

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) *"Independent directors are known to bring objective view in Board deliberations. They also ensure that there is no dominance of one individual or special interest group or the stifling of healthy debate. They act as the guardians of the interest of all shareholders and stakeholders, especially in the areas of potential conflict."*
Discuss the above statement in the light of Clause 49 of the listing agreement.
(10 marks)
- (b) *State, with reasons in brief, whether the following statements are true or false :*
- (i) *Kautilya's Arthashastra maintains that for good governance all administrators including the king were considered the masters of the people.*
 - (ii) *Clause 49 of the listing agreement obligates a company to make disclosure about the remuneration of directors.*
 - (iii) *Any person, who has access to the price sensitive information, need not be an 'insider'.*
 - (iv) *Board meetings should be held at least four times in a year with a maximum gap of six months.*
 - (v) *Shareholders activism does not refer to the active involvement of stakeholders in their company.*
(2 marks each)

Answer 1(a)

Independent directors are known to bring an objective view in board deliberations. They also ensure that there is no dominance of one individual or special interest group or the stifling of healthy debate. They act as the guardians of the interest of all shareholders and stakeholders, especially in the areas of potential conflict.

Independent Directors bring a valuable outside perspective to the deliberations. They contribute significantly to the decision-making process of the Board. They can bring on objective view to the evaluation of the performance of Board and management. In addition, they can play an important role in areas where the interest of management, the company and shareholders may diverge such as executive remuneration, succession planning, changes in corporate control, audit function etc.

Independent directors are required because they perform the following important role :

- (i) Balance the often conflicting interests of the stakeholders.
- (ii) Facilitate withstanding and countering pressures from owners.

- (iii) Fulfill a useful role in succession planning.
- (iv) Act as a coach, mentor and sounding Board for their full time colleagues.
- (v) Provide independent judgment and wider perspectives.

In this context, the Clause 49 requires that the Board of directors of the company shall have an optimum combination of executive and non-executive directors with not less than fifty percent of the board of directors comprising of non-executive directors. In terms of Clause 49 of the Listing Agreement, at least one-third of the Board should comprise of independent directors where the Chairman of the Board is a non-executive director, and in case the Chairman is an executive director, at least half of the Board should comprise of independent directors.

Further, where the non-executive Chairman is a promoter of the company or is related to any promoter or person occupying management positions at the Board level or at one level below the Board, at least one-half of the Board of the company shall consist of independent directors.”

As per Clause 49, an independent director shall mean a mean a non-executive director of the company director who:

- (a) apart from receiving director’s remuneration, does not have any material pecuniary relationships or transactions with the company, its promoters, its directors, its senior management or its holding company, its subsidiaries and associates which may affect independence of the director;
- (b) is not related to promoters or persons occupying management positions at the board level or at one level below the board;
- (c) has not been an executive of the company in the immediately preceding three financial years;
- (d) is not a partner or an executive or was not partner or an executive during the preceding three years, of any of the following:
 - (i) the statutory audit firm or the internal audit firm that is associated with the company, and
 - (ii) the legal firm(s) and consulting firm(s) that have a material association with the company.
- (e) is not a material supplier, service provider or customer or a lessor or lessee of the company, which may affect independence of the director; and
- (f) is not a substantial shareholder of the company i.e. owning two percent or more of the block of voting shares;
- (g) is not less than 21 years of age.

Answer 1(b)(i)

False. Kautilya’s Arthashastra maintains that for good governance, all administrators including the King were considered the servants of the people.

Answer 1(b)(ii)

True. Clause 49 of the listing agreement obligates a company to make disclosure about the remuneration of directors.

Answer 1(b)(iii)

False. In terms clause 2 (e) (ii) of SEBI (Prohibition of Insider Trading) Regulations, 1992, Insider is any person who has received or has had access to unpublished price sensitive information in respect of securities of the company.

Answer 1(b)(iv)

False. Board meetings should be held at least four times in a year with a maximum gap of four months.

Answer 1(b)(v)

False. Shareholder activism refers to the active involvement of stockholders in their organization.

Question 2

(a) Write short notes on any three of the following :

- (i) *The Turnbull Report*
- (ii) *CII's Desirable Corporate Governance Code*
- (iii) *Role of institutional investors in Corporate Governance*
- (iv) *Shareholders' rights.* (3 marks each)

(b) *Juris Global Ltd., an LPO company, aims for listing at New York Stock Exchange (NYSE). The companies listed on the NYSE are required to comply with certain standards regarding Corporate Governance as prescribed in the NYSE's listing rules. Your company will be required, inter alia, to comply with these rules.*

As a Company Secretary, you are required to prepare a Board note highlighting the provisions of the NYSE's listing rules with respect to the Board structure and constitution of various committees of the Board. (6 marks)

Answer 2(a)(i)**The Turnbull Report**

The original Combined Code required companies to include a narrative statement in their Annual Report of how internal control provisions had been applied. However, the combined code did not have guidelines of how the provisions should be applied by the companies. This led to the establishment of a Working Group under the Chairmanship of Nigel Turnbull. Turnbull Committee published "Internal Control Guidance for Directors on Combined Code".

In 2004, the Financial Reporting Council established the Turnbull Review Group to consider the impact of the guidance and the related disclosures and to determine whether the guidance needed to be updated. In October 2005, the revised guidance was issued.

Answer 2(a)(ii)**CII'S Desirable Corporate Governance Code**

Confederation of Indian Industry (CII) took a special initiative on Corporate Governance, the first institution initiative in Indian Industry. The objective was to develop

and promote a code for Corporate Governance to be adopted and followed by Indian companies, whether in the Private Sector, the Public Sector, Banks or Financial Institutions, all of which are corporate entities. The final draft of the said Code was widely circulated in 1997. In April 1998, the Code was released. It was called Desirable Corporate Governance Code.

Answer 2(a)(iii)

Institutional shareholders should reflect the following characteristics:

- Take active interest in the composition of board of Directors
- Be vigilant
- Maintain regular and systematic contact at senior level for exchange of views on management, strategy, performance and quality of management
- Ensure that voting intentions are translated into practice
- Evaluate Corporate Governance performance of the company

The Combined Code (2008) stated the following principles of good governance for the Institutional Shareholders

(a) *Dialogue with companies*

Institutional shareholders should enter into a dialogue with companies based on the mutual understanding of objectives.

(b) *Evaluation of governance disclosures*

When evaluating companies' governance arrangements, particularly those relating to board structure and composition, institutional Investors should give due weight to all relevant factors drawn to their attention.

(c) *Shareholder voting*

Institutional shareholders have a responsibility to make considered use of their votes.

Answer 2(a)(iv)**Shareholders' Rights**

The provisions of Companies Act 1956 guarantee shareholders with several rights some of which have been discussed hereunder :

- Right to receive copies of the abridged balance-sheet and profit & loss account, report of cost auditor, contracts for appointment of the managing director/manager & notices of the general meetings of the company
- Right to inspect statutory registers/ returns and get copies thereof on payment of prescribed fee.
- Right to attend meetings of the shareholders and exercise voting rights at these meetings either personally or through proxy.

- Apart from these shareholders have right to receive share certificates, transfer shareholdings, right to receive dividend when declared, to appoint directors, right to share the surplus assets on winding up, right to collectively make application to the Central Government for the investigation of the affairs of the company.
- Under section 106 the rights attached to the shares of any class can be varied with the consent in writing of the holders of not less than three-fourths of the issued shares of that class or sanction in a separate meeting.
- Right to make application collectively to Company Law Board/ tribunal for oppression and mismanagement.
- Right of Dissident shareholders to apply to the court.

Answer 2(b)**Board of Directors**

Juris Global Limited

Sub : A note on the listing Requirements of NYSE in respect of Board structure and its committees.

Companies listed on the New York Stock Exchange are required to comply with certain standards regarding corporate governance NYSE Listing Rules. The relevant provisions of the New York Stock Exchange's Listing Rules are summarized below:

Board Structure

Listed companies must have a majority of independent directors

This condition is however not applicable to the following companies:

- A company of which more than 50% of the voting power is held by an individual, a group or another company.
- Limited partnerships and companies in bankruptcy proceedings need not comply with the requirements
- Listed companies that are foreign private issuers are permitted to follow home country practice in lieu of this provision

Criteria for determining Independence of Director

- (i) A director who is an employee or whose immediate family member is an executive officer, of the company is not independent until three years after the end of such employment relationship.
- (ii) A director who receives, or whose immediate family member receives, more than \$100,000 per year in direct compensation from the listed company, other than director and committee fees and pension or other forms of deferred compensation for prior service, is not independent until three years after he or she ceases to receive more than \$100,000 per year in such compensation.
- (iii) A director who is affiliated with or employed by, or whose immediate family

member is affiliated with or employed in a professional capacity by, a present or former internal or external auditor of the company is not “independent” until three years after the end of the affiliation or the employment or auditing relationship.

- (iv) A director who is employed, or whose immediate family member is employed, as an executive officer of another company where any of the listed company’s present executives serve on that company’s compensation committee is not “independent” until three years after the end of such service or the employment relationship.
- (v) A director who is an executive officer or an employee, or whose immediate family member is an executive officer, of a company that makes payments to, or receives payments from, the listed company for property or services in an amount which, in any single fiscal year, exceeds the greater of \$1 million, or 2% of such other company’s consolidated gross revenues, is not “independent” until three years after falling below such threshold.

Audit Committee

Listed companies must have an audit committee

Composition of Audit Committee

- The audit committee must have a minimum of three members.
- All the members of the Audit Committee must be independent
- Each member of the audit committee must be financially literate, as such qualification is interpreted by the company’s board in its business judgment, or must become financially literate within a reasonable period of time after his or her appointment to the audit committee.
- In addition, at least one member of the audit committee must have accounting or related financial management expertise, as the company’s board interprets such qualification in its business judgment.

Remuneration/Compensation Committee

Listed companies must have a compensation committee composed entirely of independent directors.

Nominating/Corporate Governance Committee

Listed companies must have a nominating/corporate governance committee composed entirely of independent directors.

Sd/-

Company Secretary

Question 3

- (a) “The rapidly growing global economy has created an expanding array of risks to be managed to ensure the viability and success of an enterprise.” Discuss this statement enumerating various classes of risks and the ways of risk handling.
(5 marks)

- (b) *“Corporate social responsibility is an evolving concept.” Describe and distinguish ‘corporate social responsibility’ with ‘corporate philanthropy’.* (5 marks)
- (c) *“Corporate communication is all about managing perceptions and ensuring effective and timely dissemination of information, positive corporate image, and smooth and affirmative relationship with all stakeholders.” Explain and outline the scope of corporate communication.* (5 marks)

Answer 3(a)

Risk may be broadly classified under the following heads:

- (a) Industry & Services Risks
- (b) Management and Operations Risks
- (c) Market Risks
- (d) Political Risks
- (e) Credit Risks
- (f) Liquidity Risks
- (g) Disaster Risks
- (h) Systems Risks
- (i) Legal Risks
- (j) Non-compliance and related risk

Risk Handling

Firms are not entirely free to decide on how they shall handle their risks. In every country there are governmental and official regulations governing health and safety at work like fire precautions, hygiene, environmental pollution, food, handling of dangerous substances and many other matters relating to properties, personal injuries and other risks. The Central Government and State Governments have enacted compulsory insurance regulations (for vehicles and individuals). And in addition a firm may be obliged to insure certain risks under provisions of leases, construction and other contracts. Failure to comply with both safety and compulsory insurance regulations may constitute a criminal offence and may lead to the closure of a plant or other establishments. Thus, if a firm wishes to carry on certain activities it must comply with the relevant official risk handling regulations. There will remain, however, broad areas where it can exercise its own discretion to control physical or financial loss.

Risks can be handled broadly in four ways:

Risk Avoidance

It is a rare possibility to avoid a risk completely. A riskless situation is rare. Generally risk avoidance is only feasible at the planning stage of an operation.

Risk Reduction

In many ways physical risk reduction (or loss prevention, as it is often called) is the best way of dealing with any risk situation and usually, it is possible to take steps to reduce the probability of loss. Again, the ideal time to think of risk reduction measures is at the planning stage of any new project when considerable improvement can be

achieved at little or no extra cost. The only cautionary note regarding risk reduction is that, as far as possible expenditure should be related to potential future saving in losses and other risk costs; in other words, risk prevention generally should be evaluated in the same way as other investment projects.

Risk Retention

It is also known as risk assumption or risk absorption. It is the most common risk management technique. This technique is used to take care of losses ranging from minor to major break-down of operation. There are two types of retention methods for containing losses as under:

- (i) Risk retained as part of deliberate management strategy after conscious evaluation of possible losses and causes. This is known as active form of risk retention.
- (ii) Risk retention occurred through negligence. This is known as passive form of risk retention.

Risk Transfer

This refers to legal assignment of cost of certain potential losses to another. The insurance of 'risks' is to occupy an important place, as it deals with those risks that could be transferred to an organization that specialises in accepting them, at a price. Usually, there are 3 major means of loss transfer viz., (i) By Tort (ii) By contract other than insurance (iii) By contract of insurance. The main method of risk transfer is insurance. The value of the insurance lies in the financial security that a firm can obtain by transferring to an insurer, in return for a premium for the risk of losses arising from the occurrence of a specified peril. Thus, insurance substitutes certainty for uncertainty. Insurance does not protect a firm against all perils but it offers restoration, atleast in part of any resultant economic loss.

Answer 3(b)

Philanthropy means the act of donating money, goods, time or effort to support a charitable cause with regard to a defined objective. Philanthropy can be equated with benevolence and charity for the poor and needy. Philanthropy can be any selfless giving towards any kind of social need that is not served, underserved, or perceived as unserved or underserved. Philanthropy can be by an individual or by a corporate.

The Etymological origin of the word is from Late Latin philanthropia, from Greek philanthropia, from philanthropos loving people that is phil- + anthropos human being. It is the active effort to promote human welfare.

Corporate Social Responsibility on the other hand is about how a company align their values to social causes by including and collaborating with their investors, suppliers, employees, regulators and the society as a whole. The investment in CSR may be on people centric issues and/or planet issues. CSR initiatives of a corporate is not a selfless act of giving; companies derive long-term benefits from the CSR initiatives and it is this enlightened self interest which is driving the CSR initiatives in companies.

Answer 3(c)

Corporate communication means the corporation's voice and the images it projects of itself to the various stakeholders. This includes various areas such as corporate

reputation, corporate advertising, and employee communications, government relations and media management. These days most of the bigger organizations have departments of corporate communication which appears on the organizational chart along with traditional functions like marketing or accounting.

The corporate communication can also be defined as the processes a company uses to communicate all its messages to key constituencies –

- a combination of meetings,
- interviews,
- speeches,
- reports,
- images
- advertising, and
- on-line communication.

Ideally, corporate communication is an attitude or a set of mental habits that employees internalize. The result is good communication practices that permeate an organisation and are present in all its communications with constituencies.

Corporate communications also includes all the products of communication, such as memos, letters, reports, websites, e-mails, speeches or new releases. In the aggregate of these messages is what a company sends to its constituencies, whether internal or external. The communications can be written communication verbal or spoken communications or non-verbal communications. Electronic channels like email, voice mail, telephone calls video conferencing and chat sessions are gaining more importance as communication channels.

Question 4

(a) *Describe briefly any three of the following :*

- (i) *ICSI initiatives towards Corporate Governance*
- (ii) *Prohibition on insider trading*
- (iii) *Mandatory committees under the listing agreement*
- (iv) *COSO's internal control framework.* (3 marks each)

(b) *Enumerate any six Corporate Governance Forums worldwide, which are instrumental in promoting the culture of creativity and compliance among corporates.* (6 marks)

Answer 4(a)(i)

ICSI's Philosophy on Corporate Governance

The ICSI, after extensive research, has taken a lead step in defining Corporate Governance as “the application of best management practices, compliance of law in letter and spirit and adherence to ethical standards for effective management and

distribution of wealth and discharge of social responsibility for sustainable development of all stakeholders.”

The ICSI National Awards for Excellence in Corporate Governance

In pursuit for excellence and to identify, foster and reward the culture of evolving globally acceptable standards of corporate governance among Indian companies, the Institute instituted the “ICSI National Award for Excellence in Corporate Governance” in the year 2001. The underlying guideline for the Corporate Governance Award is to identify the corporates, which best establish and follow, corporate governance norms in letter and spirit.

Institute’s Post Membership Qualification Course in Corporate Governance

In order to update members of ICSI about best practices in Corporate Governance, the ICSI has introduced Post Membership Qualification Course in Corporate Governance.

Some of ICSI’s other major initiatives in Corporate Governance include

- ICSI Recommendations to Strengthen Corporate Governance Framework.
- ICSI- Centre for Corporate Governance Research and Training
- Founder Trustee of National Foundation For Corporate Governance
- Secretarial Standards Board
- Segmentwise Role of Company Secretaries
- Directors’ Training and Orientation Investor Education Programmes
- MOU with Chambers on CSR

Answer 4(a)(ii)

Prohibition on insider trading

Regulation 2(e) of Securities and Exchange Board of India (Prohibition of Insider trading) Regulations, 1992 defines “insider” as any person who,

- (i) is or was connected with the company or is deemed to have been connected with the company and is reasonably expected to have access to unpublished price sensitive information in respect of securities of a company, or
- (ii) has received or has had access to such unpublished price sensitive information;

Regulation 3 of aforesaid regulations provide for restriction on trading of securities by providing that no insider shall—

- (i) either on his own behalf or on behalf of any other person, deal in securities of a company listed on any stock exchange when in possession of any unpublished price sensitive information; or
- (ii) communicate or counsel or procure directly or indirectly any unpublished price sensitive information to any person who while in possession of such unpublished price sensitive information shall not deal in securities.

It further provides that nothing contained above shall be applicable to any communication required in the ordinary course of business or profession or employment or under any law.

Answer 4(a)(iii)

Mandatory Committees

Audit Committee and Shareholder Grievance Committees are mandatory committees which has to be constituted by a listed entity to whom clause 49 of the Listing Agreement is applicable

A qualified and independent audit committee shall be set up, having minimum three directors as members. Two-thirds of the members of audit committee shall be independent directors.

In terms of Clause 49-IV(G)(iii) of the Listing Agreement, a board committee under the chairmanship of a non-executive director shall be formed to specifically look into the redressal of shareholder and investors complaints like transfer of shares, non-receipt of balance sheet, non-receipt of declared dividends etc. This Committee shall be designated as 'Shareholders/Investors Grievance Committee'.

Answer 4(a)(iv)

COSO is the acronym for Committee of Sponsoring Organizations of the Treadway Commission. COSO is a U.S. private-sector initiative. Its major objective is to identify the factors that cause fraudulent financial reporting and to make recommendations to reduce its incidence. COSO has established a common definition of internal controls, standards, and criteria against which companies and organizations can assess their control systems.

Internal control is a process, effected by an entity's board of directors, management and other personnel, designed to provide reasonable assurance regarding the achievement of objectives in the following categories:

- Effectiveness and efficiency of operations
- Reliability of financial reporting
- Compliance with applicable laws and regulations.

Answer 4(b)

(i) National Foundation for Corporate Governance (NFCG)

With the goal of promoting better corporate governance practices in India, the Ministry of Corporate Affairs, Government of India, has set up National Foundation for Corporate Governance (NFCG) in partnership with Confederation of Indian Industry (CII), Institute of Company Secretaries of India (ICSI) and Institute of Chartered Accountants of India (ICAI).

NFCG endeavours to build capabilities in the area of research in corporate governance and to disseminate quality and timely information to concerned

stakeholders. It works to foster partnerships with national as well as international organisations.

(ii) Organisation for Economic Co-operation & Development (OECD)

The Organisation for Economic Co-operation and Development (OECD) was established in 1961. The OECD was one of the first non-government organizations to spell out the principles that should govern corporates.

The OECD Principles of Corporate Governance set out a framework for good practice which was agreed by the governments of all 30 countries that are members of the OECD. They were designed to assist governments and regulatory bodies in both OECD countries and elsewhere in drawing up and enforcing effective rules, regulations and codes of corporate governance. They also provide guidance for stock-exchanges, investors, companies and others that have a role in the process of developing good corporate governance.

(iii) Global Corporate Governance forum (GCGF)

The Global Corporate Governance Forum (the Forum) was founded in 2001 by the World Bank and the Organisation for Economic Co-operation and Development (OECD) following the financial crises in Asia and Russia in the latter part of the 1990's. It was established to promote initiatives to raise corporate governance standards and practices in developing countries and emerging markets, using the OECD Principles of Corporate Governance as the basis for its work.

(iv) Common Wealth Association of Corporate Governance (CACG)

The Commonwealth Association of Corporate Governance (CACG) was established in 1998 with the objective of promoting the best international standards on corporate governance throughout the Commonwealth as a means to achieve global standards of business efficiency, commercial probity and effective economic and social development.

(v) International Corporate Governance Network (ICGN)

The International Corporate Governance Network ("ICGN") is a not-for-profit company limited by guarantee under the laws of England and Wales. The Network's mission is to develop and encourage adherence to corporate governance standards and guidelines, and to promote good corporate governance worldwide.

(vi) European Corporate Governance Institute (ECGI)

The European Corporate Governance Institute (ECGI) was founded in 2002. It has been established to improve corporate governance through fostering independent scientific research and related activities.

(vii) Conference Board

The Conference Board was established in 1916 in the United States of America. The Conference Board governance programs helps companies improve their

processes, inspire public confidence, and ensure they are complying with regulations.

(viii) Asian Corporate Governance Association (ACGA)

The Asian Corporate Governance Association (ACGA) is an independent, non-profit membership organisation dedicated to working with investors, companies and regulators in the implementation of effective corporate governance practices throughout Asia.

(Note : Candidates may elaborate on any six forums.)

PART B

(Answer **ANY TWO** questions from this part)

Question 5

- (a) *“The code of conduct of each company summarises its philosophy of doing business.*

The exact details of this code are a matter of discretion, but there are some common principles in drafting of the code in most of the companies.” What are these principles ? (6 marks)

- (b) *Write short notes on any three of the following :*

- (i) *Activity analysis*
- (ii) *Code of ethics*
- (iii) *Deontological ethics*
- (iv) *Ethics in marketing.*

(3 marks each)

Answer 5(a)

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 5(b)(i)**Activity Analysis**

The ethical dimension of an activity can be determined with the help of the following grid which is self-explanatory:

Activity Analysis
(Ethical)

Parasite	Win-win Situation
Helping self	Helping self
Injuring Others	Helping Others
Martyr	Total Loss
Helping Others	Injuring self
Injuring self	Injuring Others

The first block in the grid – help self and injuring others is obviously unethical. The second block that is helping others and injuring self may appear to be ethical, however it is not ethical. The third grid wherein one helps self and also helps others is the most ideal and ethical situation. The win-win situation. The last grid is a situation that should be avoided at all costs and is highly unethical.

Answer 5(b)(ii)

A **code of ethics** consists of general statements, sometimes altruistic or inspirational, that serve as principles and the basis for rules of conduct. A code of ethics generally specifies methods for reporting violations, disciplinary action for violations, and a structure of due process.

A code of ethics should reflect upper managers' desire for compliance with the values, rules, and policies that support an ethical climate. The development of a code of ethics should involve the president, board of directors, and chief executive officers who will be implementing the code. Legal staff should also be called on to ensure that the code has correctly assessed key areas of risk and that it provides buffers for potential legal problems.

Corporate codes of 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.

Answer 5(b)(iii)

Deontological ethics or **deontology** (Greek: (deon) meaning 'obligation' or 'duty') is an approach to ethics that focuses on the rightness or wrongness of actions themselves, as opposed to the rightness or wrongness of the consequences of those actions. Thus, the term 'deontological' picked out the set of ethical theories that are

based on the idea that an action's being right or wrong is basic and the determining factor, and whether a situation is good or bad depends on whether the action that brought it about was right or wrong. This can be clarified with an example – if a manager decides that it is his duty to always be on time to meetings is running late for reasons not in his control, how is he supposed to drive to reach the meeting on time? Is he supposed to speed, breaking his duty to uphold the law, or is he supposed to arrive at his meeting late, breaking his duty to be on time?

Answer 5(b)(iv)

Ethics in Marketing

Marketing ethics is the area of applied ethics which deals with the moral principles behind the operation and regulation of marketing. The ethical issues confronted in this area include :

- Pricing : price fixing, price discrimination, price skimming.
- Anti-competitive practices like manipulation of supply, exclusive dealing arrangements, tying arrangements etc.
- Misleading advertisements
- Content of advertisements.
- Children and marketing.
- Black markets, grey markets.

Question 6

- (a) *"A major step in developing an effective ethics programme is implementing a training programme and communication system to communicate and educate employees about the company's ethical standards." Elucidate. (5 marks)*
- (b) *What is 'ethics committee' ? Describe the functions of an ethics committee. (5 marks)*
- (c) *"There are four theses viewing stakeholders' theory." Describe and discuss. (5 marks)*

Answer 6(a)

Ethics Training and Communication

A major step in developing an effective ethics program is implementing a training program and communication system to communicate and educate employees about the firm's ethical standards.

Training can educate employees about the firm's policies and expectations, as well as relevant laws and regulations and general social standards. Training programs can make employees aware of available resources, support systems, and designated personnel who can assist them with ethical and legal advice. They can also empower employees to ask tough questions and make ethical decisions. Many companies are now incorporating ethics training into their employee and management development training efforts.

If ethics training is to be effective, it must start with a foundation, a code of ethics, a procedure for airing ethical concerns, line and staff involvements, and executive priorities on ethics that are communicated to employees. Managers from every department must be involved in the development of an ethics training program. Training and communication initiatives should reflect the unique characteristics of an organization: its size, culture, values, management style, and employee base. It is important for the ethics program to differentiate between personal and organizational ethics.

To be successful, business ethics programs should educate employees about formal ethical frameworks and more for analyzing business ethics issue. Then employees can base ethical decisions on their knowledge of choices rather than on emotions.

Answer 6(b)

Ethics Committee

Companies should have a committee of independent non-executive directors who are responsible for ensuring that systems are in place in the company to assure employee compliance with the Code of Ethics.

Functions of Ethics Committee

The oversight process of the Ethics Committee of an organization involves the following areas to be addressed by it:

Review of the definitions of standards and procedures

The Committee should review the organization's areas of operation, the activities that require a formal set of ethical standards and procedures.

Once the review is complete and any shortcomings have come to light the ethics committee should assign the creation of revised guidelines to the appropriate personnel including the design of a formal method for communicating standards and procedures to employees. This method should ensure that employees both understand and accept the ethics program.

The ethics committee can suggest behaviors to upper management that reinforce the organization's guidelines.

Facilitate Compliance

The ethics Committee has the responsibility for overall compliance. It is the responsible authority for ethics compliance within its area of jurisdiction. It should serve as the court of last resort concerning interpretations of the organization's standards and procedures. When and if inconsistencies come to light in this manner, the committee should make recommendations on improving the existing compliance mechanisms. And, as always, there should be follow-up to ensure that compliance recommendations have been understood and accepted.

Due diligence of prospective employees

The ethics committee should define how the organization will balance the rights of individual applicants and employees against the organization's need to avoid risks that come from placing known violators in positions of discretionary responsibility. This includes

the oversight of background investigations on employees/applicants who are being considered for such positions.

Oversight of communication and training of ethics programme

The ethics committee should define methods and mechanisms for communicating ethical standards and procedures. This includes the distribution of documents (codes of conduct, for example) to ensure that every employee understands and accepts the organization's ethical guidelines. To make certain that published standards are understood, the ethics committee should provide regular training sessions as well.

Since communication is two-way, the ethics committee should solicit stakeholder input regarding how standards and procedures are defined and enforced. In this connection, it is useful to create ways of providing proof that each employee has received the appropriate documents and understands the standards and procedures described.

Monitor and audit compliance

Compliance is an ongoing necessity and the ethics committee should design controls which monitor, audit and demonstrate employees' adherence to published standards and procedures. There should also be mechanisms which check the effectiveness and reliability of such internal controls.

To warrant that the organization's goals, objectives and plans do not conflict with its ethical standards and procedures, the ethics committee should develop methods for regular review and assessment.

Enforcement of disciplinary mechanism

Disciplinary provisions should be in place to ensure consistent responses to similar violations of standards and procedures (as against applying different standards to different employees based on their position, performance, function, and the like). There should be provisions for those who ignore as well as those who violate standards and procedures.

Analysis and follow-up

When violations occur, the ethics committee should have ways to identify why they occurred. It is also important that lessons learned from prior violations are systematically applied to reduce the chance that similar violations takes place in future.

Answer 6(c)

There are four theses viewing stakeholder theory:

1. *Descriptive* : The Corporation is viewed as an assemblage of co-operative and competitive interests possessing intrinsic value. The theory is used to describe specific corporate characteristics such as nature of the firm, the way managers think about managing, how corporations are managed, or how the board members think about the interests of constituencies.

Descriptive stakeholders are defined as to whether they are affected by the firm and/or can potentially affect the firm.

2. *Instrumental* : This approach establishes a framework of examining ceteris paribus

connections, between the practice of stakeholder management and achievement of corporate performance goals. If you want to achieve (avoid) results_____, then adopt (don't adopt) principles & practices.....

Instrumental stakeholders are defined by the need of the management to take them into account when trying to achieve their goals.

3. *Normative* : The identification of moral or physical guidelines for the management of corporations. This approach is categorical in effect it says—'Do (don't do) this because it is the right (wrong) thing to do' .

Normative stakeholders have a valid normative claim on the firm.

4. *Broadly managerial* : It recommends attitudes, structures and practices that taken together constitute stakeholder management. Stakeholder management requires, as it key attribute, simultaneous attention to legitimate interests of all appropriate stakeholders, both in the establishment of organization structures and general policies.

Question 7

- (a) *Explain the Clarkson Principles of Stakeholders' Management.* (5 marks)
- (b) *"The ethical tendency or climate of an organisation is set at the top." In the light of this statement, critically examine the role of Board of directors in the ethical climate of a company.* (5 marks)
- (c) *"Social and ethical accounting is a process that helps a company to address issues of accountability to stakeholders and to improve performance of all aspects, viz., social, environmental and economic." Explain and discuss briefly the principles of social and ethical accounting.* (5 marks)

Answer 7(a)

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(b)

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 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 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 7(c)

Social and ethical accounting 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.

The dominant principle of social and ethical accounting is inclusivity. This principle

requires that the aspirations and needs of all stakeholder groups are taken into account at all stages of the social and ethical accounting process.

- *Planning* : The company commits to the process of social and ethical accounting, auditing and reporting, and defines and reviews its values and social and ethical objectives and targets.
- *Accounting* : The scope of the process is defined, information is collated and analysed, and performance targets and improvement plans are developed.
- *Reporting* : A report on the company's systems and performance is prepared.
- *Auditing* : The process of preparing the report and the report itself are externally audited, and the report is made accessible to stakeholders in order to obtain feedback from them.
- *Embedding* : To support each of the stages, structures and systems are developed to strengthen the process and to integrate it into the company's activities.
- *Stakeholder engagement* : The concerns of stakeholders are addressed at each stage of the process through regular involvement.

PART C

Question 8

Attempt any four of the following :

- (i) *Write a note on 'sustainability reporting in emerging economies'.*
- (ii) *Discuss the fundamental principles of sustainable development. How are these principles related to United Nations Conference on Environment and Development (UNCED), 1992 held at Rio de Janeiro ?*
- (iii) *What is the 'global compact' ? What are the objectives of this initiative?*
- (iv) *What is difference between 'convention' and 'protocol' ? Discuss briefly the major features of Kyoto Protocol. How was the implementation of Kyoto Protocol accorded ?*
- (v) *The Supreme Court of India has shown its concern about the discharge of untreated effluents into the rivers in many cases. Discuss the problem of water pollution in India and court's initiatives for its protection in the light of decided case law.* (5 marks each)

Answer 8(i)

Investors increasingly recognize the value of robust sustainability reporting and expectations for such reporting have spread to companies in emerging markets. While it may be difficult for emerging market companies to devote the resources to such reporting and companies should begin by taking the first step, committing to the process of reporting, and demonstrating that they are managing the sustainability issues most material to their sector. Such companies will develop a competitive advantage in the marketplace and reach a greater range of investors and customers.

Increasingly global companies understand that a commitment to sustainability reporting can contribute to financial success. Such transparency allows companies to reach a broader range of investors and customers, enhance operational efficiency, improve brand positioning, and develop leadership in the marketplace.

Answer 8(ii)

Four fundamental Principle of Sustainable Development agreed by the world community 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.

This was reinforced at the United Nations Conference on Environment and Development (UNCED) held in Rio de Janeiro in 1992. It is now universally acknowledged that the present generation has to ensure that the people coming ahead, the generations still unborn, have a world no worse than ours and hopefully better.

Answer 8(iii)

The UN Global Compact presents a unique and powerful platform for participants to advance their commitments to sustainability and corporate citizenship. More than 5200 company are participants and has stakeholders from more than 120 countries, over 60 networks in developed and emerging economies.

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.”

Answer 8(iv)

The Kyoto Protocol, adopted at the third Conference of the Parties to the UNFCCC (COP 3) in Kyoto, Japan, in 1997 came into force in 2005, is an international agreement linked to the United Nations Framework Convention on Climate Change. The major feature of the Kyoto Protocol is that it sets binding targets for 37 industrialized countries and the European community for reducing greenhouse gas (GHG) emissions. These amount to an average of five per cent against 1990 levels over the five-year period 2008-2012.

The major distinction between the Protocol and the Convention is that while the Convention encouraged industrialised countries to stabilize GHG emissions, the Protocol commits them to do so.

The Protocol requires developed countries to reduce their GHG emissions below levels specified for each of them in the Treaty. These targets must be met within a five-year time frame between 2008 and 2012, and add up to a total cut in GHG emissions of at least 5% against the baseline of 1990.

The Kyoto Protocol is generally seen as an important first step towards a truly global emission reduction regime that will stabilize GHG concentrations at a level which will avoid dangerous climate change. As a result of the Protocol, governments have already put, and are continuing to put legislation and policies in place to meet their commitments; a carbon market has been created; and more and more businesses are making the investment decisions needed for a climate-friendly future. The Protocol provides the essential architecture for any new international agreement or set of agreements on climate change. The first commitment period of the Kyoto Protocol expires in 2012.

The detailed rules for the implementation of the Protocol were adopted at COP 7 in Marrakesh in 2001, and are called the “Marrakesh Accords.”

Answer 8(v)

Water Pollution

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.

“Where in public interest litigation owners of some of the tanneries discharging effluents from their factories in Ganga and not setting up a primary treatment plant in spite of being asked to do so for several years did not care, in spite of notice to them, even to enter appearances in the Supreme Court to express their willingness to take appropriate steps to establish the pre-treatment plants it was held that so far as they were concerned on order directing them to stop working their tanneries should be passed. It was observed that the effluent discharged from a tannery is ten times noxious when compared with the domestic sewage water which flows into the river from any urban area on its bank. It was further observed that the financial capacity of the tanneries should be considered as irrelevant while requiring them to establish primary treatment plants. Just like an industry which cannot pay minimum wages to its worker cannot be allowed to exist, a tannery which cannot set up a primary treatment plant cannot be permitted to continue to be in existence for the adverse effect on the public at large which is likely to ensue by the discharging of the trade effluents from the tannery to the river Ganga would be immense and it will outweigh any inconvenience that may be caused to the management and the labour employed by it on account of its closure”.
