Business Ethics and Corporate Governance

Unit III: Corporate Governance

Corporate Governance

- Corporate Governance refers to the way a corporation is governed.
- It is the technique by which companies are directed and managed.
- It means carrying the business as per the stakeholders’ desires.
- It is actually conducted by the board of directors and the concerned committees for the company’s stakeholder’s benefit.
- It is all about balancing individual and societal goals, as well as, economic and social goals.

Corporate Governance

- Corporate Governance is the interaction between various participants (shareholders, board of directors, and company's management) in shaping corporation's performance and the way it is proceeding towards.
- The relationship between the owners and the managers in an organization must be healthy and there should be no conflict between the two.
- The owners must see that individual's actual performance is according to the standard performance.
- These dimensions of corporate governance should not be overlooked.

Corporate Governance

- Corporate Governance deals with determining ways to take effective strategic decisions.
- Corporate Governance ensures transparency which ensures strong and balanced economic development.
- Corporate Governance has a broad scope. It includes both social and institutional aspects. Corporate Governance encourages a trustworthy, moral, as well as ethical environment.

Definition

- In the words of Catherwool, "Corporate governance means that company manages its business in a manner that is accountable and responsible to the shareholders. In a wider interpretation, corporate governance includes company's accountability to shareholders and other stakeholders such as employees, suppliers, customers and local community."

Objectives

- To develop better and most efficient management of business organisation,
- Holding the balance between social and economic goals,
- To encourage the efficient use of scarce resources,
- To develop a better working environment to get some patterns of democratic style,
- To bring a high level of satisfaction to customers, employees, investors and the society at large,

Objectives

- To adopt transparent procedures and practices and arrive at decisions on the strength of adequate information,
- To provide disclosures to all the relevant facts and information to stakeholders and other partners of the business,
- To make effectively and regularly monitor and control the affairs and functioning of the managerial group of the concern.

Benefits of Corporate Governance

1. Good corporate governance ensures corporate success and economic growth.
2. Strong corporate governance maintains investors' confidence, as a result of which, company can raise capital efficiently and effectively.
3. It lowers the capital cost.
4. There is a positive impact on the share price.

Benefits of Corporate Governance

5. It provides proper inducement to the owners as well as managers to achieve objectives that are in interests of the shareholders and the organization.

6. Good corporate governance also minimizes wastages, corruption, risks and mismanagement.

7. It helps in brand formation and development.

8. It ensures organization in managed in a manner that fits the best interests of all.

Fundamental principles of Corporate Governance

- Transparency
- Accountability
- Responsibility
- Fairness

Participants in Corporate Governance

- Board of Directors
- Non-executive Directors (nominated by the govt)
- Audit Committees
- Company Secretary

Corporate Governance Control Mechanism

Internal CG Control Mechanism	External CG Control Mechanism
• Monitoring by Board	• Government Regulations
• Internal Auditors	• Media exposure
• Proper balance of power	• Market Competition
• Monitored by large shareholders and stakeholders	• Take over activities
	• Public release of financial records

Ethical Dilemma

- Ethical dilemma is a moral situation in which a choice has to be made between two equally undesirable/desirable alternatives.
- A situation that arises when all alternative choices or behaviour have been deemed undesirable because potentiality of negative ethical consequences making its difficult to distinguish right from wrong.
- Perplexing situation- A situation involving choice between equally unsatisfactory alternatives.

Ethical Dilemma

- Ethical dilemma is the situation involving conflicting morals and give raise to such questions as-
  - What harm or benefit will result from this decision or action?
  - What is good(virtue) or what is duty (right)?
- Dilemma exist when an organisational decision maker faces a choice between two or more options that will have an impact on-
  - The organisational competitiveness and profitability
  - Its stakeholders

For example-

An employee in advertising company was asked to prepare an advertisement for the client, but the employee knows that the client wants him to draft untrue information.

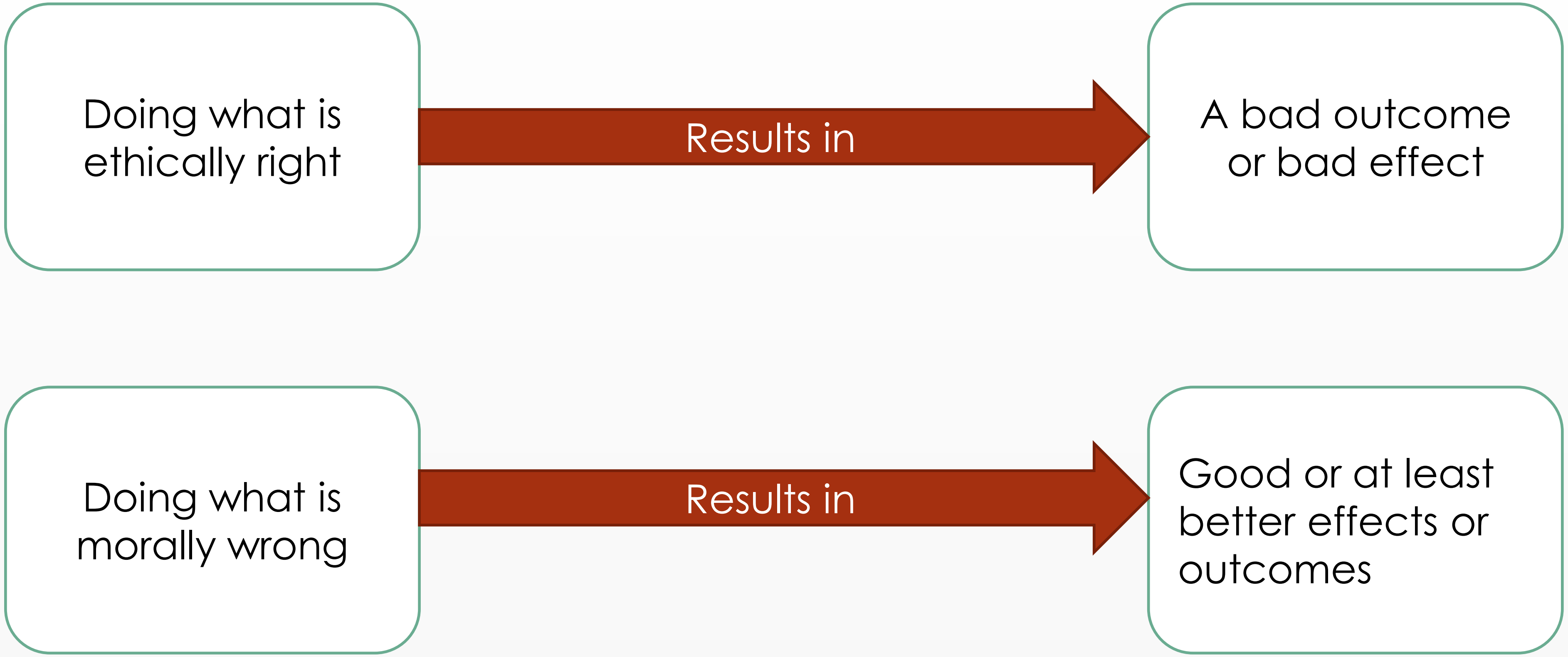
Sources of Ethical Dilemmas

- Failure of personal character
- Conflict of personal values and organisational goals
- Organisational goals versus social values
- Hazardous but popular products
- Family values vs. organisational values

Types of Ethical Dilemma

- Ethical dilemma between one ethically right and wrong alternative
- Ethical dilemma between two ethically wrong alternatives
- Ethical dilemma between two ethically right alternatives

Structure of Ethical Dilemma



How to Resolve Ethical Dilemmas?

- **1. Analyse the consequences-**

Resolution to the ethical dilemma is to be found within the confines of law.

Ethical dilemma that arises in the business should be resolved at least within the bare minimum of law and legal framework.

Before one acts, answer to the following questions will help find the type of actions that can be taken-

- Who are the beneficiaries of your actions?
- Who are likely to be harmed by your actions?
- What is the nature of benefits and harms?
- How long are these benefits and harms likely to exist?

How to Resolve Ethical Dilemmas?

- 2. **Analyse the Actions-**

Once identifying the best possible option, concentrate on the actions, find out how your proposed action measures against moral principles, such as honesty, fairness, respect for the dignity and rights of others and recognition of the vulnerability of people who are weak etc.

After considering all these possible factors in the various options it is sensible to choose the one which is least problematic.

How to Resolve Ethical Dilemmas?

- **<u>3. Make a decision-</u>**

Analyse all the options carefully and take a rational decision.

Most organisation attempts to address to ethical consideration and avoid ethical dilemmas by developing code of ethics.

Common Ethical Dilemmas in Business

1. <u>People Issues</u> - People issues include privacy discrimination sexual and other harassments

2. <u>Conflict of Interest</u> - Occurs when your judgement or objectivity is compromised.

3. <u>Use of Corporate Resources</u> - It might occur when employees have access to corporate resources including finance and reputation.

4. <u>Managing 'The Basic'</u> - Hiring, promotion, termination, performance appraisal, discipline etc.

Common Ethical Dilemmas in Business

- 5. Managing Diverse Workplace - Managers might get into ethical dilemma when dealing with individuals of different gender, ages, races, religions, ethnic groups, sexual orientation.
- 6. Managing Stakeholders - Nowadays because organisations have multiple stakeholders. Ethical dilemma might arises when thinking how to balance stakeholders' interest.

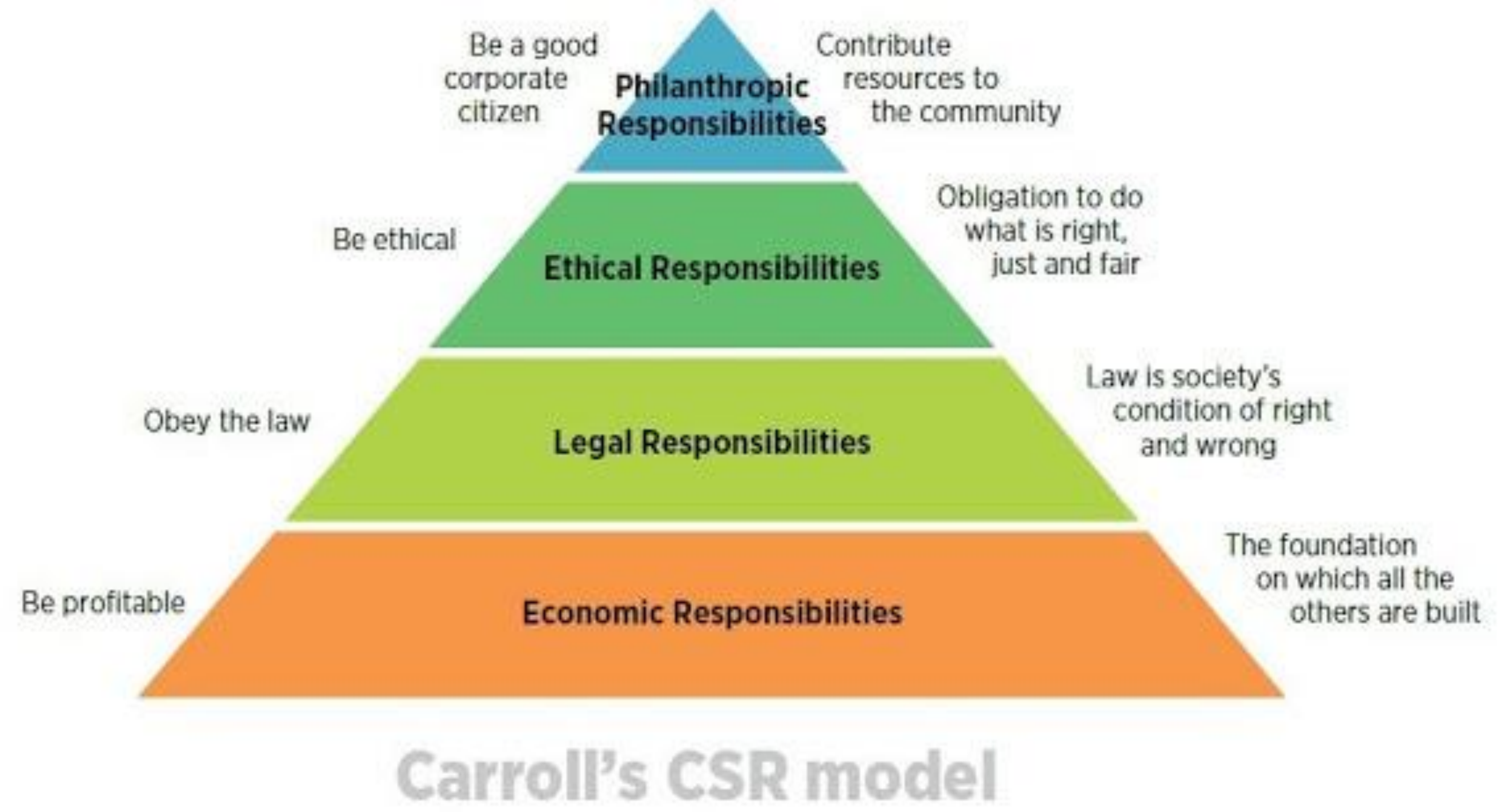
Corporate Social Responsibility

- CSR is a continuing commitment by business to behave ethically and contribute to economic development while improving the quality of life of the workforce and their families as well as the local community and society at large.
- CSR is about business giving back to society.
- CSR is not only a philanthropic activity but It is an investment in our collective future. Wealth created from society has to be ploughed back into society.
- It is a responsibility towards the ethical and social consideration.
- It is an overall relationship of the corporate with all its stakeholders.

Scope of CSR

- Understanding social responsibility of business.
- Protecting and promoting stakeholders' interest.
- Promotion of common welfare programmes.
- Render Social services.
- Abiding by rules and regulations.
- Creation of wealth.
- Focus on human element.
- Improve productivity.

Carroll's Pyramid of Corporate Social Responsibility



Carroll's Pyramid of Corporate Social Responsibility

- **Economic responsibility:** Companies have a responsibility of an economic nature, since they have a responsibility to produce goods and services that society wants and sell them in a profitable way. The basis for the functioning of a company is producing and selling goods for profit.

- **Legal liability:** The company expects companies to undertake their economic mission within the legal requirements established by the legal system of society. It is expected that the company complies with laws and regulations or that the products and services offered by companies have security standards and comply with existing environmental regulations.

Carroll's Pyramid of Corporate Social Responsibility

- **Ethical responsibility:** Represents ethical behaviours that are expected that companies have. This has become more important, because the tolerance of society against unethical behaviour is dwindling. The decision should consider the consequences of their actions, honouring the rights of others, fulfilling obligations and avoiding harming others.

- **Philanthropic responsibility**: Represents discretionary actions taken by the company in response to social expectations. They respect the activities undertaken by companies assuming a social role that goes beyond the legal and ethical obligation, assuming an increasingly strategic importance. Examples: charitable contributions, employee training, extension of benefits to employees' families

Compliance of CSR

- Under companies act 2013, section 135 any company with-
  - ✓ Net worth of Rupees 500 crore or more
  - ✓ Turnover of Rupees 1000 crore or more
  - ✓ Net profit to be 5 crore or more
- Has to spend 2% of last 3 year's average net profit on CSR activities specified in schedule VII and as amended time to time.
- The rule came in effect from 1 April 2014.
- It is applicable to all the Indian companies and also applicable to office and branches of foreign companies of India.

This Schedule Focuses on Following Activities-

- Eradicating hunger poverty and malnutrition.
- Promoting education.
- Improving maternal and child health.
- Ensuring environmental sustainability.
- Protection of national heritage.
- Promoting sports.
- Contribution to the Prime Minister national relief fund.
- Slum area development, etc.

Benefits of CSR

Corporate Social Responsibility