interests of investors and management of the firm while ensuring that the firm runs for the benefit of investors. Corporate governance as a continuously evolving discipline, is to be highlighted for addressing critical questions about how organizations operate and their ability to protect themselves against a variety of threats.

Following corporate scandals like that of Enron, WorldCom, and HIH Insurance, etc. because of poor governance and as the likelihood of a possible next financial crisis is often present, the CG structure has since been brought into the spotlight, with recently increased development of the corporate governance practices in businesses. The OECD Principles of Corporate Governance, originally issued in 1999 and revised in 2003, have turned into the international benchmark standard for good corporate governance practices, and form now the basis for effective initiatives in this domain. The OECD Principles are divided into five major categories: shareholder rights, equitable treatment of shareholders, the role of stakeholders in corporate governance, disclosure and transparency, and board responsibility (OECD, 2004).

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Despite the fact that the regulatory environment for CG is evolving in Albania, corporate governance compliance is not largely implemented. In terms of research too, there are very few studies on the topic, with existing studies being limited to the banking sector. Furthermore, although the effects of CG mechanisms such as the board of directors and ownership structure have been extensively researched in various countries, yet no study has been conducted in Albania. Such existing gaps called for further research into CG practices in Albania, where literature is very limited regarding various CG aspects like board composition and ownership concentration.

Focusing on a comparative analysis of board size and composition, board activity, and ownership concentration among others, this study gives an overview of corporate governance principles in Albania and related implications which comprises also the main objective of this study. In this context, by examining how the board of directors in Albania is established as a mechanism of corporate governance, paying particular attention to the board composition, diversity, and ownership concentration, this study will help determine whether there are any shortcomings in firms operating in Albania concerning board size and composition, ownership structure, and other corporate governance standards.

2. LITERATURE REVIEW

Corporate governance (CG) has a rich history rooted in the evolution of corporations and trade. It addresses fundamental issues arising from the separation of ownership and control within organizations, which has long been recognized as a potential source of conflict and inefficiency. Although principles of CG have been 'around' for centuries, the term "corporate governance" was coined in the 1970s as governments, international organizations, and stock exchanges began formalizing standards to address these challenges. Major corporate scandals and financial crisis highlighted the severe consequences of poor corporate governance, especially when bad actors and self-interested groups were mixed into the board of directors, emphasizing the need for effective frameworks.

Depending on the disciplinary interest or context, there are numerous ways to define, describe or outline Corporate Governance, broadly defined as the system by which companies are managed and controlled, or as the set of rules and practices that an organization establishes to oversee all its business activities. It should be emphasized that by 'control' it is referred to the degree firm stakeholders exert influence or control over people in charge of planning and running the company's operations. CG largely involves a 'set of relationships between a company's management, its board, shareholders, and other stakeholders' (OECD, 2004, p.11). This framework provides the basis for setting organizational goals, the means of achieving them, and the criteria for measuring performance. Charreaux (1997) defines it as the organizational controls that govern the behavior of managers and define their discretionary powers. According to Shleifer and Vishny (1997), corporate governance is concerned with ensuring that suppliers of finance for firms receive a return on their investment. Goergen and Renneboog (2006) define it as a set of mechanisms that ensures management manages the company for the gain of one or more stakeholders. According to Shailer (2018), it describes the processes, structures, and mechanisms that influence firm control and direction. Meanwhile, Wolfensohn (1998), Malla (2010) and Tricker (2022) emphasize the importance of fairness, transparency, accountability, and socially responsible governance practices in safeguarding stakeholder interests and societal trust. The evolution of corporate governance as a domain reflects ongoing efforts to adapt to new challenges and ensure that businesses operate in a fair, transparent, and accountable manner. Increasingly, firms are realizing that good governance and higher standards of corporate governance are not only necessary to ensure accountability but also to positively improve corporate performance (Clarke, 2022).

What is known today as Corporate Governance can be explained by both the convergences and divergences of several theoretical approaches, each grounded in distinct economic, social, legal, and historical contexts. Among these, the most prominent and debated theories are the Agency Theory, Shareholder Theory, and Stakeholder Theory. Agency Theory, rooted in the "principal-agent" problem which can be traced back to the work of Adam Smith (1776) and Berle and Means (1932), is a central framework in corporate governance. This theory addresses the relationship between shareholders (principals) who own the company and managers (agents) who run it. The core idea lies in the separation of ownership and control of the firm as a fundamental issue in modern corporations, leading to conflict or what is known as the agency problem. Shareholder Theory instead posits that the primary responsibility of a firm is to maximize shareholder value and that a firm's only obligation is to its shareholders, who are the rightful recipients of the company's profits. It can be traced back to the work of Milton Friedman (1962) who notably argued that a firm's sole social responsibility is to stockholders, of course within the constraints of free-market capitalism. The Shareholder Theory has faced criticism for encouraging short-term thinking and neglecting the interests of other stakeholders. Meanwhile, Stakeholder Theory prioritizes all parties who can affect or are affected by the achievement of the firm's objectives including shareholders, managers, employees, suppliers, customers, other businesses, etc. Unlike agency theory where managers are expected to serve the shareholders' interests, stakeholder theory suggests that managers serve a network of relationships both internally and outside of firm borders (Freeman, 1999). This latter approach is argued to converge more with the principles of corporate governance.

OECD (2004, 2015) has set a global standard and reference for best practices that can be adapted to different national contexts in this area with the OECD's Principles of Corporate Governance, established initially in 1999 and revised since then, that provide a fundamental framework based on four key principles: accountability, transparency, fairness, and responsibility. These principles are essential for guiding corporate strategy and decision-making. Accountability ensures that business decisions are justified and that risks are managed, which is crucial for building trust with shareholders and other stakeholders. Transparency involves the accurate and timely disclosure of important company information enabling informed decisions. Fairness emphasizes ethical practices and fair treatment of all stakeholders. Lastly, Responsibility requires a clear strategic direction, with the board of directors capable of effective oversight of the firm's management, and proactively considering the interests of all parties, including non-shareholder stakeholders.

The board of directors is considered as the main mechanism of corporate governance, and the activity of boards heavily shapes and influences corporate governance. Legal and regulatory obligations of a relevant geography can shape the foundations of a board, which can range from a highly regulated environment that mandates board membership and responsibilities to no applicable rules at all, depending on the country in which the firm is headquartered. The board, which is generally made up of insiders and independent members, is responsible for making critical decisions. An independent director has no relationships with the company, its affiliated firms, or its officers that could interfere with, or be reasonably believed to interfere with, the director's independent business judgment in the best interests of the company (OECD, 2004). Another critical issue is the number of independent directors on the board. It is largely agreed upon that the duality of the CEO and Chairman may either boost the CEO's decision-making speed or diminish the Chairman's monitoring responsibilities, thus affecting business value (Ma & Tian, 2014).

According to Carter et al. (2003), many corporate executives believe that there is a beneficial relationship between board diversity and shareholder value. Board diversity has long sought to promote a diverse range of demographic qualities and characteristics in the boardroom, including age, gender, race, educational background, and professional skills. Overseeing the management team, making critical decisions on key issues such as mergers and acquisitions, determining executive compensation, and ensuring that the company complies with regulatory requirements are all part of effective board activities. Board activity reflects the board's level of involvement in monitoring, as the board has the authority to make critical decisions and supervise the board of management. Ownership concentration refers to the allocation of the company's shares among its shareholders. Structures of control and ownership are critical components of corporate governance. These structures aid in determining how power and decision-making authority is distributed within an organization. When ownership is concentrated among a few shareholders, it can have an impact on corporate governance since these shareholders may have undue influence over the company's decision-making. Ownership and control may be closely related in some circumstances, such as in family-owned enterprises, where the founder and their successors retain ownership and influence over the company's future.

Corporate governance is increasingly important in developing countries too, due to globalization and rising capital mobility. It's particularly crucial for countries that have transited from centralized to market economies, where past government monopolies left little room for private ownership like in the case of Albania. The necessity for corporate governance practices in Albania is a result of the liberalization and privatization processes of formerly state-owned enterprises which have lasted for many years. The establishment, organization and exercise of commercial activity are well-regulated with a decent legal basis. The government and business sectors have been active in developing and attempting to implement corrective policies, such as policies that aim to significantly reduce corruption and increase transparency, accountability, fairness, and responsibility. Despite this, the implementation of corporate governance principles has been limited. This is partly because Albania has a voluntary corporate governance code, which is rarely followed. In 2011, the Ministry of Economy, Trade, and Energy (METE) of Albania adopted the Corporate Governance Code for unlisted companies in Albania, closely related to the OECD Principles (Dibra & Bezo, 2021). The Code's application is entirely voluntary, and it is meant to serve as a good practice reference for unlisted companies to build solid governance frameworks, however, there is little evidence of the implementation and monitoring of the code. Another important reason is the lack of a Stock Exchange with real operational activity, given that generally stock exchanges have played the role of disclosure and compliance monitoring for standards, and are considered as strong promoters of corporate governance recommendations for listed companies.

In light of the gap in research for the case of Albania, the researchers seek to conduct a comparative analysis of Board of Directors practices in Albania, with a particular emphasis on the role of the board of directors, board size, board independence, board composition, diversity, and ownership concentration.

3. METHODOLOGY

The primary objective is to study the concept of corporate governance, and its mechanisms particularly board composition, ownership concentration, and board activity, thus one could consider this as qualitative empirical research. Due to the lack of previous studies, notably in the case of Albania, an exploratory study through content analysis of company reports and other documents is conducted. The structure of the Albanian economy is dependent on several sectors, including energy, mining, agriculture, technology, and information technology, thus including companies from various industries was considered important.

The sample of companies used for this study was selected through purposive sampling from the list of 200 most profitable companies operating in Albania for the year 2022 (*Monitor 200*) as listed by Monitor Magazine (Monitor Magazine, 2023). This list is compiled based on the data retrieved from the General Directorate of Taxation and the financial statements deposited in the National Business Center (NCB). The sample composed of the top 29 companies of the list, included companies covering most of the significant industries. The selected sample provided wider access to their reports, financial statements, etc. The initial intention was to focus on the top 30 companies, but the last ranked company lacked the necessary data to be included in this study.

The proposed study is focused on the use of secondary data in order to produce more solid and triangulated conclusions. The data has been accessed from secondary data sources. Information about the board of directors and ownership concentration data are secondary data and obtained from annual reports and financial statements at Trade Register (NCB) and on multiple occasions are available on companies' websites. The National Business Center (NCB) database and official business websites were used to get all financial data, company profile, ownership structure and board structure for the companies included in the study.

4. EMPIRICAL FINDINGS

The companies covered in the study make a significant contribution to Albania's GDP and cover the most important sectors in the economy. Table 1 below gives an overview of their commercial activity.

Table 1. Distribution of the sample by commercial activity

Commercial Activity	*No. of firms*
Financial Services - Banking	7
Telecommunication	2
Retail	4
Oil and Gas retailing	2
Construction & Engineering	7
Production of construction materials	2
Food and drinks processing	2
Other	3

Source: Own research

62% of the firms included in the study have more than 20 years of economic activity and are still operating in the market, followed by 24% of firms with an activity of 11-20 years, and 14% of the firms with a maximum of 10 years of activity. In terms of the legal form, they are almost equally divided into limited liability companies (Shoqëritë me Përgjegjësi të Kufizuar, SHPK) and joint stock companies (Shoqëritë Aksionere, SHA), and very few of them as PPP (Public Private Partnership) or branches of MNCs. While limited liability corporations are more frequent in Albania, joint stock companies are commonly utilized by larger enterprises, particularly those seeking external investment or a higher level of transparency.

According to the observations, companies in Albania generally have a board of directors in charge of overall management and strategic decision-making. There is no explicit rule that specifies a minimum or maximum number of board members for corporations in terms of board size, though boards appear to be small. A smaller board may be more agile and efficient, yet a larger board may bring in more knowledge. Nevertheless, this does not appear to be the case in Albania. It is difficult to determine whether boards have a diversified mix of skills as companies do not disclose the board members' qualifications. Overall, boards of directors in Albanian firms appear to perform a wide range of tasks, including oversight of the company's operations, strategic direction, financial performance, and sustaining good corporate governance principles. Despite this, it was impossible to find any board evaluation practice used to assess the activities of boards as this information was not disclosed.

As a means of analysing *Board Composition* of firms, the researchers of this study observed the repetition of the same surname among board members. Such a case basically would mean filling board seats with family members, clearly a sign of a lack of board independence. The board composition, consequently, ownership structure, personal relationships, and power dynamics within the Albanian companies might generate issues about meritocracy and nepotism, thereby undermining the organization's fairness values (Demaj, 2012).

Table 2. Repetition of the same surname in the company

Repetition of the same last name in the company	Frequency	Percentage
No repetition of the same surname twice or more	20	69
Repetition of the same last name twice or more	9	31
Total	29	100.0

Source: Own research

According to observations as seen in Table 2 above, 31% of the firms have a repetition of the same last name twice or more, while in 69% of them, there is no repetition. This can be a result of the fact that in Albania, family businesses prevail, and this pattern of concentrated ownership coexists with a strong understanding of shareholder rights and the significance of transparency. 31% of the firms in this study have at least two or more individuals with the same last name; this condition is more prominent in the firms with Albanian ownership. Among the firms where the same last name is repeated twice or more, 70% of them have entire Albanian ownership, which proves once more the family relationships domination among Albanian firms. These links can be seen in leadership structures regardless of ability level. This phenomenon is said to be impeding management and non-managerial workforce selection methods, and it raises serious concerns about whether Albanian employment practices foster professionalization or partiality. Family-owned enterprises are distinguished by the fact that ownership and control are held by one or more family members. In all cases mentioned above, the founding family typically retains a large ownership share, and decision-making authority is delegated to family members who serve as executives or on the board of directors. Family-owned enterprises may confront governance difficulties as a result of blending family dynamics and professional management.

Board Diversity expressed in terms of gender diversity is limited though improvement is seen. Legislative measures have pushed to improve the number of women on boards. These rules demand a particular percentage of women to serve on boards of directors in certain types of businesses. While there has been a growing emphasis on encouraging gender diversity and inclusivity in corporate governance, the overall presence of women on boards in Albania remains relatively low, and more efforts to promote gender equality are required. Women appear to be underrepresented on boards with only 38% of firms from the sample having at least one female member in the board of directors, and 62% of the firms with all-male boards. In terms of *Board Nationalities*, the selected firms appear to score better. Foreign direct investments and the banking sector are seen to have more international board members. It results that 55% of the firms have at least one international board member, instead 45% have all-Albanian boards. While not all firms provide enough information about their boards, it can be emphasized that in enterprises having Albanian ownership, the boards are composed of entirely Albanian members.

In terms of *Board Structure*, while there is no legal obligation for all firms to have a certain number of independent members on their boards, the law does necessitate the nomination of 'independent directors' in some instances. According to the law on Commercial Companies, in joint-stock corporations, the majority of the board members need to be independent directors. Individuals who are not employed by the company and have no material links with the company or its management are considered independent directors. They are supposed to contribute objectivity, impartiality, and expertise to the decision-making processes of the board. However, even the definition of 'independence' is provided differently in various instances, which creates confusion, making this threshold seem to be 'too much' as it is not successfully executed in practice in any of the firms. Nevertheless, the level of board independence varies from one company to another, in most instances with firms not having defined independent board members. As seen in Table 3 below, it results that a majority of 62% of firms have not defined any independent member in their boards of directors. It is worth mentioning, however, that the presence of independent board members is most visible in the banking sector, where all firms in the study have independent board members.

Table 3. Independent Board Members

Independent Board Members	Frequency	Percentage
Firms with independent board members	11	38
Firms without independent members	18	62
Total	29	100.0

Source: Own research

Ownership Concentration is another important element of corporate governance worth observing. Since the country transitioned to a market economy, there has been a shift toward a more diverse ownership structure, with a mix of state-owned, privately-owned, and foreign-owned businesses. Various variables influence ownership concentration in corporate governance in Albania, including regulatory frameworks, historical background, and market dynamics. Privatization measures have aided the expansion of private sector firms, attracting both international and domestic investment, which is reflected in the ownership structure of firms. 48% of the firms have full private capital, 41% of them are FDI and the rest is state-owned or mixed ownership. Foreign direct investment (FDI) has also increased in Albania in recent years, resulting in a bigger representation of foreign-owned enterprises, which offers new viewpoints and practices to corporate governance, frequently pressing for greater transparency and accountability. Firms with entirely Albanian private capital appear to have distributed their shares among family members. The significant presence of family-owned firms is a notable characteristic of the Albanian corporate governance landscape. Family-owned businesses frequently have concentrated ownership, with a few family members holding control retaining ownership and administration control ever since their establishment. This level of concentration is critical because firms owned by a small group of people or a family can lead to a lack of transparency, accountability, and conflicts of interest. For this reason, additional reforms strengthened enforcement mechanisms, and a firm commitment to transparency and accountability are required to successfully address ownership concentration issues.

Transparency and Disclosure are essential for good corporate governance, but they seem to be often lacking in Albania. Firms typically upload their simple/historical extracts in the Trade Register, but complete data and histories of business actions were not fully accessible by the researchers of this study. Firms have disclosure obligations, but they are not consistently applied, making the dependability on publicly available information, such as annual reports, questionable. The law "On Accounting and Financial Statements" mandates that financial statements must accurately represent a company's financial status and performance, and firms are required to provide substantial nonfinancial information on their websites too, but in reality, compliance to the above is poor, with minimal information available online. Even the largest companies offer limited details, including director credentials, board meetings and activities, and even ownership structure. Furthermore, in terms of transparency and disclosure, legal provisions mandate firms to hire an independent external auditor and to publicly publish their identity, nonetheless, despite the legal requirements about 42% of firms have not defined and published their external audit firm.

5. CONCLUSION

Corporate governance (CG) has become a crucial component of organizational success in recent years. Effective CG ensures that resources are allocated efficiently, risks are managed appropriately, and strategic goals are achieved responsibly. These principles are essential for building trust with investors and other stakeholders, ultimately leading to better financial performance and sustainability. The board of directors plays a critical role in CG by overseeing management and ensuring that decisions align with the best interests of stakeholders.

This study explored the current practices of corporate governance in the context of Albania, focusing especially on the board composition and activity, identifying key practices, strengths, and shortcomings. Despite legal reforms, Albania faces challenges in fully adopting CG principles, with a general lack of awareness and recognition of the benefits of good governance practices. The institutional and legal framework in Albania seeks to align with international standards, but implementation remains relative. Generally speaking, observations reveal that in Albania corporate governance is influenced by agency theory, which prioritizes maximizing investor profits rather than all stakeholder interests. This study's findings once again highlight the critical role of CG in promoting ethical decision-making and responsible behavior within organizations. Additionally, the research identifies several factors that can undermine CG effectiveness, such as inadequate enforcement of governance policies and poor risk management practices. The study also points out that Albania's financial and banking sectors have relatively well-developed CG frameworks, which could serve as models for other industries. However, challenges persist, including limited awareness, sporadic empirical research, and a lack of comprehensive data on CG practices in the country. Nevertheless, the findings of this study should further encourage decision-makers to understand that effective CG frameworks contribute to better resource allocation, risk management, and innovation, all of which are crucial for long-term success. In a country level too, the adoption of CG principles can foster a more favorable economic environment, attracting investment and enhancing competitiveness.

In terms of theoretical implications, this study contributes to the theoretical understanding of CG by exploring its application in a unique context—Albania. It identifies gaps in existing literature and provides a foundation for further research on the nuances of CG practices in different economic and institutional environments. By comparing CG practices across different sectors within Albania, the study offers insights into the variations in governance outcomes. Some practical implications can be induced for stakeholders too as findings emphasize the importance of robust CG frameworks in enhancing organizational performance and stakeholder trust. A diverse and competent board of directors is crucial for effective CG, as is the timely and accurate dissemination of information to stakeholders. Implementing strong CG practices can lead to improved corporate performance, increased investment, and long-term value creation.

This study offers some recommendations to improve CG in Albania, among others,

- Enhancing CG Compliance with International Standards, where Albania should strive to align its CG principles with OECD norms, which would help attract foreign investment and promote sustainable economic growth.
- Strengthening the Legal Framework, where there is a need for stricter regulations regarding board composition, independence, and accountability. This includes further promoting the recruitment of non-executive independent board members.
- Encouraging Board Diversity, where firms should further diversify their boards in terms of gender, expertise, and background. Diverse boards are more likely to bring a wider range of perspectives and are better equipped to address complex challenges.
- Improving Governance in all Sectors, because findings show uneven implementation of CG principles across sectors, and it is essential for all sectors adhere to CG standards.
- Reducing Informality and Enhancing Transparency, where efforts should be made to eliminate informal market practices and strengthen auditing processes to ensure greater transparency in business operations.
- Collaborative Efforts, actors like regulators, industry stakeholders, and professional organizations collaborate to strengthen the implementation of CG practices in Albania.

Researchers of this study acknowledge some limitations too, like the limited sample size which may not capture the full diversity of CG practices in Albania, and the short time horizon because the study's findings are based on data from a single year. The researchers faced seriously limited access to comprehensive data and thus had to rely on the sometimes limited publicly available data. This study focused only on the board composition, size, and ownership structure, and it did not explore other important aspects of corporate governance that would give a broader and more complete overview of the subject matter.

Despite these limitations, this study offers valuable insights into the state of CG in Albania and provides a foundation for future research and policy development. It highlights the importance of ongoing efforts to improve CG practices, which are essential for fostering a sustainable and competitive business environment in Albania.

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