GOVERNANCE AND ETHICS

CS SECTION 5

STUDY NOTES

KASNEB SYLLABUS

CONTENT

CHAPTER ONE

INTRODUCTION TO GOVERNANCE

Introduction

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

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

Corporate Governance deals with the manner the providers of finance guarantee themselves of getting a fair return on their investment. Corporate Governance clearly distinguishes between the owners and the managers. The managers are the deciding authority. In modern corporations, the functions/ tasks of owners and managers should be clearly defined, rather, harmonizing.

Corporate Governance deals with determining ways to take effective strategic decisions. It gives ultimate authority and complete responsibility to the Board of Directors. In today's market- oriented economy, the need for corporate governance arises. Also, efficiency as well as globalization are significant factors urging corporate governance. Corporate Governance is essential to develop added value to the stakeholders.

Corporate Governance ensures transparency which ensures strong and balanced economic development. This also ensures that the interests of all shareholders (majority as well as minority shareholders) are safeguarded. It ensures that all shareholders fully exercise their rights and that the organization fully recognizes their rights.

Corporate Governance has a broad scope. It includes both social and institutional aspects. Corporate Governance encourages a trustworthy, moral, as well as ethical environment.

Importance of Corporate Governance

1. Good corporate governance ensures corporate success and economic growth.
2. Strong corporate governance maintains investors' confidence, as a result of which, company can raise capital efficiently and effectively.
3. It lowers the capital cost.
4. There is a positive impact on the share price.
5. It provides proper inducement to the owners as well as managers to achieve objectives that are in interests of the shareholders and the organization.
6. Good corporate governance also minimizes wastages, corruption, risks and mismanagement.
7. It helps in brand formation and development.
8. It ensures organization in managed in a manner that fits the best interests of all.

Principles of Corporate Governance

Corporate governance in the Company is based on the following principles:

Accountability
The Code of Corporate Governance envisages accountability of the Board of Directors of the Company before all shareholders in accordance with the legislation in force, and is the governing document for the Board of Directors in issues related to strategy planning, administration and control over the Company's executive bodies.

Fairness
The Company undertakes to protect the rights of its shareholders and treat all shareholders on an equal basis. The Board of Directors enables its shareholders to receive efficient protection if their rights are violated.

Transparency
The Company shall provide timely disclosure of credible information on all the important facts related to its activities, including information on its financial condition, social and environmental measures, results of activities, ownership and management structures; the Company shall provide free access to such information for all interested parties.

Responsibility
The Company acknowledges the rights of all interested parties envisaged by the legislation in force, and aims at cooperation with such parties in order to provide steady development and ensure financial stability of the Company.

PRINCIPLES OF GOOD CORPORATE GOVERNANCE

i. introduction

Corporate Governance is concerned with the establishment of an appropriate legal, economic and institutional environment that would facilitate and allow business enterprises to grow, thrive and survive as institutions for maximizing shareholder value while being conscious of and providing for the well-being of all other stakeholders and society.

Good Corporate Governance requires that the State puts in place and maintains an enabling environment in which efficient and well-managed companies can thrive. It is therefore expected that companies will continue to play their part in encouraging dialogue between the public and private sectors in promoting good public governance and an enabling business environment.

It is the responsibility of the owners of the corporation to elect competent directors and to ensure that they govern the corporation in a manner consistent with their stewardship.

Good corporate governance dictates that the Board of Directors governs the corporation in a way that maximizes shareholder value and in the best interest of society. It is neither in the long-term interest of the enterprise or society to short-change customers, exploit labour, pollute the environment or engage in corrupt practices.

The guidelines which follow set 21 principles of good corporate governance, aimed primarily at the Board of Directors in corporations with a unitary Board structure. These are followed by a sample code which expounds on these principles.
The following is a summary of the principles of good corporate governance:

Authority and Duties of Members [or Shareholders]

Members or shareholders [as owners] of the corporation shall jointly and severally protect, preserve and actively exercise the supreme authority of the corporation in general meetings. They have a duty, jointly and severally, to exercise that supreme authority of the corporation to:

- ♦ Ensure that only competent and reliable persons, who can add value, are elected or appointed to the Board of Directors;
- ♦ Ensure that the Board is constantly held accountable and responsible for the efficient and effective governance of the corporation so as to achieve corporate objectives, prosperity and sustainability.
- ♦ Change the composition of a Board that does not perform to expectation or in accordance with the mandate of the corporation.

Leadership
Every corporation should be headed by an effective Board that should exercise leadership, enterprise, integrity and judgment in directing the corporation so as to achieve continuing prosperity and to act in the best interest of the enterprise in a manner based on transparency, accountability and responsibility.

Appointments to the Board
Appointments to the Board of Directors should, through a managed and effective process, ensure that a balanced mix of proficient individuals is made and that each of those appointed is able to add value and bring independent judgment to bear on the decision-making process.

Strategy and Values
The Board of Directors should determine the purpose and values of the corporation, determine the strategy to achieve that purpose and implement its values in order to ensure that the corporation survives and thrives and that procedures and values that protect the assets and reputation of the corporation are put in place.

Structure and Organization
The Board should ensure that a proper management structure [organization, systems and people] is in place and make sure that the structure functions to maintain corporate integrity, reputation and responsibility.

Corporate Performance, Viability and Financial Sustainability
The Board should monitor and evaluate the implementation of strategies, policies and management performance criteria and the plans of the corporation. In addition, the Board should constantly review the viability and financial sustainability of the enterprise and must do so at least once every year.

Corporate Compliance
The Board should ensure that the corporation complies with all relevant laws, regulations, governance practices, accounting and auditing standards.

Corporate Communication
The Board should ensure that the corporation communicates with all its stakeholders effectively.

Accountability to Members
The Board should serve the legitimate interests of all members and account to them fully.

Responsibility to Stakeholders
The Board should identify the corporation‘s internal and external stakeholders; agree on a policy or policies determining how the corporation should relate to, and with them, in creating wealth, jobs and the sustainability of a financially sound corporation while ensuring that the rights of stakeholders [whether established by law or custom] are respected, recognized and protected.

Balance of Powers

The Board should ensure that no one person or group of persons has unfettered power and that there is an appropriate balance of power on the Board so that it can exercise objective and independent judgment.

Internal Control Procedures
The Board should regularly review systems, processes and procedures to ensure the effectiveness of its internal systems of control so that its decision-making capability and the accuracy of its reporting and financial results are maintained at the highest level at all times.

Assessment of Performance of the Board of Directors

The Board should regularly assess its performance and effectiveness as a whole and that of individual members, including the Chief Executive Officer. A summary of the major findings together with a statement confirming that the Board has carried out a self-assessment exercise should be made to the annual general meeting.

Induction, Development and Strengthening of Skills of Board Members

The Board should recognize the need for new members to be inducted into their roles and for all Board members to develop and strengthen their governance skills in light of technological developments, changing corporate environment and other variables. The Board should accordingly organize for the systematic induction and continuous development of its members.

Appointment and Development of Executive Management

The Board should appoint the Chief Executive Officer and participate in the appointment of all senior management, ensure motivation and protection of intellectual capital crucial to the corporation, ensure that there is appropriate and adequate training for management and other employees and put in place a succession plan for senior management.

Adoption of Technology and Skills

The Board must recognize that to survive and thrive it has to ensure that the technology, skills and systems used in the corporation are adequate to run the corporation and that the corporation constantly reviews and adopts the same in order to remain competitive.

Management of Corporate Risk

The Board must identify key risk areas and key performance indicators of the corporation‘s business and constantly monitor these factors.

Corporate Culture
The Board should define, promote and protect the corporate ethos, ethics and beliefs on which the corporation premises its policies, actions and behaviour in its relationships with all who deal with it.