

GOVERNANCE, BUSINESS ETHICS AND SUSTAINABILITY

Time allowed : 3 hours

Maximum marks : 100

PART A

Answer Question No. 1 which is compulsory
and any two of the rest from this part.

Question 1

- (a) *In United Kingdom, the Combined Code on Corporate Governance of 2008 is the result of studies made from time to time by various committees to prevent the recurrence of scandals and financial collapses experienced in 1980s and early 1990s, when Cadbury Committee was first set-up in 1992 which gave a new dimension to the Corporate Governance.*

List out the three important recommendations made by Cadbury Committee and outline atleast five major landmarks in the historical development since the setting-up of the Cadbury Committee for improvement in the Corporate Governance. (10 marks)

- (b) *State, with reasons in brief, whether the following statements are correct or incorrect:*
- (i) *All non-executive directors are independent directors.*
 - (ii) *Compliance Management Committee is compulsory under clause 49 of the listing agreement.*
 - (iii) *The Sarbanes-Oxley Act, 2002 is applicable to listed companies in India.*
 - (iv) *Enron debacle led to the appointment of Naresh Chandra Committee in 2002.*
 - (v) *Shareholders activism played a major role in eradicating apartheid in South Africa through divestment. (1 mark each)*
- (c) *Choose the most appropriate answer from the given options in respect of the following :*
- (i) *The mechanism for employees to report certain events to the management, like—unethical behaviour, suspected fraud or violation of the company's code, is known as —*
 - (a) *Whistle Blower Policy*
 - (b) *Surveillance action*
 - (c) *Market abuse*
 - (d) *Snap investigation.*
 - (ii) *Out of the following, which is an institutional investor group —*
 - (a) *Foreign Institutional Investors*
 - (b) *Mutual funds*
 - (c) *Banks and financial institutions*
 - (d) *All the above.*

- (iii) *Out of the following, which is a Corporate Social Responsibility (CSR) reporting framework —*
- (a) *CSR 1982*
 - (b) *SA 8000*
 - (c) *MCA-21*
 - (d) *SA 800.*
- (iv) *A person can hold office of director of the public companies at the same time in —*
- (a) *Not more than 20 companies*
 - (b) *Not more than 11 companies*
 - (c) *Not more than 15 companies*
 - (d) *Any number of companies.*
- (v) *Remuneration Committee is appointed for the purpose of recommending remuneration of —*
- (a) *Chief Executive Officer*
 - (b) *Managing Director*
 - (c) *Whole-time Director*
 - (d) *All the above.*
- (1 mark each)*

Answer 1(a)

Historical developments in the UK for the improvement in corporate governance since the setting of Cadbury Committee are as under:

- (i) The Cadbury Report 1992;
- (ii) The Greenbury Report, 1995;
- (iii) The Hampel Report 1998
- (iv) The Turnbull Report;
- (v) Higgs Report
- (vi) Smith Report;
- (vii) The Tyson Report
- (viii) The combined code on Corporate Governance as revised in 2003;
- (ix) The combined Code of Corporate Governance, 2006, and;
- (x) The combined Code on Corporate Governance 2008;
- (i) *The Cadbury Report 1992*

Due to several scandals and financial collapses in the UK in the late 1980s and early 1990s, London Stock Exchange set up the Cadbury Committee in May 1991 to raise the standard of corporate governance for preventing such scandals

and financial collapses in future. This Committee, in its report known as 'Cadbury Report, recommended mainly :

- Separating the role of CEO and Chairman of the Board
- Balanced composition of Board of Directors with executive and non-executive directors.
- Selection process for non-executive directors.

(ii) *The Greenbury Report 1995*

The Confederation of British Industry set up a group under the Chairmanship of Sir Richard Greenbury to examine the remuneration of the directors. It recommended the formation of Remuneration Committee composed of non-executive directors. Its recommendations were incorporated in the Listing Rules of the London Stock Exchange.

(iii) *The Hampel Report 1998*

The Hampel Committee was set up to review the implementation of Cadbury and Greenbury Reports and to see that their purposes were being achieved. The recommendations of this committee coupled with further consultations by the London Stock Exchange resulted in a Combined Code on Corporate Governance – the original Combined Code, 1998.

(iv) *The Turnbull Report*

A working group under the chairmanship of Nigel Turnbull recommended the Internal Control Guidance for Directors which were included in the combined code.

(v) *Higgs Report*

The Combined Code was reviewed in July 2002 by Derek Higgs about the role and effectiveness of non-executive directors.

(vi) *Smith Report*

A group under the chairmanship of Sir Robert Smith was set up to develop Guidance for Audit Committee in the Combined Code.

(vii) *The Tyson Report*

The Tyson Report was commissioned on the recruitment and development of non-executive directors.

(viii) *The Combined Code on Corporate Governance as revised in 2003*

On the basis of recommendations of all the reports the Combined Code was revised in 2003

(ix) *The Combined Code on Corporate Governance 2006*

The Combined Code on Corporate Governance was again revised in 2006.

(x) *The Combined Code on Corporate Governance 2008*

The Combined Code on Corporate Governance 2008 sets out standards of good practice in relation with shareholders. All companies incorporated in the UK and listed on the London Stock Exchange are required to report in their annual reports and accounts about the implementation of the combined code on Corporate Governance .

Answer 1(b)(i)

Incorrect

Non-executive directors may or may not be independent directors

Answer 1(b)(ii)

Incorrect

Corporate Compliance Committee is not amongst the mandatory committees which have to be constituted by a listed entity to which clause 49 of the Listing Agreement is applicable. The mandatory committees are, Audit Committee and Shareholders Grievance Committee.

Answer 1(b)(iii)

Incorrect

This Act was passed in the United States and is applicable to companies listed in the US.

Answer 1(b)(iv)

Correct

The Enron debacle of 2001 involving the hand-in-glove relationship between the auditor and the corporate client, the scams involving the fall of the corporate giants were some important factors which led the Indian Government to wake up and in the year 2002, Naresh Chandra Committee was appointed to examine and recommend inter alia amendments to the law involving the auditor-client relationships and the role of independent directors.

Answer 1(b)(v)

Correct

Shareholder activism played a major role in eradicating apartheid in South Africa through divestment.

Answer 1(c)(i)

- (a) Whistle Blower Policy.

Answer 1(c)(ii)

- (d) All the above.

Answer 1(c)(iii)

- (b) SA 8000.

Answer 1(c)(iv)

- (c) Not more than 15 companies.

Answer 1(c)(v)

- (d) All the above.

Question 2

- (a) Write short notes on the following :

- (i) Rules vs. principles
- (ii) Parties to corporate governance.

(3 marks each)

- (b) Expand the following abbreviations :

- (i) OECD
- (ii) NFCG
- (iii) COSO
- (iv) ASSOCHAM.

(1 mark each)

- (c) Draw a comparison between section 292A of the Companies Act, 1956 and clause 49 of the listing agreement with regard to composition of the audit committee.

(5 marks)

Answer 2(a)(i)**Rules v. Principles**

Rules are written prescriptions for conduct or action and are absolute. Principles, on the other hand, provides a guidance of acceptable actions that are fair and equitable.

Under rules-based governance, companies must comply with a specific set of procedural requirements, a checklist of what to do and what not to do. Under a principles-based regime, however, corporate behavior is guided by a focus on end results. This approach emphasizes “doing the right thing,” by whatever means the company’s leadership feels most appropriate.

Rules are typically thought to be simpler to follow than principles, demarcating a clear line between acceptable and unacceptable behaviour. Rules also reduce discretion on the part of individual manager or auditors.

Hon’ble Supreme Court of India in a case of Bajaj Auto Limited, defined the discretion as proper adoption of the rules.

In practice rules can be more complex than principles. They may be ill equipped to deal with new types of transaction not covered by the Code. Moreover, where clear rules are followed one can still find a way to circumvent their underlying purpose. This is harder to achieve if one is bound by broader principles.

Principles are a form of self regulation. They allow the respective sector to determine what standards are acceptable or unacceptable. It also pre-empts over zealous legislations that might not be practical.

Answer 2(a)(ii)**Parties to corporate governance**

The Board of Directors play a central role in ensuring good governance in a corporate. In a business context, those who have a “stake” or claim in some aspect of a company’s products, operations, markets, industry, and outcomes are known as stakeholders. The various stakeholders of a corporate are all parties to corporate governance. The stakeholders of a corporate include its employees, shareholders, suppliers, vendors, customers, creditors, regulators, government/s and the community at large. These groups are influenced by business, and they also have the ability to affect the business.

Answer 2(b)(i)

OECD – Organisation for Economic Co-operation and Development.

Answer 2(b)(ii)

NFCG – National Foundation for Corporate Governance.

Answer 2(b)(iii)

COSO – Committee of Sponsoring Organization of the Tread way Commission.

Answer 2(b)(iv)

ASSOCHAM – Associated Chambers of Commerce and Industry.

Answer 2(c)**Comparison between Clause 49 and Section 292A of the Companies Act, 1956**

<i>Requirements of Clause 49</i>	<i>Requirements of Section 292A of Companies Act</i>
Applicable to all listed companies with paid-up capital of more than Rs.3 Cr or Networth greater than Rs. 25 Cr at any time in the history of the company and to companies seeking listing	Applicable to public companies with paid-up capital greater than Rs.5 Cr
2/3rd of the directors shall be independent directors	Members shall be other than managing or whole-time directors i.e. members shall be non-executive directors.
All members shall be financially literate and at least one member shall have accounting expertise	No corresponding requirement
“independent” director can be Chairman	Any member of Audit Committee can be Chairman
Auditors, internal auditor & director-finance or other executives may be present as invitees	Auditors, internal auditor & the director-finance shall attend & participate at meetings of Audit Committee but shall not vote
Company secretary to be secretary of the Audit Committee	No corresponding requirement

Question 3

- (a) *What are the major legislations/regulations/guidelines dealing with transparency and disclosures by companies ?* (5 marks)
- (b) *Discuss in brief some of the main Corporate Social Responsibility (CSR) Reporting Frameworks.* (5 marks)
- (c) *What is 'risk management process' ? What are the four steps in risk management?* (5 marks)

Answer 3(a)

The following are some of the major legislations on transparency and disclosure:

1. Companies Act, 1956

In terms of Companies Act, 1956 the aspect of disclosure and transparency spans over several sections. Some of the major disclosures contemplated in terms of Companies Act include the Balance sheet, profit and loss account, Board's Report, Auditor's Report, Annual Return and the various filings with ROC.

With the e-filing of forms with the Registrar of Companies, The Ministry of Corporate Affairs has put in place a mechanism that is imaginative, technologically savvy and stakeholder friendly. Through the application of Information Technology to the Government functioning in order to bring about Simple, Moral, Accountable, Responsive and Transparent (SMART) Governance, the MCA aims at moving from paper based to nearly paperless environment.

2. Listing Agreement In terms of the Listing Agreement several clauses deal with disclosure. The following are some of the clauses dealing with disclosure – Clauses 19, 22, 29, 30, 31, 32, 35, 36, 41. Clause 49 of the listing agreement deals with Corporate Governance and mandates various disclosures like remuneration to directors, directors' attendance in board, committee and Annual General Meetings, Management Discussion and Analysis Report, etc.
3. (Erstwhile) SEBI (DIP) Guidelines 2000 (now Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2009.
4. SEBI (SAST) Regulations, 1997.
5. SEBI (Prohibition of Insider Trading) Regulations, 2002.
6. Securities Contract (Regulations) Act, 1956.

Answer 3(b)

The following are some of the main standards for social, ethical and environmental reporting currently in use internationally:

The AA 1000 - framework developed by the Institute of Social and Ethical Accountability provides a standard for social and ethical accounting, auditing and reporting, including mandatory external verification and stakeholder engagement.

The Social Accountability - SA 8000 is an international standard for social accountability initiated by Council on Economic Priority Accreditation Agency (CEPAA) conventions, the Universal Declaration on human rights and the Child. SA 8000 seeks to provide transparent, measurable and verifiable performance standards in the areas of child labour; forced labour; health and safety; compensation; working hours; discrimination; discipline; free association and collective bargaining; and management systems.

The Good Corporation - global standard of corporate social responsibility developed by the Institute of Business Ethics. This covers fairness to employees, suppliers, customers and providers of finance; contributions to the community; and protection of the environment. Company performance is assessed annually by an independent verifier.

The UN Global Compact

The Global Compact is a voluntary corporate citizenship initiative with two objectives:

“Making the Global Compact and its principles part of business strategy and operations.”

“Facilitating cooperation among key stakeholders and promoting partnerships in support of U.N. goals.”

The Global Compact's ten principles in the areas of human rights, labour, the environment and anti-corruption.

The OECD Guidelines for Multinational enterprises - set out recommendations for responsible business conduct in employment and industrial relations; human rights; the environment; information disclosure; competition; taxation; science and technology; combating bribery; and protection of consumer interests. They are not legally binding and there is no requirement for reporting or external measurement. (www.oecd.org/daf/investment/guidelines)

Answer 3(c)

Risk Management Process

Risk management is a structured, consistent and continuous process, applied across the organisation for the identification and assessment of risks, control assessment and exposure monitoring.

The objectives of the Company's risk management framework comprises the following:

- To identify, assess, prioritize and manage existing as well as new risks in a planned and coordinated manner.
- To increase the effectiveness of internal and external reporting structure.
- To develop a risk culture that encourages employees to identify risks and associated opportunities and respond to them with appropriate actions.

Steps in Risk Management

The process of risk management consists of four logical and sequential steps as under:

- (i) Identification of risk.
- (ii) Evaluation/measurement of risks.
- (iii) Handling of risks.
- (iv) Implementation of risk management decisions.

Question 4

(a) *What are the legal remedies available in India for the redressal of the following complaints :*

- (i) *Delay in refund of application money;*
- (ii) *Delay in transfer of securities;*
- (iii) *Insider trading of shares;*
- (iv) *Delay in payment of dividend; and*
- (v) *Delay in re-payment of deposits.*

(5 marks)

(b) *Discuss briefly the role of directors in the good corporate governance.*

(5 marks)

(c) *What are the principles of corporate governance as evolved by the ICSI ?*

(5 marks)

Answer 4(a)(i)**Delay in refund of excess application money or allotment letters**

Section 73 of the Companies Act, 1956 provides for payment of interest for the period beyond 70 days from the closure of subscription list @ 15 percent

Answer 4(a)(ii)**Delay in Transfer of Shares**

Section 113 of the Companies Act, 1956 provides a time limit of 60 days provided for effecting transfer. If default is made every officer of the company who is in default shall be liable to fine which may extend to Rs.5000 for every day during which the default continues.

As per listing agreement the time limit is 30 days.

Answer 4(a)(iii)

Insider Trading, rigging and other mal practices

Investors can make complaints to SEBI for the violation of SEBI (Prohibition of Insider Trading) Regulations, 1992

Answer 4(a)(iv)

Section 207 of the Companies Act, 1956 casts an obligation on the company to pay dividend within 30 days from its declaration. In case of default every director who is party to the default is punishable with imprisonment and fine of Rs.1000/- for each day the default continues.

Answer 4(a)(v)

In terms of Section 58A (9) of the Companies Act, 1956 where a company has failed to repay any deposit or part thereof in accordance with the terms and conditions of its acceptance, the Company Law Board may on its own motion or an application by a depositor direct the company to make the repayment of the deposit.

In terms of Section 58AAA any offence arising out of acceptance of deposit is a cognizable offence under Code of Criminal Procedure 1973.

Answer 4(b)

The Board of Directors play a pivotal role in ensuring good governance. The contribution of directors on the Board is critical to the way a corporate conducts itself. The responsibilities of the directors and the Board derive from law, custom, tradition and current practice. In the present times, transparency, disclosure, accountability, issues of sustainability, corporate citizenship, globalization are some of the concerns that the Boards interlocks. The Boards today have to respond to the explosive demands of the marketplace. The contribution of directors on the Board of companies is critical for ensuring appropriate directions with regard to leadership, vision, strategy, policies, monitoring, supervision, accountability to shareholders and other stakeholders, and to achieving greater levels of performance on a sustained basis as well as adherence to the best practices of corporate governance.

Directors have the ultimate responsibility for the longer-term prosperity of the company. They are required in law to apply skill and care in exercising their duty to the company and are subject to fiduciary duties. If they are in breach of their duties or act improperly, directors may be made personally liable in both civil and criminal law.

Directors are accountable to the shareholders for the company's performance and can be removed from office by them or the shareholders can pass a special resolution requiring the Directors to act in a particular way. Directors act as "Fiduciaries" of the shareholders and should act in their best interests but also taking into account the best interests of the company as a whole (as a separate legal entity) and the other stakeholders.

Directors have a key role in the determination of the value and ethical position of the company.

Answer 4(c)

The principles of corporate governance evolved by the ICSI are as under:

- Sustainable development of all stakeholders – to ensure growth of all individuals associated with or affected by the enterprise on sustainable basis.
- Effective management and distribution of wealth – to ensure that enterprise creates maximum wealth and judiciously uses the wealth so created for providing

maximum benefits to all stakeholders and enhancing its wealth creation capabilities to maintain sustainability.

- Discharge of social responsibility – to ensure that enterprise is acceptable to the society in which it is functioning.
- Application of best management practices – to ensure excellence in functioning of enterprise and optimum creation of wealth on sustainable basis.
- Compliance of law in letter and spirit – to ensure value enhancement for all stakeholders guaranteed by the law for maintaining socio-economic balance.
- Adherence to ethical standards – to ensure integrity, transparency, independence and accountability in dealings with all stakeholders.

PART B

(Answer ANY TWO questions from this part)

Question 5

- (a) *“Ethics in business is simply the application of moral or ethical norms to business.” Explain and discuss the advantages of business ethics. (5 marks)*
- (b) *Write notes on any two of the following :*
- (i) *Enlightened-egoism*
 - (ii) *Ethics in compliance*
 - (iii) *Social and ethical accounting. (5 marks each)*

Answer 5(a)

Business ethics is a form of applied ethics. In broad sense ethics in business is simply the application moral or ethical norms to business. Ethics is a set of principles or standards of human conduct that govern the behavior of individuals or organizations. Using these ethical standards, a person or a group of persons or an organization regulate their behavior to distinguish between what is right and what is wrong as perceived by others.

The advantages of business ethics include :

1. *Attracting and retaining talent*

People aspire to join organizations that have high ethical values. Companies are able to attract the best talent and an ethical company that is dedicated to taking care of its employees will be rewarded with employees being equally dedicated in taking care of the organization. Ethical organizations create an environment that is trustworthy, making employees willing to rely, take decisions and act on the decisions and actions of the co-employees. In such a work environment, employees can expect to be treated with respect and consideration for their colleagues and superiors. It cultivates strong teamwork and productivity and support employee growth.

2. *Investor Loyalty*

Investors are concerned about ethics, social responsibility and reputation of the company in which they invest. Investors are becoming more and more aware that an ethical climate provides a foundation for efficiency, productivity and

profits. Relationship with any stakeholder, including investors, based on dependability, trust and commitment results in sustained loyalty.

3. *Customer satisfaction*

Customer satisfaction is a vital factor in successful business strategy. Repeat purchases/orders and enduring relationship of mutual respect is essential for the success of the company. The name of a company should evoke trust and respect among customers for enduring success. This is achieved by a company that adopts ethical practices. When a company because of its belief in high ethics is perceived as such, any crisis or mishaps along the way is tolerated by the customers as a minor aberration. Such companies are also guided by their ethics to survive a critical situation. Preferred values are identified ensuring that organizational behaviors are aligned with those values. An organization with a strong ethical environment places its customers' interests as foremost. Ethical conduct towards customers builds a strong competitive position. It promotes a strong public image.

Answer 5(b)(i)

Enlightened-egoism

This model takes into account harms, benefits and rights. Therefore, under this model an action is morally correct if it increases benefits for the individual in a way that does not intentionally hurt others, and if these benefits are believed to counterbalance any unintentional harms that ensue. For example, a company provides scholarships for education to needy students with a condition that the beneficiary is required to compulsorily work for the company for a period of 5 years. Although, the company's providing the scholarship benefits the needy students, but ultimately it is in the company's self interest.

Answer 5(b)(ii)

Ethics in Compliance

Compliance is about obeying and adhering to rules and authority. The motivation for being compliant could be to do the right thing out of the fear of being caught rather than a desire to be abiding by the law. An ethical climate in an organisation ensures that compliance with law is fuelled by a desire to abide by the laws. Organisations that value high ethics comply with the laws not only in letter but go beyond what is stipulated or expected of them.

Answer 5(b)(iii)

Social and ethical accounting

It is a process that helps a company to address issues of accountability to stakeholders, and to improve performance of all aspects i.e. social, environmental and economic. The process normally links a company's values to the development of policies and performance targets and to the assessment and communication of performance.

Social and ethical accounting has no standardized model. There is no standardized balance sheet or unit of currency. The issues are defined by the company's values and by the interests and expectations of its stakeholders, and societal norms and regulations.

With the focus on the concerns of society, the social and ethical accounting framework implicitly concerns itself with issues such as economic performance, working conditions, environmental and animal protection, human rights, fair trade and ethical trade, human resource management and community development, and hence with the sustainability of a company's activities.

Question 6

- (a) *What is the role of Board of directors in ethical management of a company ?*
(5 marks)
- (b) *Discuss 'ethics programme'. Set-out the relevant provisions in clause 49 of the listing agreement.*
(5 marks)
- (c) *What is the significance of organisation structure in business ethics ?*
(5 marks)

Answer 6(a)

The board of directors hold the ultimate responsibility for their firm's success or failure, as well as for ethics of their actions. As has been stated earlier the ethical tone of an organization is set at the top, the actions and attitudes of the board greatly influence the ethical climate of an organization. The directors on a company's board assume legal responsibility for the firm's resources and decisions. Board members have a fiduciary duty, i.e. a position of trust and confidence. Due to globalization, the role of the media, technology are revolutionizing the nature and speed of communication, directors are feeling greater demands for accountability and transparency. This calls for ethical decision making and providing an ethical decision making framework.

The perspective and independent judgement of independent directors can be helpful in determining a company's approach towards ethical issues and stakeholder interests. Independent directors are in a position to challenge current practices and also contribute knowledge and experience of good practices.

A Report by the Conference Board Commission on Public Trust and Private Enterprise suggested the following areas of oversight of ethics programme by a Board:

- Designation of a Board committee to oversee ethics issues;
- Designation of an officer to oversee ethics and compliance with the code of ethics;
- Inclusion of ethics-related criteria in employees' annual performance reviews and in the evaluation and compensation of management;
- Representation by senior management that all known ethics breaches have been reported, investigated, and resolved; and
- Disclosure of practices and processes the company has adopted to promote ethical behavior.

Answer 6(b)

Ethics Programme

A company must have an effective ethics program to ensure that all employees understand its values and comply with the policies and codes of conduct that create its ethical climate.

Two types of control systems can be created.

Compliance Orientation Programme : A compliance orientation creates order by requiring that employees identify with and commit to specific required conduct. It uses legal terms, statutes, and contracts that teach employees the rules and penalties for non-compliance.

Values Orientation : Values Orientation strives to develop shared values. Although penalties are attached, the focus is more on an abstract core of ideals such as respect and responsibility. Instead of relying on coercion, the company's values are seen as something to which people willingly aspire.

Most companies begin the process of establishing organizational ethics programs by developing codes of conduct. **Codes of conduct** are formal statements that describe what an organization expects of its employees

Corporate codes of conduct/ethics often contain about six core values or principles in addition to more detailed descriptions and examples of appropriate conduct. The six values that are desirable for codes of ethics include: (1) trustworthiness, (2) respect, (3) responsibility, (4) fairness, (5) caring, and (6) citizenship.

In India, Clause 49 of the Listing Agreement requires that

- (i) The Board shall lay down a code of conduct for all Board members and senior management of the company. The code of conduct shall be posted on the website of the company.
- (ii) All Board members and senior management personnel shall affirm compliance with the code on an annual basis. The Annual Report of the company shall contain a declaration to this effect signed by the CEO.

Explanation : For this purpose, the term “senior management” shall mean personnel of the company who are members of its core management team excluding Board of Directors. Normally, this would comprise all members of management one level below the executive directors, including all functional heads.

Answer 6(c)

An organization's structure is important to the study of business ethics. In a **Centralized organization**, decision-making authority is concentrated in the hands of top-level managers, and little authority is delegated to lower levels. Responsibility, both internal and external, rests with top management. This structure is especially suited for organizations that make high-risk decisions and whose lower-level managers are not highly skilled in decision making. It is also suitable for organizations in which production processes are routine and efficiency is of primary importance.

These organizations are usually extremely bureaucratic, and the division of labour is typically very well defined. Each worker knows his or her job and what is specifically expected, and each has a clear understanding of how to carry out assigned tasks. Centralized organizations stress formal rules, policies, and procedures, backed up with elaborate control systems. Their codes of ethics may specify the techniques to be used for decision making.

Because of their top-down approach and the distance between employee and decision maker, centralized organizational structures can lead to unethical acts. If the centralized organization is very bureaucratic, some employees may behave according to “the letter of the law” rather than the spirit.

In a **decentralized organization**, decision-making authority is delegated as far down the chain of command as possible. Such organizations have relatively few formal rules, and coordination and control are usually informal and personal. They focus instead on increasing the flow of information. As a result, one of the main strengths of decentralized organizations is their adaptability and early recognition of external change. With greater flexibility, managers can react quickly to changes in their ethical environment. Weakness of decentralized organizations is the difficulty they have in responding quickly to changes in policy and procedures established by top management. In addition, independent profit centers within a decentralized organization may deviate from organizational objectives.

Question 7

- (a) *“The code of conduct of a company sets for the legal and ethical standards of conduct for its directors and its employers.” Discuss and list out the important contents of the code of conduct of a company. (7 marks)*
- (b) *Discuss briefly the Clarkson principles of stakeholder management. (4 marks)*
- (c) *Explain briefly the following :*
 - (i) *Virtue Ethics Theory*
 - (ii) *The Caux Round Table. (2 marks each)*

Answer 7(a)

Code of conduct or what is popularly known as Code of Business Conduct contains standards of business conduct that must guide actions of the Board and senior management of the Company.

The Code may include the following:

- (a) Company Values.
- (b) Avoidance of conflict of interest.
- (c) Accurate and timely disclosure in reports and documents that the company files before Government agencies, as well as in Company’s other communications.
- (d) Compliance of applicable laws, rules and regulations including Insider Trading Regulations.
- (e) Maintaining confidentiality of Company affairs.
- (f) Non-competition with Company and maintaining fair dealings with the Company.
- (g) Standards of business conduct for Company’s customers, communities, suppliers, shareholders, competitors, employees.
- (h) Prohibition of Directors and senior management from exploiting corporate opportunities for themselves or their families.

- (i) Review of the adequacy of the Code annually by the Board.
- (j) No authority of waiver of the Code for anyone should be given.

The Code of Conduct for each Company summarises its philosophy of doing business.

Although the exact details of this code are a matter of discretion, the following principles have been found to occur in most of the companies:

- Use of company's assets;
- Avoidance of actions involving conflict of interest;
- Avoidance of compromising on commercial relationship;
- Avoidance of unlawful agreements;
- Avoidance of offering or receiving monetary or other inducements;
- Maintenance of confidentiality;
- Collection of information from legitimate sources only.
- Safety at workplace
- Maintaining and Managing Records
- Free and Fair competition
- Disciplinary actions

Answer 7(b)

The Clarkson Principle of Stakeholder Management

Max Clarkson (1922-1998) founded the Centre for Corporate Social Performance and Ethics in the Faculty of Management, now the Clarkson Centre for Business Ethics & Board Effectiveness, or CC(BE) 2. The Clarkson Principles emerged from a project undertaken by the Centre for Corporate Social Performance and Ethics :

Principle 1 : Managers should acknowledge and actively monitor the concerns of all legitimate stakeholders, and should take their interests appropriately into account in decision-making and operations.

Principle 2 : Managers should listen to and openly communicate with stakeholders about their respective concerns and contributions, and about the risks that they assume because of their involvement with the corporation.

Principle 3 : Managers should adopt processes and modes of behavior that are sensitive to the concerns and capabilities of each stakeholder constituency.

Principle 4 : Managers should recognize the interdependence of efforts and rewards among stakeholders, and should attempt to achieve a fair distribution of the benefits and burdens of corporate activity among them, taking into account their respective risks and vulnerabilities.

Principle 5 : Managers should work cooperatively with other entities, both public and private, to insure that risks and harms arising from corporate activities are minimized and, where they cannot be avoided, appropriately compensated.

Principle 6 : Managers should avoid altogether activities that might jeopardize

inalienable human rights (e.g., the right to life) or give rise to risks which, if clearly understood, would be patently unacceptable to relevant stakeholders.

Principle 7: Managers should acknowledge the potential conflicts between (a) their own role as corporate stakeholders, and (b) their legal and moral responsibilities for the interests of all stakeholders, and should address such conflicts through open communication, appropriate reporting and incentive systems and, where necessary, third party review.

Answer 7(c)(i)

Virtue Ethics theory is a branch of moral philosophy that emphasizes character, rather than rules or consequences, as the key element of ethical thinking. An example of this – when a person of good standing is found possessing a valuable article belonging to someone else it will be presumed that the article was loaned to him or kept with him for safe-keeping, whereas if it were in the possession of a person of doubtful or dubious character it would be presumed that he has stolen the article.

Answer 7(c)(ii)

The Caux Round Table

The Caux Round Table (CRT) is based on the belief that the world business community should play an important role in improving economic and social conditions. As a statement of its aspirations, it developed a document that aims to express a world standard against which business behavior can be measured.

The CRT Principles for Business articulate a comprehensive set of ethical norms for businesses operating internationally or across multiple cultures. These principles are rooted in two basic ethical ideals: kyosei and human dignity. The Japanese concept of “kyosei” means living and working together for the common good enabling cooperation and mutual prosperity to coexist with healthy and fair competition.

PART C

Question 8

Attempt any four of the following :

- (i) *What is the difference between ‘sustainable development’ and ‘corporate sustainability’. List out four fundamental principles of sustainable development agreed in the United Nations Conference on Environment and Development (UNCED), 1992.*
- (ii) *Discuss the significance of ‘shareholders inclusiveness’ in sustainability reporting.*
- (iii) *Write a note on ‘Agenda-21’.*
- (iv) *Discuss briefly the principle of absolute liability with the help of rule laid down in Rylands vs. Fletcher.*
- (v) *Discuss river water pollution citing at least one decision of the Supreme Court of India.* (5 marks each)

Answer 8(i)

Sustainable development is a broad concept that balances the need for economic growth with environmental protection and social equity. It is a process of change in which the exploitation of resources, the direction of investments, the orientation of technological development and institutional change are all in harmony and enhance both current and future potential to meet human needs and aspirations. Sustainable development is a broad concept and it combines economics, social justice, environmental science and management, business management, politics and law.

Corporate sustainability is a business approach that creates long-term shareholder value by embracing opportunities and managing risks deriving from economic, environmental and social developments. Corporate sustainability describes business practices built around social and environmental considerations.

It encompasses strategies and practices that aim to meet the needs of stakeholders today while seeking to protect, support and enhance the human and natural resources that will be needed in the future.

The four fundamental Principle of Sustainable Development agreed by the United Nations Conference on Environment and Development (UNCED) are:

1. *Principle of Intergenerational equity* : need to preserve natural resources for future generation.
2. *Principle of sustainable use* : use of natural resources in a prudent manner without or with minimum tolerable impact on nature.
3. *Principle of equitable use or intergenerational equity* : Use of natural resources by any state / country must take into account its impact on other states.
4. *Principle of integration* : Environmental aspects and impacts of socio-economic activities should be integrated so that prudent use of natural resources is ensured.

Answer 8(ii)

Companies generally consider the interests of the shareholders as the foremost. However, they should take into account other stakeholders interests also.

Stakeholders are entities or individuals that can reasonably be expected to be significantly affected by the organization's activities, products and/or services. Stakeholders' actions are also reasonably expected to affect the ability of the organization to successfully implement its strategies and meet its objectives. This included entities or individuals whose rights under law or international conventions provide them with legitimate claims vis-à-vis the organization.

Stakeholders engagement activities are an important tool in this direction. These may include for example, stakeholder engagement for the purpose of compliance with internationally agreed standards, or informing ongoing organizational / business processes. Organizations can also use other means such as the media, the scientific community, or collaborative activities with peers and stakeholders.

'The reporting organization should identify its stakeholders and explain in its report how it has responded to their reasonable expectations and interests'

The GRI guidance requires organization to document the stakeholder engagement processes. This will make the sustainability report assurable.

When stakeholder engagement processes are used for reporting purpose, they should be based on systematic or generally accepted approaches, methodologies or principles. The idea is to develop a proper understanding of the stakeholder information needs. “The reporting organization should document its approach for defining which stakeholders it engaged with, how and when it engaged with them, and how engagement has influenced the report content and the organization’s sustainability activities”

Answer 8(iii)

Agenda 21 – a blueprint for sustainable development into the 21st Century which was agreed during the “Earth Summit” at Rio in 1992, and signed by 179 Heads of State and Government.

Agenda 21 is a guide for individuals, businesses and governments in making choices for development that help society and the environment. Agenda 21 deals with

1. *Social and economic dimensions* : developing countries; poverty; consumption patterns; population; health; human settlements; integrating environment and development.
2. *Conservation and management of resources* : atmosphere; land; forests; deserts; mountains; agriculture; biodiversity; biotechnology; oceans; fresh water; toxic chemicals; hazardous radioactive and solid waste and sewage.
3. *Strengthening the role of major groups* : women; children and youth; indigenous peoples; non-governmental organisations; local authorities; workers; business and industry; farmers; scientists and technologists.
4. *Means of implementation* : finance; technology transfer; science; education; capacity-building; international institutions; legal measures; information.

Answer 8(iv)

In the past all actions for environmental torts against companies and industries were governed by the principle of strict liability. Strict liability means liability without fault i.e., without intention or negligence. In other words, the defendant is held liable without fault. Absolute liability for the escape of impounded waters was first established in England during the mid-nineteenth century in the case of *Rylands v. Fletcher*, (1868) LR 3 330.

The liability under this rule is strict and it is no defence to say that the thing escaped without that person’s willful act, default or neglect or even that he had no knowledge of its existence. The House of Lords, however, added a rider to the above statement stating that – this rule applies only to non-natural user of the land and it does not apply to things naturally established on the land or where the thing escaped due to an act of God or an act of stranger or the default of the person injured or where the thing which escapes is present by the consent of the person injured or in certain cases where there is statutory authority.

Answer 8(v)

Leather industry is one of the three major industries besides paper and textiles, consuming large quantities of water for processing of hides and skins into leather. Naturally

most of the water used is discharged as waste water containing putrescible organic and toxic inorganic materials which when discharged as such will deplete dissolved oxygen content of the receiving water courses resulting in the death of all aquatic life and emanating foul odour. The M.C. Mehta v. Union of India [AIR 1988 SC 1037] also known as the Kanpur Tanneries or Ganga Pollution case is among the most significant water pollution case. Detailed scientific investigations and the reports were produced before the Court as evidence. The alarming details given by M.C. Mehta about the extent of pollution in the river Ganga due to the inflow of sewage from Kanpur only, the Court came down heavily on the Nagar Mahapalika (Municipality) and emphasised that it is the Nagar Mahapalika of Kanpur that has to bear the major responsibility for the pollution of the river near Kanpur city.
