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# National Conference On "Corporate Governance in Business Ethics"

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**INTRODUCTION**

Over the last two decades, corporate governance has attracted a great deal of public interest because of its apparent importance for the economic health of corporations and society in general. Corporate governance is the system by which business corporations aredirected and controlled. The corporate governance structure specifies the distribution of rights and responsibilities among different participants in the corporation, such as, the board, managers, shareholders and other stakeholders and spells out the rules and procedures for making decisions in corporate affairs. By doing this, it also provides the structure through which the company objectives are set and the means of attaining those objectives and monitoring performance.

***Importance of Ethics in Business***

Metaethics is the study of the origin and meaning of ethical concepts. Broadly, it deals with metaphysical, psychological and linguistic issues. While normative ethics establishes certain moral standards for human behavior. Normative ethics is further classified as: teleological, deontological and virtue ethics. According to teleological ethical theory, an action is considered morally correct if the consequences of that action are more favorable than unfavorable. Deontological ethical theory focuses on certain fundamental duties such as duties to God, duties to oneself and duties to others. Applied ethics deals with specific controversial issues like capital punishment, abortion and nuclear war.

***Ethical Issues in Finance***

The attitude of a business towards its employee's acts is a litmus test for its ethical character. The relationship between the business and its employees is based on the employment contract. An ethical organization follows the principle of ethical selection for hiring prospective employees. According to the principle of ethical selection factors like age, gender, religion and nationality are irrelevant for hiring a person. Ethical remuneration rewards only those acts of an employee that contribute to long-term owner value.

***Ethical Issues in Human Resource Management***

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***Corporate responsibility towards stake holders***

It provides an overview of corporate responsibility towards its stakeholder's i.e. internal and external stakeholders. Internal stakeholders are shareholders, employees and management. External stakeholders include consumers, suppliers, creditors competitors and community. Shareholders are important to the business, because they have a primary stake in the business. To provide professional management, fair returns on their investment, disclose relevant information, protect shareholders assets etc. The organizations responsibility towards employees are improving working conditions, maintaining open and honest communications, welcoming

suggestions/complaints, providing equal opportunity etc. Management plays a key role in balancing the multiple claims of stakeholders. Therefore the responsibility of management involves maintaining healthy relationships among the stakeholders.

***Corporate Governance and Business Ethics***

Sound corporate governance and ethical business practices are critical to a company's long-term success. Corporate governance refers to how a company is structured including its by-laws, code of ethics, and board of directors as well as the incentives and culture established at the top. Business ethics refers to the morality and integrity of how a company conducts its operations around the world, including its policies for suppliers and vendors. A well-governed company has strong, transparent policies in both areas with accountability and rigorous board oversight and operates in the best interests of its shareholders, employees, customers, community, and the environment. Over the past decade, we have witnessed numerous corporate governance and ethics scandals, from accounting irregularities, to rogue stock traders costing investors billions of dollars, to allegations of bribery and illicit corporate payments to foreign governments. But the most devastating example of all was the lack of adequate governance and oversight by many financial organizations including rating agencies and regulators that led to the 2008 financial crisis. Clearly, a company's governance and ethical business practices affect not only its reputation, brand, employees, and bottom line; they can impact an entire industry, as well as investors, governments, and consumers.

***Good Governance***

These areas are especially important in assessing governance and business ethics practices:

- **Sustainability Reporting.** The regularity and degree of transparency in a company's sustainability reports is a key barometer of its governance standards. As they say, "What isn't measured isn't managed." Therefore, annually published reports, with audited and independently verified data, is considered a corporate governance best practice. Momentum is growing for companies to follow the Global Reporting Initiative (GRI) guidelines—the most widely used, standardized sustainability reporting framework in the world. The guidelines were created by an international, independent group of businesses, investment firms, and non-governmental agencies, in which Calvert participated. The GRI seeks to make sustainability reporting as common—and as comprehensive—as financial reporting. Calvert gives high marks to companies that use the GRI sustainability reporting guidelines.
- **Board Diversity.** For years, Calvert has regarded board diversity as a critical governance goal. A company's board membership should broadly reflect its customer base and employees. The array of viewpoints, skills, background, and experience provided by boards whose members have diverse backgrounds gives the company a broader foundation to draw upon for strategic decision-making especially in today's highly competitive, global marketplace. Unfortunately, while progress has been made over the years, women still hold just 18% of corporate board of director seats, yet comprise nearly 50% of the workforce. We believe that to be marketplace leaders, companies must actively seek women and minority candidates for their boardrooms. In fact, a McKinsey & Company study found that companies with the highest share of women on executive committees outperformed those with all-male executive committees, earning a 41% higher return on equity and 56% better operating results.
- **Executive Compensation.** Since the onset of the financial crisis, reports of multi-million dollar compensation and severance packages received for executives of companies that have suffered losses, foreclosed on homeowners, or laid off employees have sparked a public outcry. Doling out excessive payments to executives at the expense of other employees is in direct contrast to shareholders' interests and often increases employee turnover. We also have found that excessive executive compensation during a period of lackluster business performance may be an early indication of bigger trouble at a company. Poorly designed compensation programs that encourage executives to manage for short-term performance—at the expense of long-term profitability are another concern, potentially compromising the governance goals of a corporation. We strongly believe it is in the best interests of a firm to align senior management's risks and rewards with those of employees, shareholders, and the long-term performance of the corporation. "Pay-for-performance" compensation plans, for example, typically link executive compensation to clearly defined and rigorous criteria.

***Driving Progress in Corporate Governance***

As customers and investors have raised their expectations for companies to operate sustainably, the United States has toughened its regulation of corporate governance issues. In 2002, the Sarbanes-Oxley Act set today's standards for U.S. public company boards, management, and public accounting firms in an effort to restore public confidence in corporate America. More recently, in the wake of the global financial crisis, Calvert joined forces with other investors to advocate for the Dodd-Frank Wall Street Reform and Consumer Protection Act, specifically those provisions on executive compensation, golden parachutes, share holder "say on pay," and "claw-back" policies to recover pay from employees whose actions created substantial financial or legal repercussions. The Act was passed in 2011. . Over the last decade, we believe companies have made progress in the corporate governance arena in response to both public and private pressures and increased regulatory oversight. Ultimately, reinforcing this link will promote more sustainable long-term performance for companies and their shareholders.

***Business ethics should permeate the whole organisation***

The trouble with much of the debate about corporate governance is that it looks on it as a separate discipline, a series of boxes to be ticked, including ensuring that the business is perceived to be ethical. Often this results in grandiose statements or whole reports in the annual accounts about all the initiatives the company funds, participates in or supports in other ways. Worthy as these initiatives may be, in our view, in most cases this is at least as much (or more) about the perception than a real commitment to running the business ethically. To do this requires business ethics to permeate the whole organisation - including/especially the recruitment process - and have measures in place to catch questionable practices. In this way it is much less likely that people with malicious intent or susceptible natures will survive in the organisation, because such behaviour will be picked up and fed back - crucially, independently - to senior management and the board, ideally via the Senior Independent Director and other non-executives. As the famous saying goes, the fish rots from the head, so this requires complete commitment from the board not only to the principles of business ethics but to the measurement and benchmarking of ethical performance.

***Corporate Social Responsibility (CSR)***

CSR can be understood in terms of corporate responsibility, but with greater stress upon the obligations a company has to the community, particularly with respect to charitable activities and environmental stewardship. Corporate and social responsibility is sometimes described as being a tacit contract between business and a community, whereby the community permits the business to operate within its jurisdiction to obtain jobs for residents and revenue through taxation. Additionally, the community expects the business to preserve the environment and to make the community a better place to live and to work through charitable activities Business for Social Responsibility (2001) speaks of CSR in the following terms: "Socially responsible business practices strengthen corporate accountability, respecting ethical values in the interests of all stakeholders. Responsible business practices respect and preserve the natural environment. Helping to improve the quality and opportunities of life, they empower people and invest in communities where a business operates." Currently, European companies seem to be adopting offices of corporate environmental and social responsibility more often than U.S. companies. It should be noted that some business ethics organizations believe that corporate responsibility encompasses all responsibilities that a company has to all of its stakeholders, which includes ethical, social and environmental responsibilities.

***CSR/Sustainability Report***

Leadership companies understand the value of assessing their social and environmental performance on a regular basis. From the informal query "how are we doing?", to scheduled surveys, to formal audit processes conducted by outside experts, companies are seeking information about how they are viewed and how they are progressing in meeting the expectations of investors, employees, customers, business partners, and community leaders on a range of corporate social and environmental responsibility issues. Companies that produce these reports show a resource commitment to the issues and a willingness to be transparent. While no company completely

discloses all of their information, companies that make stakeholders aware of their policies and procedures build trust. Reporting allows investors, employees, consumers and regulators to make informed decisions. Sample companies fulfilled this indicator if they produced and released a CSR/sustainability report in the last two years. Companies that just mentioned CSR activities on a website or have not kept their reporting practices up to date were not seen as having a strong enough commitment of resources to CSR and did not meet the indicator. If a company devoted a large portion of its Annual Report to CSR/sustainability the company was credited.

***CSR as a Corporate Principle***

If a company is truly committed to CSR they regard it as an integral part of the business decision making process and prominently place it in the company's core mission, vision, and values documents. These simple but important statements succinctly state company goals and aspirations. They also provide insight into a company's values, culture, and strategies for achieving its aims. The mission or vision of a socially responsible business frequently references a purpose beyond "making a profit" or "being the best," and specifies that it will engage in ethical businesses practices and seek to create value for a variety of stakeholders, including shareholders/owners, employees, customers, vendors, communities, and the natural environment (A. Townley, personal communication, May 5, 2004). Sample companies satisfied this indicator if they stated CSR as an intricate part of their corporate objectives and conducted their business in a manner that was consistent with their statement.

***Fraud Can Happen Anywhere***

Traditionally, European and U.S. business cultures have been defined, in part, by how much influence outsiders wield over a company's operations. In the U.S., there is a strong shareholder ethic in which anyone, at least in theory, can gain influence by purchasing shares in a company. Moreover, because pension funds invest a large share of their money in stock and bond markets, even average Americans who do not own stocks directly, have a vested interest in the country's corporate health. And, companies usually raise capital through public measures, such as bond or stock issues , therefore there is in turn a sense of responsibility to the investing public. As a result, there has been a strong connection between the interests of U.S. business and the nation as a whole; and, the U.S. regulatory philosophy, though not always effective in practice, has developed along those lines.

***Irresponsible and Unethical Business Behavior***

The U.S. scandals of 2001 and 2002 were not enough to wake up European businesses; they too had to learn the hard way. Post-Parmalat, European government bodies realize they must move toward stronger enforcement mechanisms required by a more open, American style business economy. The European Commission is already working on a series of governance reforms inspired by the Parmalat scandal, and is moving closer to adopting the new universal accounting standards being devised by the International Accounting Standards Board (IASB) (King, 2004). The European Commission is using the U.S. 2002 Sarbanes Oxley Act as a yardstick as they attempt to thwart the accounting misdeeds that have recently plagued Europe. The Commission's financial reporting proposal requires companies to appoint audit committees that act independently from management. If the proposal passes EU law will require national regulators to impose criminal sanctions for serious offenses and require all EU member states to insist that stock exchange listed companies change their audit firms every seven years or replace their lead audit partner every five years.

## CONCLUSION

***Evaluating Business Ethics and implementing improvement programmes***

An experienced eye and ear will recognise the ethical stance of a business within a fairly short while from talking to directors and senior management, and this will be rounded out by discussions with a representative sample of staff, particularly those concerned with customers and personnel management. It will almost certainly be confirmed by a conversation with the Finance director and an appreciation of how the money matters are dealt with. Clearly it is necessary to deploy rather more than gut feel in examining a business's position in regard to business ethics and in the rest of this corporate governance best practice section and our corporate governance course you can find out how to install an

effective, ongoing assessment and monitoring programme which uses primary research, including market research, a key differentiator to other approaches. In our view it is the only way to pick up on questionable behaviour and so ensure good corporate governance. It is also offers a highly effective and detailed way of measuring the importance of business ethics to all within - and connected to - the organisation.

This is the first in our series on Best Corporate Governance Practice - the Golden Rules of corporate governance:

Rule1: The Importance of Business Ethics
Rule2: Towards a Common Goal - Align Business Goals
Rule3: The Importance of Strategic Management
Rule4: Organisational Effectiveness for Good Corporate Governance
Rule 5: The Importance of Corporate Communication

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