SEMESTER – **B.Com**, **SEMESTER 4**

SUBJECT – **Business Ethics**

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LECTURE NO. - 6

Note: If anyone is interested to get a scanned copy of the chapters I am covering, please contact me in whatsapp at 9163019220 and I will send you the same.

Unit 5: Ethics & Corporate Governance

Concept of Corporate Governance

Corporate governance is a set of processes, policies, regulations, rules, customs and laws governing the way how a corporation should be directed, administered and controlled to maximize the efforts of its employees and the resulting for all stakeholders. Stakeholders include shareholders, promoters, and board of directors, management, financiers, employees, customers, creditors, society, community and government. It forms part of a broader international effort to promote increased transparency, reliability and the rule of law. So, corporate governance is the system of rules, practices and processes by which a firm is directed and controlled.

Corporate Governance ensures transparency which ensures strong and balanced economic development. This also ensures that the interests of all shareholders (majority as well as minority shareholders) are safeguarded.

"Corporate governance is the system by which companies are directed and controlled." – The Cadbury Committee (U.K.)

Our Five Golden Rules of best corporate governance practice is:

- **Ethics**: Clear ethical practices should be applied to the business
- **Align Business Goals**: appropriate goals, arrived at through the creation of a suitable stakeholder participation in decision making model
- **Strategic management:** an effective strategy process which incorporates stakeholder value

- **Organisation:** an organisation suitably structured to give effect to the good corporate governance
- **Reporting:** reporting systems structured to provide transparency and accountability.

Principles of Corporate Governance: (or major issues involved in corporate governance)

The fundamental or key principles of corporate governance are described below:

(i) **Transparency:** Transparency is the foundation of corporate governance, which helps to develop a high level of public confidence in the corporate sector. There should be an accurate, adequate and timely disclosure of all relevant information about the performance of the corporate enterprise to the stakeholders.

(ii) **Accountability:** Accountability is a liability to explain the results of one's decisions taken in the interest of others. In the context of corporate governance, accountability implies the responsibility of the Chairman, the Board of Directors and the chief executive for the use of company's resources (over which they have authority) in the best interest of company and its stakeholders.

(iii) **Independence:** The top management of the corporation i.e. the Board of Directors must be independent enough to take all corporate decisions based on business prudence. That is one of the reasons why the companies act 2013 has mandated the presence of independent directors in the Board of directors.

<u>Importance / Significant / Need of corporate governance</u>

The significance of corporate governance is highlighted by the following factors:

1. **Wide Spread of Shareholders:** Since shareholders are very large in numbers spread at distant places, many of who have indifferent attitude toward corporate affairs, the idea of shareholders' democracy remains confined only to the law and the Articles of Association; which requires a practical implementation through a code of conduct of corporate governance.
2. **Changing Ownership Structure**: The pattern of corporate ownership has changed considerably, in the present-day-times; with institutional investors (foreign as well

Indian) and mutual funds becoming largest shareholders in large corporate private sector. These investors have become the greatest challenge to corporate managements, forcing the latter to abide by some established code of corporate governance to build up its image in society.

3. **Corporate Scams or Scandals:** Corporate scams (or frauds) in the recent years of the past have shaken public confidence in corporate management. The need for corporate governance is, then, imperative for reviving investors' confidence in the corporate sector towards the economic development of society.
4. **Greater Expectations of Society of the Corporate Sector:** Society of today holds greater expectations of the corporate sector in terms of reasonable price, better quality, pollution control, best utilisation of resources etc. To meet social expectations, there is a need for a code of corporate governance, for the best management of company in economic and social terms.
5. **Failed mergers and acquisitions:** Failed mergers and acquisitions witnessed in several countries, put a question mark on the efficiency of managements of these acquiring companies. This factor also points out to the need for corporate governance, in the form of an efficient code of conduct for corporate managements.
6. **Huge Increase in Top Management Compensation**: It has been observed in both developing and developed economies that there has been a huge increase in the monetary payments (compensation) packages of top level corporate executives. This factor necessitates corporate governance which puts a pressure on the top management to elaborate the work done in their reports and restrain for any fraud.
7. **Globalisation:** Desire of more and more Indian companies to get listed on international stock exchanges also focuses on a need for corporate governance. There is no doubt that international capital market recognises only companies which are well-managed according to standard codes of corporate governance.